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# Internal market for electricity

On 30 November 2016, the European Commission presented a legislative proposal for a regulation on the internal market for electricity, as part of a comprehensive legislative package on the energy union. The proposed regulation is aimed at making the electricity market fit for more flexibility, decarbonisation and innovation, by providing for undistorted market signals. It sets out rules for electricity trading within different time frames and clarifies the responsibilities of the market actors. It defines principles for assessing capacity needs at regional and European level and proposes design principles for market-based capacity mechanisms with cross-border participation. It introduces regional operational centres for handling-system operation and a European entity for distribution system operators.

The proposal has been referred to the Committee on Industry, Research and Energy (ITRE).

#### Proposal for a Regulation of the European Parliament and of the Council on the internal market for electricity (recast)

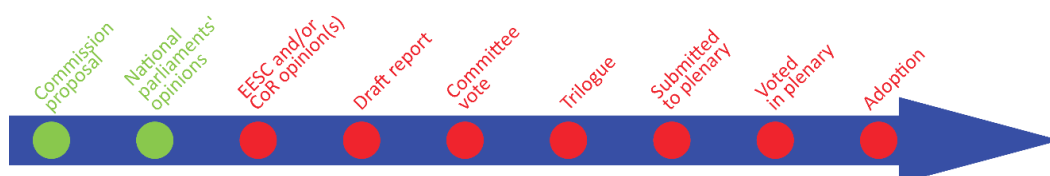
COM(2016) 861, 30.11.2016, 2016/0379 (COD), Ordinary legislative procedure (COD) (Parliament and Council on equal footing – formerly 'co-decision')

Committee responsible: Industry, Research and Energy (ITRE)

Rapporteur: Krišjānis Kariņš (EPP, Latvia)

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Kaja Kallas (ALDE, Estonia)  
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Next steps expected: Initial discussions in committee



9 March 2017

First edition

The 'EU Legislation in Progress' briefings are updated at key stages throughout the legislative procedure.

Please note this document has been designed for on-line viewing.

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## Introduction

Electricity markets<sup>1</sup> in the EU are faced with serious challenges, such as the transition towards a low-carbon energy system, the cost-efficient integration of variable renewable energy sources, the trend towards decentralised renewable energy production, the evolving role and stronger participation of energy customers (both households and industrial customers) and the requirement to ensure the security of supply in the short and long term efficiently and at affordable costs.

In order to stimulate competition and reward innovation in services, products and technologies, electricity markets should be open to new participants. Moreover, they should provide the right signals to investors in order to ensure that the necessary long-term investments will be made in the most cost-effective way. Concerns about a lack of investment in electricity generation capacity to meet peak demand have prompted several Member States to introduce capacity payments.

In order to address the challenges in the electricity market, the European Commission presented a [legislative package](#) on 30 November 2016. It consists of a communication entitled 'Clean Energy for all Europeans', eight legislative proposals and a number of reports and communications. With respect to the electricity market, the package comprises five legislative proposals and three reports.<sup>2</sup>The bundling of these legislative proposals into a single package aims to ensure their mutual coherence.

The proposed internal electricity market regulation ([COM\(2016\) 861](#)), which is a part of the legislative package, is aimed at making the electricity market fit for more flexibility, decarbonisation and innovation by providing for undistorted market signals. It sets out rules for balancing markets, day-ahead and intraday markets; sets out a process for defining regional electricity markets (bidding zones); updates rules on network access charges; and sets out design principles for national capacity mechanisms, which may only be used if the European resource adequacy assessment has identified a concern. The proposal clarifies the responsibilities of the market participants, introduces regional operational centres that would ensure the reliable and efficient operation of cross-border grids, and establishes a new European entity for distribution system operators that would participate in grid planning and the development of rules for the electricity grid (network codes). The procedure for developing network codes is streamlined.

## Existing situation

Today's liberalised internal energy market for gas and electricity, established to encourage competition on wholesale and retail markets, came into existence by means of three consecutive legislative packages, adopted in the 1990s, and then in 2003 and 2009. For the electricity market, these are [Directive 96/92/EC](#) on the common rules for the internal electricity market, [Directive 2003/54/EC](#), enabling new electricity

1 The EPRS briefing [Understanding electricity markets in the EU](#) provides an introduction to EU electricity markets.

2 Proposal for a directive on common rules for the internal electricity market ([COM\(2016\) 864](#)), proposal for a regulation on the internal electricity market ([COM\(2016\) 861](#)), proposal for a revised regulation on the European Agency for the Cooperation of Energy Regulators ([COM\(2016\) 863](#)), proposal for a new regulation on risk preparedness in the electricity sector ([COM\(2016\) 862](#)), proposal for a revised Renewable Energy Directive ([COM\(2016\) 767](#)), evaluation of the electricity market design and security of supply ([SWD\(2016\) 413](#)), report on sector inquiry on capacity mechanisms ([COM\(2016\) 752](#)), and report on energy prices and costs in Europe ([COM\(2016\) 769](#)).



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suppliers to enter Member States' markets and allowing customers to choose their electricity supplier, and [Directive 2009/72/EC](#), which further liberalised the market by unbundling supply, generation and networks, providing market access to third parties, and increasing the transparency of retail markets. Other aspects include the Member States' obligation to ensure the provision of a universal service to all households and mechanisms for regulatory oversight, in particular through cooperation amongst energy regulators and the establishment of an Agency for the Cooperation of Energy Regulators (ACER) through [Regulation \(EC\) No 713/2009](#). ACER started work in March 2011 and is mainly responsible for promoting cooperation between national regulatory authorities, monitoring progress in the implementation of the 10-year network development plans and monitoring the internal markets in electricity and gas.

Furthermore, [Regulation \(EC\) No 714/2009](#) on conditions for access to the network for cross-border exchanges in electricity established a European network of transmission system operators for electricity (ENTSO-E).<sup>3</sup> Its tasks include elaborating rules (network codes) for the operation of the electricity transmission network and coordinating grid operation through the exchange of operational information and the development of common safety and emergency standards and procedures. ENTSO-E is also responsible for drafting a 10-year network development plan every two years, which is then reviewed by ACER. The rules for the EU electricity market were further elaborated in [Commission Regulation \(EU\) 2015/1222](#) establishing a guideline on capacity allocation and congestion management and [Commission Regulation \(EU\) 2016/1719](#) establishing a guideline on forward capacity allocation.

The EU internal energy market is still facing some obstacles, notably persistent barriers to cross-border trade, insufficient competition in retail markets and weaknesses in consumer protection, as noted in the European Commission's [evaluation](#) of the EU's regulatory framework for electricity market design and consumer protection and a recent EPRS [implementation appraisal](#). According to the European Parliament's third [Cost of non-Europe report](#), a more physically integrated internal energy market could deliver annual efficiency gains of at least €250 billion.

[Directive 2009/28/EC](#) (the Renewable Energy Directive) obliges Member States to open their power grids to energy from renewable sources, including priority grid access (priority dispatch). Other [electricity-related EU legislation](#) concerns the security of electricity supply, trans-European networks and the EU emissions trading system (emission allowances for fossil-fuel-fired power plants). EU competition policy (state aid rules in particular) and tax policies are other important policy areas.

## European Parliament's starting position

In its [resolution of 13 September 2016](#) on moving towards a new energy market design, the Parliament notes that the task of integrating a growing share of renewables and prosumers (active energy consumers that both consume and produce electricity) into the electricity markets, but also of encouraging demand response and storage, requires a combination of liquid short-term markets and long-term price signals. It calls for time-varying prices that reflect the scarcity of supply and provide incentives for storage and demand response, complemented by instruments aimed at mitigating revenue risk over 20-30 years and by a regulatory framework for prosumers focussed on self-production and local energy storage.

<sup>3</sup> The European network of gas transmissions system operators (ENTSO-G) was established by [Regulation \(EC\) No 715/2009](#).



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The new market design should provide technical and market conditions for energy storage, including the introduction of smart grids and smart meters. Renewables should be integrated into the market and participate in balancing services, while support for mature renewables should be phased out. Market-based cross-border capacity mechanisms should only be allowed under certain conditions. The resolution emphasises the importance of regional cooperation and calls for ACER to be given additional competences.

Parliament's [resolution of 26 May 2016](#) on delivering a new deal for energy customers calls for empowering citizens (individually or collectively) to produce, consume, store or trade their own renewable energy, to actively engage in the energy market through customer choice, and to participate in demand response. It calls for addressing the causes of energy poverty, protecting customers from unfair practices, and providing clear information to customers.

In recent years, Parliament has adopted several resolutions related to energy markets: on [making the internal energy market work](#) (10 September 2013), on the [energy union](#), on [interconnection targets](#) (15 December 2015), and on the [renewable energy](#) progress report (23 June 2016). To some extent all have addressed issues relating to electricity market design.

## Council and European Council starting positions

The [conclusions](#) of the March 2015 European Council on the energy union call for a more effective, flexible market design in combination with enhanced regional cooperation that should help integrate renewables and provide affordable energy to households and industry while retaining the right of Member States to decide on their own energy mix. Public interventions should be compatible with the internal market.

The [messages from the Council presidency](#) on electricity market design and regional cooperation of 19 May 2016 conclude that measures are needed to improve market functioning and remove barriers to flexibility. It highlights regional cooperation, based on a bottom-up approach, as an important step towards a more integrated, effective and flexible internal market. It calls for more interconnections and sufficient transmission capacity within and across borders. In the June 2016 Transport, Telecommunications and Energy Council [meeting](#), most Member States welcomed the presidency messages.



## Proposal

### Preparation of the proposal

After [evaluating](#) the performance of the current legislation (third energy package), the Commission concluded that, overall, it has increased competition within and across borders and strengthened customers' position. However, they found that barriers to cross-border trade persist and interconnector capacities are under-utilised. With respect to retail markets, they concluded that competition could be improved significantly.

The Commission ran three public consultations. The first (November 2012 – February 2013) concerned resource adequacy and security of supply. It was followed by consultations on retail electricity markets and end-customers (January – April 2014) and on electricity market design (July – October 2015). A total of 705 responses arrived.

Due to the inter-relations between the different proposals in the legislative package, the Commission produced a single [impact assessment](#) for four legislative proposals.<sup>4</sup> It is based on almost 30 studies and modelling tools, prepared mostly by external experts. The impact assessment compared a number of policy options for adapting the market design to an increasing share of renewables and to technological developments, for addressing investment in generation capacity, and for improving competition and services in retail markets. According to the impact assessment, the proposed legislation would establish a level playing field for different supply and demand-side resources, result in more competition and lower prices, more reliable electricity systems at a lower cost, and more efficient operation of the transmission and distribution systems. It expects indirect environmental benefits through the improved integration of renewables, and positive effects on health and well-being through the proposed measures on energy poverty.

### The changes the proposal would bring

The proposed regulation, which recasts<sup>5</sup> Regulation (EC) No 714/2009, is focused on the functioning of the EU electricity market. It would apply from 1 January 2020.

#### Objective and main principles

In addition to the existing objectives regarding the functioning of the market and cross-border trading, the proposal introduces the objective of enabling market signals for increased flexibility, decarbonisation and innovation, in support of the energy union objectives and the EU 2030 climate and energy targets. The proposed regulation is aimed at setting 'principles for well-functioning, integrated electricity markets, which allow non-discriminatory market access for all resource providers and electricity customers, empower

4 The impact assessment covers the proposals COM(2016) 864; COM(2016) 861; COM(2016) 863, and COM(2016) 862.

5 [Recasting](#) brings a legislative act and all the amendments made to it together in a single new act. The new legislative act passes through the full legislative process and repeals all the acts being recast.



consumers, enable demand response and energy efficiency, facilitate aggregation of distributed demand and supply, and contribute to the decarbonisation of the economy by enabling market integration and market-based remuneration of electricity generated from renewable sources.' The proposal emphasises the principle of market-based prices by generally excluding any maximum limit on wholesale electricity prices. It sets out the following principles:

- > Customers should benefit from market opportunities and increased competition on retail markets, while aggregation of generation and demand should enable consumers and small businesses to participate in the market.
- > Market rules should enable the integration of electricity from renewable sources, and incentivise energy efficiency and investment on generation, storage, energy efficiency and demand response. Actions which hinder the development of more flexible generation, low carbon generation or more flexible demand, should be avoided.
- > There should be no barriers to cross-border electricity flows and cross-border transactions.
- > All generation, storage and demand resources should participate in the market on an equal footing, and all producers be responsible for selling the electricity they generate.

Moreover, market rules should encourage effective regional cooperation, allow for progress in research and development, enable the efficient dispatch of generation and demand response<sup>6</sup> and allow for entry and exit of electricity generators and suppliers. Long-term hedging opportunities should be tradable on exchanges.

### Balancing, day-ahead and intraday markets

All market participants should aim towards balancing of supply and demand in the grid, and would be financially responsible for any imbalances they cause, with possible national exceptions under clearly defined conditions. The proposal sets out rules for the balancing markets, to which all market participants would have access. It further sets out rules for integrated 'day-ahead' and 'intraday' markets, which would be jointly managed by transmission system operators (TSO) and nominated electricity market operators (NEMO).<sup>7</sup> Trading in these markets would be as close to real time as possible, and market operators would be free to develop products and trading opportunities.

### Dispatch and curtailment

Dispatching<sup>8</sup> would generally be market-based. Priority dispatch for renewables and high-efficiency cogeneration, which were introduced by the Renewable Energy Directive (2009/28/EC) and the Energy Efficiency Directive (2012/27/EU), respectively, would be limited to small installations (with capacities

6 Demand response' means the adaptation of electricity demand to scarcity in supply in response to market signals.

7 Market operator designated by the competent authority to perform tasks related to day-ahead or intraday coupling.

8 Dispatch' means the activation of an electric generator to meet demand, generally selected to minimise overall costs. 'Redispatch' is a deviation from the normal dispatching rules to accommodate constraints in the transmission network. 'Curtailment' is the shutdown of an electricity generator in case of excess electricity supply.



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below 500 kW and below 250 kW from 2026), demonstration projects and existing installations that already benefit from priority dispatch. The rules for curtailment and redispatch should be based on objective, transparent and non-discriminatory criteria. Transmission system operators (TSOs) and distribution system operators (DSOs) would have to make sure that the grid can transmit energy from renewables or high-efficiency cogeneration with minimum possible curtailment or redispatching. Self-generated electricity would not be curtailed except in emergencies.

### Regional electricity markets

The proposal sets out a process for defining bidding zones<sup>9</sup> in such a way that economic efficiency and cross-border trading opportunities are maximised and security of supply is maintained, in line with the review process created in [Commission Regulation \(EU\) 2015/1222](#) establishing a guideline on capacity calculation and congestion management. It sets out rules for the allocation of transmission capacity and contains rules to prevent national limitations on cross-border electricity flows.

### Network charges and congestion income

The rules on network access charges are updated to rule out discrimination and disincentives against energy storage and demand response. Tariffs should incentivise TSOs and DSOs to increase efficiencies, foster market integration and security of supply and support investments. The rules for the use of congestion rents<sup>10</sup> are amended.

### Resource adequacy assessment and capacity mechanisms

The proposal updates the rules for European resource adequacy assessments<sup>11</sup> and sets out design principles for national capacity mechanisms,<sup>12</sup> which may only be applied if the European resource adequacy assessment has identified a concern, and the Member State has a reliability standard indicating its desired level of security of supply. Capacity mechanisms should be open to participation of capacity providers from other Member States, provided that there is a network connection. Member States would have to consult with neighbouring Member States before introducing a capacity mechanism. Power plants constructed after the entry into force of the proposed regulation may only participate in capacity mechanisms if they emit less than 550 g of CO<sub>2</sub> per kWh. For pre-existing power plants, the emissions limit will be applied five years later. Existing capacity mechanisms would have to be adapted to the new rules.

9 'Bidding zone' means the largest geographical area within which market participants are able to exchange energy without capacity allocation (allocation of transmission capacity).

10 Congestion rent' is the payment collected by the owners of the rights to a transmission line, whose amount is typically equal to the line's capacity times the difference between the prices at the two ends of the line.

11 Resource adequacy' is the ability to meet electricity demand with adequate generation resources.

12 Capacity mechanisms' are measures taken by Member States to ensure that electricity supply can match demand in the medium and long term. The European Commission's [sector inquiry on capacity mechanisms](#) analyses capacity mechanisms in the EU and offers conclusions about the design principles to ensure their effectiveness.



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## Transmission system operators and regional operational centres

The proposed regulation sets out the tasks and responsibilities of ENTSO-E and emphasises its duty to act independently and for the European good, while also elaborating the monitoring tasks of ACER in this regard. Furthermore, the proposal lays down rules on the connection of cogeneration units; such rules were previously included in the Energy Efficiency Directive.

The proposal introduces regional operational centres (ROCs), which would have to be established by TSOs. ROCs would complement the role of TSOs by ensuring the efficient and reliable operation of interconnected transmission systems. A full list of their functions is provided in [Annex I](#). The proposal provides criteria for defining the system operation regions covered by each ROC and sets out the organisational and working arrangements.

## New entity for distribution system operators

The proposed regulation defines a procedure for establishing a new European entity for DSOs, defines its tasks (including a role in the development of network codes) and specifies how DSOs and TSOs should cooperate with regard to the planning and operation of their networks.

## Network codes and guidelines

The proposed regulation confirms pre-existing powers and rules for the Commission to adopt delegated acts in the form of network codes or guidelines. It clarifies the legal nature and adoption of network codes and guidelines, and extends their possible contents to distribution tariff structures; rules for the provision of non-frequency ancillary services; demand response, energy storage and demand curtailment; cybersecurity; ROCs; and the curtailment of generation and redispatch of generation and demand. It simplifies and streamlines the procedure for the development of network codes, and empowers national regulators within ACER to take decisions regarding the implementation of network codes and guidelines. It involves the European entity for DSOs and other stakeholders more closely in the development of network codes.



[Advisory committees](#)[National parliaments](#)[Stakeholders' views](#)

## Views

### Advisory committees

The European Economic and Social Committee (EESC) and the Committee of the Regions (CoR) have been consulted on the proposal and may give their opinions.

In January 2016, the EESC adopted an [opinion](#) on energy market design that called for a careful balance between the market and regulation, as well as for new approaches to pricing that reflect the true overall cost, including negative external effects. It emphasises the importance of ensuring the active involvement of consumers in production and local and regional marketing and envisages a decentralised grid made up of interconnected 'production and supply islands'.

### National parliaments

The proposal has been passed to the national parliaments. The [deadline](#) for the submission of reasoned opinions on the grounds of subsidiarity passed on 27 January 2017 with none being submitted.

### Stakeholders' views<sup>13</sup>

[Eurelectric](#), representing the European electricity industry, generally welcomes the Commission's proposal, but regrets that policy support costs, which increase customers' electricity bills, are not addressed. [European energy regulators](#) also welcomed the proposals, which they consider well aligned with the regulators' position. [ENTSO-E](#) is critical of the proposed ROCs, which it considers unnecessary because their function is already being performed by the existing regional security coordinators. ENTSO-E is concerned that the proposed set-up would result in lower security of supply and a less clear liability. ENTSO-E considers the proposed role of ACER in developing network codes as a 'counter-productive, unnecessary and additional layer of administration'.

[Greenpeace](#) criticises capacity mechanisms as a subsidy to fossil-fuel power plants and warns that the abolishment of the priority dispatch puts new investments in renewable energy sources at risk. [Climate Action Network](#) (CAN) Europe considers that the proposed legislation undermines market access for renewable energies, and that capacity mechanisms could be used to subsidise old coal-fired power plants.

<sup>13</sup> This section aims to provide a flavour of the debate and is not intended to be an exhaustive account of all different views on the proposal. Additional information can be found in related publications listed under 'EP supporting analyses'.



## Legislative process

The proposal has been referred to the European Parliament's Committee on Industry, Research and Energy (ITRE). Other Parliament committees – on Budgets (BUDG), Economic and Monetary Affairs (ECON), Environment, Public Health and Food Safety (ENVI) and Internal Market and Consumer Protection (IMCO) – have been invited to give their opinions, while the Legal Affairs Committee (JURI) has been invited to give its opinion on the recast technique.



## References

### EP supporting analyses

[Energy Union: key decisions for the realisation of a fully integrated energy market](#), European Parliament, DG IPOL, April 2016.

[Understanding electricity markets in the EU](#), EPRS, November 2016.

[Electricity 'Prosumers'](#), EPRS, November 2016.

[Overview of the internal energy market design legislation](#), EPRS Implementation Appraisal, January 2017.

### Other sources

[Internal market for electricity. Recast](#) / European Parliament, Legislative Observatory (OEL).

[Re-powering markets: Market design and regulation during the transition to low-carbon power systems](#), International Energy Agency, February 2016.

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