

IWEA Response to the DG Competition Draft Guidelines on Environment and Energy Aid for 2014-2020

14 February 2014

The Irish Wind Energy Association (IWEA) welcomes this opportunity to respond to the European Commission consultation on Environmental and Energy Aid Guidelines 2014-2020. IWEA is Ireland's leading renewable energy representative body representing more than 200 members involved in wind and renewable energy development in Ireland and Northern Ireland (through the Northern Ireland Renewables Industry Group (NIRIG), set up in collaboration with Renewable UK). IWEA represents members with projects across the spectrum, in operation, under construction and awaiting connection. In Ireland IWEA members are involved in the majority of connected projects but also involved in more than 85% of the MW of currently grid contracted projects.

Through NIRIG we represent more than 25 company members that have developed over 85% of renewable generation operational in Northern Ireland today and who will contribute a significant majority of renewable energy required to deliver the 2020 targets.

The IWEA membership base includes all large, medium and many small developers as well as financial, legal advisory, consultancy, contractors and other service providers involved in the renewables sector in Ireland and Northern Ireland.

1. Introduction

IWEA welcomes the review of the State Aid Guidelines for environmental protection as it provides an opportunity to provide additional clarity on the legal framework for wind energy support mechanisms. In the past, there have been significant delays in achieving State Aids approval for national support schemes, and IWEA believes that this review provides an opportunity to streamline the approval process and remove uncertainty through the provision of a clear set of guidelines. IWEA believes that the main aim of these guidelines should be to ensure that the objectives of State Aid are streamlined such that the support schemes do not inhibit trade between Member States. The guidelines should focus on these objectives rather than the actual mechanisms used.

Due to their binding nature and immediate applicability, State Aid Guidelines are one of the most potent regulatory instruments available to the European Commission to further the EU's energy policy objectives. The wind industry considers the on-going review as an opportunity to promote competition, the sector's competitiveness, and well-designed and stable support mechanisms for wind power thereby ensuring the cost-effective implementation of the 2020 renewable energy targets. However, under the current version, the Guidelines would fail to meet these objectives.

Their implementation would result in significant unnecessary reforms which would bring considerable uncertainty to the industry in the short to medium term.

The objective of the wind industry is to be competitive in a fair and fully liberalised electricity market, delivering the benefits of wind energy in the most affordable way. The industry would welcome progressive convergence based on common guidelines and benchmarks building on bottom-up regional integration. This is however not the approach taken by the Commission in the State Aid Modernisation process.

- Generally speaking, the Commission's approach in developing these Guidelines attributes market distortions almost exclusively to the regulatory frameworks for the promotion of renewables. This fails to acknowledge that power sources such as oil, gas, coal and nuclear were also developed, and continue to be supported, through State subsidies and levies on electricity bills. IWEA would welcome concrete steps towards realising the Commission's policy of phasing out subsidies to fossil fuels.
- While the convergence of methodologies for support across a liberalised European Market is to be welcomed, there should still be some flexibility to Member States to define their own support schemes, taking into account varying grid access costs, administrative costs, access to (and cost of) capital and national fiscal frameworks. Until the market is fully liberalised, there may be a need for different characteristics in individual Member States.
- The DG Competition proposal for State Aid Guidelines would overly restrict effective and efficient tools available to Member States to compensate market failures, resulting from the narrow definition of operating aid.

2. Feed in Tariffs

As stated above, IWEA believes that the Guidelines should focus on the objectives of State Aids rather than being prescriptive of the mechanisms to be used in individual member states. In the discussion of Feed in Premiums, the Guidelines state that 'equivalent measures involving the direct marketing of energy produced' are possible. There is no clear definition of what this encompasses. It could be that the Irish REFIT scheme and the UK's proposed CfD would come within this definition, as renewable generation is exposed to market prices under both schemes. As set out below, we consider that the REFIT scheme has been successful and on this basis we believe there is merit in permitting such a scheme under the Guidelines. We consider that this point should be clarified so that member states do not develop non-compliant schemes; this could frustrate achievement of 2020 targets.

Under the draft version of the Guidelines, Feed-in Tariffs would need to be phased out over the coming years (provided they are State Aid). IWEA believes this is premature as Feed in Tariffs have been shown to work well in the deployment of renewable technology. In Ireland, Feed in Tariffs have worked well to date and ensured investment in renewable technologies, without overcompensating renewable energy. As part of the 2030 Package the European Commission released a Working Document on Energy Prices and Costs. On page 234 this European Commission document states:

"The merit-order effect is evaluated in several scientific studies which indicate that the additional supply of electricity from renewable sources reduces the spot price, and sometime so much that it outweighs the costs of the subsidies. The table below shows some of the results of the literature for

Member States in Europe; it shows that for wind electricity in Spain and Ireland the benefits for electricity consumers in terms of reduction in whole-sale prices outweigh the costs of subsidies.”

This clearly shows that a feed in tariff can be used for competitive deployment of renewables. IWEA believes it is premature to phase these out at this stage, without rigorous analysis that efficient deployment will continue under any revised approach being considered.

3. Technology Neutrality

IWEA welcomes the notion of differentiated treatment for technologies at different levels of development which allows for a tailor-made approach ensuring maximum cost effectiveness of national support mechanisms. This recognises that newer technologies will require additional support in the early stages, however we have some concerns in relation to the methodology used.

4. Methodology for determining deployed technologies

The methodology distinguishing between mature and immature technology based on a threshold of EU-wide electricity consumption/production is overly simplistic and will not allow targeting the aid efficiently to key technologies.

In addition, the suggested range for the threshold is too low, defeating the purpose of the Commission proposal. According to article 119, any technology which contributes to more than [1-3] % of EU-wide electricity consumption/production would be considered a deployed technology and therefore need to meet the most stringent criteria in these guidelines. Offshore wind will meet the threshold in the period up to 2020. Imposing the most stringent rules for support mechanisms to offshore wind would stifle its industrialisation process and the ensuing economies of scale which drive down capital costs. The proposal would slow progress to competitiveness instead of creating the conditions for offshore wind to become competitive.

With the threshold based on EU wide consumption, it is also likely to create a barrier to entry in those Member States where there has been less development to date, and which may need additional support to overcome initial barriers. We note that the need for support depends on both technical and commercial maturity; while technology can be more often be easily transferred, in order to reach commercial maturity it is necessary to build up a national or regional supply chain and go through the ‘learning by doing’ phase. In the absence of complete market liberalisation, IWEA believes this approach would not work.

EWEA has recommended that an approach based on the European Investment Bank lending criteria¹ would be more appropriate. Among commercially proven technologies, the EIB distinguishes between mature and emerging categories, taking into account potential for cost reductions and contribution to long term decarbonisation objectives. Offshore wind has significant potential for cost reductions and will be key to any credible strategy to meet the EU’s long term decarbonisation goals. There is, therefore, a strong rationale for offshore wind to be considered as an emerging technology in the State aid guidelines as under the EIB criteria. IWEA also supports this recommendation, however we believe that there should also be flexibility for Member States to identify the

¹ [European Investment Bank Energy lending criteria - 25 July 2013](#)

appropriate levels for themselves. When parties are making their submissions for state aid they should have to justify what they are giving and to what type of technology and in so doing outlining why the different technologies are eligible for the aid.

If a market share definition is to be used, we submit that one based on Member State or regional grouping would be more appropriate, although our view is that this would be relatively inflexible.

5. Tenders

The draft guidelines recommend a combination of Feed-in-Premiums with tenders as an appropriate mechanism to remunerate *deployed technologies* (article 120). The limited experience with this model (the SDE+ model in the Netherlands) has been disappointing which makes it difficult to understand why the Commission should promote such a system over any other.

5.1 *The Irish Experience of Tenders*

Ireland has previously used the tender approach in selecting renewable energy projects. The Alternative Energy Requirement (AER) programme was launched in 1996 and was the first step towards a market support for renewable energy as part of the Department's programme to promote the generation of electricity from renewable resources. In total 4 tenders were held for wind energy projects between 1996 and 2003: AER I, AER III, AER V and AER VI.

The AER contracts were allocated in a number of rounds. AER I aimed to secure 75MW of electricity generation capacity from renewables. 34 projects were selected to receive the offer of Power Purchase Agreements (PPA's) from the ESB. 22 projects were commissioned with a total installed capacity of 70.62MW, of which 45.8 MW was wind electricity generation capacity.

The Third Alternative Energy Requirement competition (AER III) was launched in March 1997 and the results were announced in April 1998. The original target was to provide 100 Megawatts of new electricity generation capacity. In order to allow for possible fall-out, contracts for 158.75MW, including 137.33 MW of wind, were provided for. In total, 30 projects were selected to receive the offer of Power Purchase Agreements from the ESB for a period of 15 years. A total of 11 projects were constructed including 6 windfarms, 4 small-scale hydro schemes and one Biomass landfill gas project. Of the 137.33MW of wind offered contracts, only 42.11 Megawatts in electricity generating capacity was added to the national grid as a result². The big fallout was due to speculative bids, which were not economically feasible, were awarded contracts. This clearly shows that, despite allowing for some fall-out in the design of the scheme, the tender process did not deliver the capacity that was needed.

AER 3 provides a good example of how the tender process does not always work well. 137.33 MW of wind capacity was made available under this round, however less than 50% of the required capacity and less than 30% of the contracted capacity was actually built. This was due to companies bidding tenders which were unrealistic and were then unable to meet the commitments. This led to a considerable under utilisation of the available capacity and resulted in a lower build out than expected.

² [AER Programme 2005](#)

AER V offered contracts for 240MW of wind but only 44.345MW was built. This was quickly followed by AER VI, which, even though a competitive bidding, offered a better price and indexation.

The last round of competitive tendering occurred in 2005. Experience from the tender process showed that this is not necessarily the most efficient process, in particular in smaller markets with limited competition. There was an acknowledgement that a more efficient way of incentivising investment in renewables was required, leading to the introduction of a feed-in-tariff. REFIT stands for 'Renewable Energy Feed in Tariff' and is the primary means through which electricity from renewable sources is supported in Ireland. The first REFIT scheme ('REFIT 1') was announced in 2006 and state aid approval was obtained in September 2007. Under this scheme renewable generation is exposed to the market price, and receives a REFIT payment where the market price is lower than the scheme strike price. The introduction of REFIT has seen increased development in wind energy due to the certainty it provides, and as discussed in the Commission's recent Energy Prices paper the cost of the scheme is outweighed by the benefits. This scheme has worked well in Ireland through the delivery of efficient development and in good quantities. There is also a reduced administrative burden associated with this approach which is of benefit as RES projects tend to be quite small in scale in comparison to other generation technologies.

5.2 General Comments on Tenders

Tender-based approaches have had mixed results in the past and there is no evidence that this is the most cost effective way to deploy renewables. They rely on sufficient competition and the significant upfront costs with no certainty of return can be a significant barrier to entry.

IWEA is concerned that the tender process may create a barrier to entry for smaller projects and developers. The resources required to carry out the work for a tender bid are quite substantial and would be very risky to take on with no guarantee of your project being selected. There is significant risk for all project developers, large and small, which will have a knock-on impact on the availability of finance, and result in reduced levels of development. The tender process is also perceived to be a barrier to smaller players due to the larger resource requirements upfront with little guarantee of success.

Article 120 (a) outlined that aid is to be granted in a "genuinely competitive bidding process". Footnote 57 goes on to say that this requires a sufficient number of undertakings to participate. No guidance is given as to what a "sufficient" number of undertakings is, or how operating aid should be allocated in the case where there are not a sufficient number of undertakings. This may be especially relevant in smaller markets with limited capacity and participants, in particular where there are concerns regarding market power.

It should be left to the Member States to determine whether the market is sufficiently liquid and whether there is a bidding structure that allows for effective tendering. If this is not the case Member States should be able to allocate Feed-in Premiums and Feed-in Tariffs outside of tender processes.

It is therefore not appropriate for tenders to be imposed as part of the Environmental and Energy Aid Guidelines. In principle, the Commission should promote good design, not specific systems, as is the case in the guidance on support mechanisms. IWEA believes that the tender-based approach of the Commission is too prescriptive.

6. Thresholds

IWEA welcomes that aid in the form of feed-in-tariffs may be granted to installations of first commercial scale and to small installations with an electricity generation capacity. In the absence of feed-in-tariffs being available to all renewable generation, IWEA believes that the threshold for wind generation should be increased to 10MW. This will help keep the market open to small and independent generators without the risks associated with the feed-in-premium which is proposed.

One important aspect to be considered is that many of these smaller projects are local rural community developments which are very important for community acceptance of wind energy. IWEA is concerned that, through overly prescriptive support mechanisms, tender processes and compulsory engagement in the market, the market may become closed to these smaller projects, thereby closing down opportunities for community involvement.

7. Balancing responsibilities

The draft guidelines propose imposing standard balancing responsibility on renewables. IWEA is concerned about this provision and welcomes the Commission's request for feedback on the implementation of this condition (articles 120d; 121c; 129c; 130b). Indeed, if the right caveats are not put in place, there is a risk that producers will bear unnecessary cost increases thus favouring conventional technologies, or certain market participants who do not have the same forecasting risks.

The current text states the following: "Beneficiaries are subject to standard balancing responsibilities where competitive intraday markets are in place".

IWEA believes that this requirement is too prescriptive for inclusion in the Guidelines and that this should be considered a feature of market design. In order for beneficiaries to be fully exposed to balancing responsibilities it would be essential that the following elements are included in the market design in which the beneficiaries operate:

- existence of intra-hour gate closures;
- state of the art forecasting tools and in place;
- imbalance settlement is harmonised and designed to be cost effective and market based;
- imbalance settlement should contain the true price of balancing, including procurement cost, but without any other components such as penalties;
- Producers of energy from renewable sources can bid in the balancing market.

8. Violation of priority access principle

Article 120 b of the Commission proposal includes a provision enabling Member States to *exclude electricity from specific renewables sources in certain geographic areas if necessary to secure grid stability*. This is clearly at odds with the Renewables directive which sets a principle of priority access to the grid for renewables:

"Member States shall also provide for either priority access or guaranteed access to the grid-system of electricity produced from renewable energy sources" (article 16.2.c. Directive 2009/28/EC).

This principle of guaranteed access is *subject to requirements relating to the maintenance of the reliability and safety of the grid*. However, article 16.2 of the directive includes important caveats: measures to safeguard the reliability and safety of the grid must be based on *transparent and non-discriminatory criteria*. It is therefore illegal to limit access to the grid to renewable energy producers without proper justification.

More fundamentally, the wording in the Commission proposal fails to mention the other key component of article 16 of the Renewables directive whereby Member States should develop the grid to allow for a higher penetration of renewables.

“Member States shall take the appropriate steps to develop transmission and distribution grid infrastructure, intelligent networks, storage facilities and the electricity system, in order to allow the secure operation of the electricity system as it accommodates the further development of electricity production from renewable energy sources [...].”

The wording of article 120b of the Commission proposal does not capture the balance struck in article 16 of the Renewables Directive. This reinterpretation of existing legislation is ill-advised and should be removed from the Environment and Energy Aid Guidelines. Should access to the grid need to be mentioned in article 120 of the guidelines, a reference to article 16 of the Renewables Directive would be sufficient.

9. Impact of the guidelines on current and future support mechanisms

Changes to existing frameworks can be necessary to reflect cost reductions and technical improvements, but experience shows that these changes need to be foreseeable and transparent for the investor and not be undertaken as a sudden shift or retroactive cut.

The principle whereby Member States are free to dictate the pace of reforms to their support mechanisms is essential to maintaining investor certainty. Likewise, the provision whereby these new guidelines do not apply retroactively - in line with the Commission's October 2013 recommendations on support mechanisms³ - is of critical importance.

To ensure this, Article 230 whereby *“schemes concerning operating aid in support of energy from renewable sources only need to be amended when Member States change their existing scheme”* should be maintained. It is essential that support schemes which have been approved already are not impacted by these latest guidelines. It should also be clarified that support schemes which have already been approved will remain open for the duration for which they are approved, and that projects which are building with an expectation of them remaining open will not be impacted by these guidelines. The relevant footnote (100) should, however, be reconsidered.

This footnote states that any adjustment to an existing mechanism (with the exception of tariff changes according to an already existing methodology) would be considered as a change under the current guidelines. This means that technical adjustments would *de facto* entail a complete change of the mechanism to comply with the new guidelines.

³ EC Communication: [Delivering the internal electricity market and making the most of public interventions](#) 5 November 2013

IWEA considers that only fundamental changes in national support mechanisms (such as changes in the nature of the mechanism) should be considered as changes under article 230. The current wording of the footnote means that Member States will be reluctant to make sometimes necessary technical adjustments to their mechanisms for fear that this would necessarily result in a fundamental change of the system. Instead of rewarding flexibility, as intended, this would make national support mechanisms more difficult to adjust.

IWEA also notes that there may be instances where the introduction of a new support scheme may overlap with an already existing support scheme. There should be a transition period allowed where member states are moving to a new support scheme which falls under these guidelines, but where an already approved scheme is already in place. Any changes to existing schemes on the basis of the introduction of a new scheme would be considered a retrospective change and bring uncertainty to investors.

10. Aid for Generation Adequacy

IWEA believes that the guidelines should focus on the objectives to be considered in the design of any capacity payment mechanism (CPM) and should not be prescriptive about what the mechanism should look like. As outlined in the consultation paper, different generation adequacy measures can be designed in a variety of ways to pursue different objectives. IWEA believes that there should be flexibility for Member States to design schemes to address generation adequacy which are appropriate to the specific requirements.

We submit that as well as examining capacity adequacy that member states should assess revenue adequacy in a market, where it is insufficient developers will not build capacity, existing capacity will be shut and a shortage will result. Given the long lead time with energy projects it is too late to tackle such a problem once a capacity shortage exists. The calculation of the necessary level of reliability must factor in EU priority dispatch rules, renewables targets, the resulting fuel mix of a member state and technical limitations of a system (such as limitations on levels of non-synchronous generation in a synchronous system).

Interconnectors don't represent generation capacity, rather transfer capacity, and they don't replace the need for system-wide adequacy, whether at national, regional or EU level. CPMs should allow cross border participation where technically and commercially feasible.

We would note that not all CPMs constitute State Aid. Furthermore, we consider that CPMs do not necessarily increase the overall levelised cost of electricity, rather it may be designed as a redistribution of costs of energy and capacity. It should also be noted that there are cases where a capacity mechanism is an integral part of the market design, such as in the Single Electricity Market in Ireland, and this may not fall under state aid requirements.

We agree that alternatives to fossil fuels should be used where applicable and we understand that this provision operates to allow non-fossil fuel solutions to participate. However, the focus must remain on ensuring revenue adequacy for the required level of generation (or non generation capacity) which will lead to capacity adequacy.

In order to ensure cost effective solutions we believe that CPMs must be open to new and existing generation and allow them to compete on a level playing field.

Limiting schemes to four years or less will not give the long term confidence necessary to drive investment decisions given the long lead time and lifetime of these assets.

11. Summary

In summary, IWEA welcomes the consultation on Environment and Energy Aid Guidelines and considers the on-going review as an opportunity to promote competition, the sector's competitiveness, and well-designed and stable support mechanisms for wind power. This will help ensure the cost-effective implementation of the 2020 renewable energy targets. **However, IWEA believes that the current version of the Guidelines is overly prescriptive and would fail to meet these objectives. Their implementation would result in significant unnecessary reforms and would not result in efficient roll out of renewable technology.**