PROPOSAL TO SHIFT REMUNERATION OF NEW AND EXISTING LOW-CARBON TECHNOLOGIES TO CONTRACTS FOR DIFFERENCE

Points of attention and concerns

Energinet

BACKGROUND INFORMATION FOR THE MEETING ON DECEMBER 1st 2022
One Side of the Market: Remunerating Renewables and other Technologies Based on Their True Production Costs

- Renewables and other types of inframarginal generators (e.g., nuclear) would be remunerated under contracts for difference, independently of the marginal price. The price of these contracts would typically be established by tendering and will be a direct function of the actual production costs of the relevant technologies.

- This shift to a remuneration based on contracts for difference can be implemented very swiftly and easily for new capacity entering the market. For existing generators, the current inframarginal cap could be directly integrated into the functioning of the wholesale market to facilitate its practical implementation and incentivise the transition of existing generators to a long-term pricing structure based on contracts for difference.
LONG-TERM NET EFFECT ON CONSUMER PRICES

Does shifting remuneration of new and existing renewables and low-carbon generation to two-sided CfDs solve the problem of excessive dependence of European electricity bills on highly volatile natural gas markets or does it simply postpone payments from now to later? Will we face the same pressure to intervene during year 3 or 4 when spot prices (expectedly) drop below the CfD strike price?
POINTS OF ATTENTION AND CONCERNS

Design of the CfDs (tender conditions)

- Duration of CfDs based on expected asset lifetime or should they be renegotiated once spot prices fall? How should one distinguish between new and existing assets when choosing the duration?

- Counterparty for the CfDs – who are the parties in these CfDs?
  - Default option: Member States and generators → What are the consequences for taxpayers of taking on this increased counterparty risk (which is out of their control)? Could market parties (BRPs and/or suppliers) be a party in these CfDs?

- How to apply caps for the payouts to generators and Member States (or other counterparty on behalf of consumers)?
  - Asymmetric (e.g., cap payouts from Member States but not from generators) or symmetric? What does this mean for generators’ risk premia?

Effects on financial (forward) markets and hedging options (liquidity loss)

- What is the impact on liquidity and hedging options in forward markets, if all existing and new generation are on a CfD-based fixed price contract?

Market impact on incentives for providing flexibility?

- How can the spot market ensure efficient dispatch and facilitate incentives for market participants to provide flexibility and act on price signals, if consumers and generators have hedged against price risk through CfD-based fixed price contracts and therefore have little or no incentive to behave flexibly when the system needs it?

Inftramarginal revenue cap as a permanent part of market design to incentivise shift to CfD based remuneration

- Will the design of the cap be the same as in the emergency council regulation (with high degree of national flexibility in implementation) or will it be harmonised at EU-level based on best practices from national implementations?