

Joint letter of the Baltic electricity market participants to the services of the EC Commission

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Director-General
DG Energy

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Carbon leakage in the Baltic electricity market

Dear Sirs,

We, the undersigned Baltic electricity market participants, would hereby like to inform you of the ongoing and deepening carbon leakage problem in the Baltic electricity market, which primarily for security of supply reasons have been neglected for years. As by now the connections of the Baltic electricity systems with the neighbouring systems (Finland, Sweden and Poland) have significantly been strengthened, then there is an urgent need for application of corrective policy measures for ensuring level playing field in the Baltic electricity market.

Last year about every fifth kilowatt hour of electricity which was consumed in the Baltic states was imported from the third countries (Russia and Belarus). This was about 67% more than a year earlier¹. First 4 months of the current year show that this increase of imports from third countries is about to continue² as it is supported by high price of CO₂ in the EU ETS. According to our estimation, the imports from the third countries pose a single largest distortion of the Baltic electricity market, which is caused by:

- 1) de facto absence of climate policy in Russia and Belarus, which provides at current CO₂ prices in the EU ETS a very large competitive advantage to third countries' generators;
- 2) absence of reciprocity in cross-border trading – Russian trader Inter RAO can enter the Baltic market freely but the markets of third countries are not accessible for Baltic market participants of EU origin;
- 3) Baltic TSOs are applying different congestion management method towards the third countries imports (no congestion rent is charged by Baltic TSOs on price difference between neighbouring markets); and
- 4) Russian generators can obtain natural gas for prices which are not accessible for Baltic generators of EU origin.

As a result, Russian trader Inter RAO earned about 166 million euros of windfall profit from the Baltic market last year, market share of local producers is continuing to decrease and there is very little activity in terms of development of new generation projects. Situation is especially grim in Lithuania which can currently cover only about 30% of its consumption by its own generation capacities but the situation is quickly deteriorating also in Estonia. At the same time Russia has constructed 4 new power plants (ca 1000 MW) in the Kaliningrad region, including new coal plant, with the primary objective to export power to the Baltic markets. Given the circumstances, current situation poses an act of carbon leakage in the power generation sector of the EU and thereby puts in danger market driven investments and generation in the Baltics. If given distortion is not swiftly resolved, it may trigger the need for market interventions so that the generation adequacy is ensured in the Baltic region.

¹ In 2018 imports increased (from 3,29 TWh) to 5,5 TWh. Given statistics is not covering third countries imports which are entering the Baltic states via Finland. Combined annual power consumption of the Baltic states is about 25 TWh.

² In comparison to first 4 months of the last year further increase of 92% was recorded.

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In its 28 February 2018 communication³, the EC Commission stated that *"the EU must take all necessary measures to safeguard and boost its own prospects for economic and social development as well as to address its own vulnerabilities emanating from climate change or from harmful unilateral policies by other global players"*. Moreover, the EC Commission also stated that *"proactive or corrective policies may be needed to ensure a fully competitive and level playing field in line with International obligations. Just as the EU remains open for climate-friendly investment and trade it should also defend its right to reciprocal, fair and transparently governed access to partner countries' markets, infrastructure and critical raw materials"*. Last but not least, in Article 3 of new Electricity Market Directive, it is stated that *"Member States shall ensure that market participants from third countries, when operating within the internal market for electricity, comply with applicable Union and national law, including that concerning environmental and safety policy"*.



Moreover, we were informed at the last Baltic Electricity Market Forum in Jurmala that the EC Commission shall represent the interests of the Baltic states at the negotiations with Russia regarding the terms of desynchronisation of the Baltic electricity systems from BRELL synchronous area. Therefore, we strongly insist that the EC Commission should refrain from concluding any agreements which enable continuation of currently happening carbon leakage and/or price distortion in the Baltic electricity market.

We are looking forward to your reply at your earliest convenience.

With best regards



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Bethers
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³ Baltic Energy Market Interconnection Plan foresees introduction of common trading principles towards non-EEA third countries by Estonia, Latvia, Lithuania and Finland

⁴ A clean planet for all – A European strategic long-term vision for a prosperous, modern, competitive and climate neutral economy. Brussels, 28.11.2018, COM (2018) 773 final