European Commission Spells Out Conditions for Public Support to the Energy Sector

2014-01-08

The European Commission has for the first time prepared detailed rules for public support that EU Member States may grant to the energy sector. The proposed new energy rules focus on renewables support, energy infrastructure, generation adequacy and energy-intensive industries. Stakeholders have until February 14, 2014 to comment on a draft of these rules, which the Commission plans to put into force before July 1, 2014.

On December 18, 2013, the Commission published draft “Guidelines on environmental and energy aid for 2014”, asking stakeholders for their comments by February 14, 2014 (See Commission Press Release IP/13/1282 of December 18, 2013). The guidelines spell out the conditions under which public support measures that meet all criteria of State aid under Article 107(1) of the Treaty on the Functioning of the European Union (TFEU) can be declared compatible with the EU (“Union”) market under Article 107(3) TFEU. The Commission plans to finalize and adopt the guidelines before July 1, 2014. The new guidelines will replace the current “Community guidelines on State aid for environmental protection” of 2008.

The most important proposed change in the guidelines is the **extension of their scope beyond the environmental field into the energy area**. Already the existing environmental guidelines apply to some energy measures, but only to the extent that they serve environmental protection and climate objectives. In contrast, the new proposed guidelines contain comprehensive energy-related rules, which focus on renewables, energy infrastructure, generation adequacy and energy-intensive industries.

Renewables Support

The Commission intends to **facilitate the decarbonization of energy supply** and the integration of the EU internal energy market (but has, in response to opposition from Member States based on previous consultation documents, excluded nuclear energy from the scope of the guidelines and toned down the overall notion of technology neutrality).

- The Commission considers that the **existing EU legislative acts** supporting the Union’s climate change and energy sustainability targets set in the Europe 2020 strategy (e.g., the EU Emission Trading Scheme, the Renewable Energy Directive and the Fuel Quality Directive) **do not (yet) fully internalize the costs of environmental pollution**, so that a residual market failure remains, which State aid for renewable energy can address. The Commission is prepared to authorize aid schemes for renewable energy for a maximum duration of 10 years.

- With an increasing penetration and decreasing costs of renewable energy, the Commission
considers that **State aid should move away from feed-in tariffs and towards a more market- friendly support of renewable energy**, namely either in the form of market premiums (providing producers with a supplement on top of the wholesale price) or in the form of schemes involving certificates that are tradable between producers and suppliers of renewable energy.
- According to the Commission, **investment aid** for the promotion of energy from renewable sources should be allowed to cover up to 45% (55% for medium-sized enterprises, 65% for small enterprises, plus 5–15 percentage points in underdeveloped regions) of eligible costs for new installations.1 If the aid is a fixed amount that is distributed to beneficiaries based on their initial bids in a genuinely competitive bidding process on the basis of clear, transparent and non-discriminatory criteria, then the aid amount may reach 100% of eligible costs.
- Regarding **aid covering operating costs** for the promotion of energy from renewable sources (other than biomass, for which special rules exist), the Commission prefers feed-in premiums (or equivalent measures involving the direct marketing of produced electricity) and tradable green certificates over feed-in tariffs, which may be granted only to small installations with a generation capacity below [1]2 MW—except for wind energy, where a threshold of [5 MW or 3 generation units] applies.

As regards **permissible aid amounts**, the Commission distinguishes between deployed technologies (which it proposes to define as technologies having a share of more than [1-3]% in electricity production at EU level) and other, less deployed technologies.

- For **deployed technologies**, the Commission requires:

  - in case of feed-in premiums, that aid is limited by way of a genuinely competitive bidding process on the basis of clear, transparent and non-discriminatory criteria;
  - in case of green certificates, that the scheme in the aggregate does not result in overcompensation over time and across technologies or for individual technologies; and
  - that the aid is technology neutral (i.e., all generators producing electricity from renewable energy sources must be able to participate in the bidding process for the feed-in premiums or receive aid in the form of green certificates, respectively). If needed for an energy mix, Member States may require a minimum number of different

renewable energy sources but may not pre-define the technologies.

- In contrast, for **less deployed technologies**, the Commission only requires:

  - in case of feed-in premiums, that the aid per unit of energy does not exceed the difference between the (regularly updated) total levelized costs of producing energy from the particular technology in question and the market price of the form of energy concerned; and
  - in case of green certificates, that for each differentiated level of support that may be applied, the scheme does not in the aggregate result in overcompensation.

– Further rules include:

- Any investment aid previously received must be deducted from the operating aid.
- Feed-in premiums are only granted until the plant has been fully depreciated according to normal accounting rules.
- Green certificates must be designed so as not to dissuade renewable energy producers from becoming more competitive.
- To the extent the produced energy is electricity, aid beneficiaries are subject to standard balancing responsibilities where competitive intra-day balancing markets exist.

Energy Infrastructure

The Commission recalls that it has estimated **total investment needs in energy infrastructures of European importance up to 2020 at about EUR 200 billion**. The Commission acknowledges that in the area of energy infrastructure, market failures may arise in particular because of problems of coordination and asymmetric information, and that not all of these market failures can be solved by tariff and access and unbundling regulation.

The Commission therefore considers with regard to all investments in trans-European energy infrastructure projects (as defined based on Regulation 347/2013, i.e., in particular (smart) grid interconnection between Member States) and in energy infrastructure in underdeveloped regions, the market failures are so significant that State aid may be granted. The aid may cover up to 100% of the funding gap, i.e., of the portion of the discounted cost of the initial investment not covered by the discounted net revenues of the project. For other projects, the Commission will assess on a case by case basis whether State aid is necessary.

Generation Adequacy

The Commission recognizes that the recent move in many Member States from fewer, more stable and more continuous towards more but **smaller and less stable electricity sources raises challenges for ensuring generation adequacy** and that market and regulatory failures may cause insufficient investment in generation capacity. However, the Commission also points out that granting energy generators support for the mere availability of generation capacity may contradict the objective of phasing out environmentally harmful subsidies notably for fossil fuels.

Thus, the Commission considers State aid for promoting generation adequacy to be permissible only if additional energy infrastructure or alternative measures—such as a more responsive demand side management or increasing interconnection capacity or electricity storage—have been demonstrated to be unable to address the concerns. In addition, the Commission imposes various conditions to avoid that such aid unduly favors national generation or particular technologies, in order to limit the risks of strong distortions of competition and environmental harm. For example, the amount of aid must be limited by providing only for reasonable rates of return, which can be achieved for example by awarding the aid in a genuinely competitive bidding process on the basis of clear, transparent and nondiscriminatory criteria.

Energy-Intensive Industries

The Commission points out that in recent years, the financing of renewable support measures through surcharges and other instruments has led in many Member States to an increase of electricity costs which affects the competitiveness of energy-intensive users and risks leading to carbon leakage due to the relocation of production outside the EU. The Commission therefore proposes to **allow the burden on energy-intensive users to be reduced, while putting in place safeguards to limit the distortions of competition that such selective support is bound to trigger and to avoid subsidy races between Member States**.

Specifically, the Commission proposes the following conditions for such reductions of the burdens on energy-intensive users:

- In parallel to exemptions from the EU Emission Trading Scheme, the reduction should be limited to sectors that have an **intensity of trade with third countries above [10]%** and in which the costs of funding renewable energy support leads to an **increase in production costs of at least [5]% of total gross value added**, because only such sectors are actually exposed to a significant risk of carbon leakage.
- The reduction must be paid as a lump sum and must be limited to [85]% of the regular burden until the end of [2017] and to [80]% thereafter.
- The beneficiaries of the reduction must be chosen on the basis of objective and transparent criteria, and the reduction must not discriminate between competitors in the same sector or relevant market.

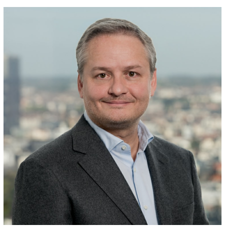
One of the first measures to which the Commission will likely apply these new guidelines will be the reduction of the renewables surcharge that Germany grants to energy-intensive companies under its Renewable Energy Act (EEG) as amended in 2012. The Commission opened an in-depth State aid investigation into the EEG on the same day on which it published the new draft guidelines (cf. Commission Press Release IP/13/1283 of December 18, 2013). Judging from the press release, the Commission apparently takes the preliminary position that not only the reduction of the renewables surcharge but also the entire EEG surcharge mechanism involves State aid in the meaning of Article 107(1) TFEU.

---

[1] Eligible costs are only the costs necessary to achieve the increased level of environmental protection, which are identified by reference to a similar, less environmentally friendly investment that would have been credibly carried out without the aid.

[2] Amounts in square brackets are indicative proposals in the draft guidelines, on which the Commission invites comments from stakeholders.

Authors



Frédéric Louis

PARTNER

frederic.louis@wilmerhale.com

+32 2 285 49 53

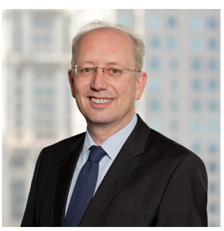
Prof. Dr. Hans-Georg Kamann

PARTNER

Vice Chair, Antitrust and Competition Practice

hans-georg.kamann@wilmerhale.com

+49 69 27 10 78 204



Ulrich Quack

PARTNER

ulrich.quack@wilmerhale.com

+49 30 20 22 63 25

Dr. Stefan Ohlhoff LLM

PARTNER

stefan.ohlhoff@wilmerhale.com

+49 30 20 22 63 55

Dr. Oliver Fleischmann, LL.M.

SPECIAL COUNSEL

oliver.fleischmann@wilmerhale.com

+49 30 20 22 64 26