



The publication of the European Commission's consultation on electricity market design highlights the need to reflect on the design elements which should be considered to achieve a market that guarantees compliance with the 2050 decarbonization targets.

The European Commission has released a consultation which will establish the basis of a legislative proposal. It contains a series of proposals, including the promotion of long-term contracts (PPAs¹ and CfDs²) as tools to reduce consumers' bills. Among others, it proposes measures aimed at facilitating PPA contracts, schemes in which it is the regulator who makes such contracts (CfDs) with the new infra-marginal generation on a voluntary basis, and it even contemplates the possibility of imposing them on the existing generation.

An electricity market model based on centralized purchases of most of the infra-marginal energy (renewables, nuclear and hydro) with fixed price energy contracts, which could be imposed by Member States unilaterally, could affect the market and commercialization activities, fragmenting the internal market and discouraging the development of the flexibility in the system.

The reform of the electricity market must preserve legal certainties for investors and consumers without enabling retroactive changes that alter the already-agreed economic flows or the existing legal framework, so as to preserve a climate of confidence in the financial markets.

A market reform should include a Transition Plan from the current model to the agreed one, establishing the phases and timing for the implementation of the changes agreed on. For some measures, a testing process with sandboxes may be necessary to simulate the effects, detect failures and gain stakeholders' confidence in the proposed changes to the current model.

Here are some elements that should serve as guidelines:

1. Promote the deployment of the renewable generation:

- **Ensuring all agents can choose freely and without limitations or obligations between investing under CfDs support schemes or selling energy to the market, including sales in wholesale markets, to suppliers or directly to customers (PPA).** The new model's success will depend on providing attractive environments for investors by making all the possibilities of operating in the market coexist. Each country has its own trajectory and approach, and the various tools have been penetrating differently in each one.

¹PPAs: Long-term power purchase agreements, usually between renewable producers and large consumers.

² CfDs: For the purposes of this note, contracts for difference in which it is the regulator who enters into a long-term fixed-price contract.

- **Recognizing that PPAs efficiently incentivize investment in renewables, while allowing consumers to reduce the volatility of electricity prices, and that it is, therefore, necessary to promote their development by eliminating existing barriers. To this end, we proposed:**
 - Encourage aggregation and pooling mechanisms for buyers and sellers in line with the regulation on electro-intensive consumers.
 - Consider facilitating the demand to establish long-term hedges, as well as schemes that provide support for hedging risks in order to finance guarantees.
- **Keeping mechanisms, such as the CfDs, that have proven to be effective in a) promoting investment, b) ensuring that States meet energy and climate targets and c), developing technologies that are not yet mature.**
 - CfDs should be allocated to generators through competitive mechanisms and designed to minimize distortions. Their design may incorporate elements to increase the liquidity on forward markets.
 - CfDs must be voluntary for both generation and demand. Otherwise, an allocation of the costs or payments created by CfDs to all demand may distort the market, the PPA deployment and the trading activity.
- 2. **Keeping short-term markets, based on marginal pricing, as an instrument to guarantee the optimization of generation dispatch and cross-border energy flows, and complete the regulatory development necessary for storage participation and efficient demand management.**
- 3. **Non penalizing supplier activity, avoiding that market interventions reduce liquidity, that the distortion of price signals ends up affecting the competitiveness of suppliers and that the configuration of excessively burdensome operation guarantees in the market becomes a barrier.**
- 4. **Encourage forward energy contracting, eliminating existing barriers to its deployment.**
 - Organized markets and bilateral contracting allow generators and consumers to obtain stable cash flows in the contracting horizons that they decide. Mechanisms that allow all suppliers to access the energy under market conditions should be promoted.
 - Eliminating barriers to its development, such as those derived from limitations on the duration of contracts in the case of certain consumers (residential and SMEs in the case of Spain), excessive regulation or lack of regulatory stability.
 - Making the collateral regime for operating in the market more flexible so that it does not become a barrier to market operations.
 - The creation of a state or European clearing house to make this type of contract affordable, so that it becomes accessible to a larger number of players and allows sellers and buyers to compete on equal terms.
 - Renewable capacity auctions would allow for greater competition if part of this capacity were made available directly to demand as demand takers.
 - Long-term contracts should remain voluntary for market participants, respecting European commercial law and therefore without generating limitations to the free internal electricity market.
- 5. **Maintaining security of supply through capacity markets to ensure a robust and flexible system.**

- **Capacity markets need to be an integral part of the market design, providing efficient compensation for the firmness and flexibility needed to ensure faster and more accelerated deployment of renewables.** Incentives to achieve the necessary investment in generation, storage and demand-side management resources³ will at the same time provide a greater security of supply.
- **Capacity markets should be designed under the principle of technological neutrality.** Therefore, they should include an emissions threshold, remunerate all capacity according to its firmness, be harmonized at the European level, and no longer be considered as temporary solutions.

6. Provide flexibility to the electricity market.

- Facilitate access to flexibility markets for all resources in the system, encourage distributed resource aggregation models, simplify enabling processes and eliminate barriers to entry (e.g., minimum size regulatory zone)
- Incentivize investment in resources that provide flexibility to the electricity system, develop local markets and creation of a primary ancillary service market.

7. Promote electrification and new business models associated with the energy transition.

In order to efficiently incentivize new business models, such as renewable hydrogen, demand response or battery investment by the consumer, **it is necessary that the consumer can be exposed to the marginal price of electricity.** In order to keep coherence in the energy transition, the market design should not negatively affect an energy vector that is necessary to advance the transition.

It is necessary that this demand modulates its consumption in accordance with the marginal price of electricity. On the other hand, if all consumers were subject to the CfDs, their price curve would be artificially flattened, and investment in options that provide manageability to the system would be discouraged.

Demand participation in balancing services should be maximized.

8. System adequacy should be assessed periodically.

In order to provide visibility to market participants and network operators, it is proposed to carry out periodic assessments to analyze:

- The needs in terms of firmness and flexibility to ensure the power system security of supply.
- The progress of electrification, renewable development, and the evolution of demand.
- The pathway to achieve net zero emissions (potentially longer term than the current 10-year plans) incorporating a cross-sectoral perspective, including the development of new energy carriers, such as renewable hydrogen.
- Re-evaluation of the development needs of the transmission and distribution networks with a maximum periodicity of 2 years.

9. Consolidating the Internal Energy Market.

³As ENTSOE's "European Resource Adequacy Assessment Report 2022" points out, interventions are needed to ensure supply, especially in Central European countries, but in a generalized manner throughout Europe. Specifically for Spain, ENTSOE forecasts that Loss of Load Expectation levels of 6.7 hours/year will be reached, more than double the value considered acceptable (3 hours/year), if the current situation without a capacity market is maintained.

- The European market is based on market rules and free competition in investment and energy trade, which is allowing investment in clean energy and greater efficiency in supply.
- Consumers must continue to benefit from an internal energy market that guarantees competitive electricity prices. To this end, the progressive reduction of the spectrum of customers entitled to regulated tariffs should be implemented.
- Any emergency regulation of the market must be truly exceptional and not applied for a prolonged period of time. Investment requires regulatory stability.
- To maintain the internal market, the EU should strive to implement homogeneously both the market design and the possible exceptional measures. At MS level, disparate applications should be avoided, to not alter the unity of the single European market.

