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Analysis of the measures contained in the emergency intervention regulation to address high energy prices

The OJEU of 7 October 2022 published Council Regulation (EU) 2022/1854 of 6 October 2022 on an emergency intervention to address high energy prices ("**Regulation 2022/1854**" or the "**Regulation**").

According to recital (6) of the Regulation, the aim of the emergency intervention is "*a temporary mitigation of the risk that electricity prices and the cost of electricity for final customers reach even less sustainable levels and that Member States adopt uncoordinated national measures.*"

In this context, and as stated in its first article, the Regulation aims to establish an emergency intervention to mitigate the effects of high energy prices through exceptional, targeted and time-limited measures aimed at (i) reducing electricity consumption; (ii) capping the market revenues received by certain producers from electricity generation and redistributing them to final electricity customers in a targeted manner to enable Member States to implement public intervention pricing measures for the supply of electricity to household customers and SMEs; and (iii) establishing rules for a mandatory temporary solidarity contribution from Union companies and permanent establishments operating in the crude petroleum, natural gas, coal and refinery sectors, in order to contribute to the affordability of energy for households and businesses.

The legal basis for the Regulation is article 122(1) TFEU, which has enabled an urgent procedure without the intervention of the European Parliament, but is limited to exceptional and temporary measures. This article is known as the "solidarity clause", as it allows economic policy measures to be taken in the event of supply difficulties, particularly in the field of energy.

The Regulation will be in force until 31 December 2023.

This Legal Briefing analyses the key aspects of the measures contained in the Regulation.

Measures relating to the electricity market

1. Demand reduction measures

Member States must take appropriate measures to reduce electricity consumption in order to meet the following targets:

- Reduction of total monthly gross electricity consumption by 10% compared to the average of Gross Electricity Consumption[1] in the months corresponding to the Reference Period[2] , but allowing Member States to take into account, in calculating the reduction in gross electricity consumption, the increase in gross electricity consumption resulting from the achievement of gas demand reduction targets and general electrification efforts to phase out fossil fuels.

1 Gross Electricity Consumption is defined as the overall supply of electricity for activities in the territory of a Member State.

2 The Reference Period is defined as the period from 1 November to 31 March of the five consecutive years preceding the date of entry into force of the Regulation, starting with the period from 1 November 2017 to 31 March 2018.

- Reduction of gross electricity consumption during peak hours by at least an average of 5% per hour.

For this purpose, each Member State must identify the Peak Hours[3] corresponding in total to at least 10% of the hours for the period between 1 December 2022 and 31 March 2023. However, Member States are allowed to set a different percentage of Peak Hours provided that at least 3% of the Peak Hours are covered, and provided that the energy saved during these Peak Hours is at least equal to the energy that would have been saved within the above parameters.

By way of derogation, demand reduction measures will not apply to outermost regions which cannot be interconnected with the Union electricity market (in Spain, the Canary Islands).

In terms of specific measures, Member States will be free to choose appropriate measures to reduce gross electricity consumption in order to meet the targets, including the extension of national measures that are already in place[4]. In any case, the measures must be clearly defined, transparent, proportionate, targeted, non-discriminatory and verifiable, and comply with the following conditions:

- Where financial compensation is paid in addition to market revenues, the amount of such compensation must be determined through an open competitive process;
- They must only involve financial compensation where financial compensation is paid for the additional electricity not consumed compared to the expected consumption in the relevant hour without the tender;
- They must not unduly distort competition or the proper functioning of the internal market in electricity;
- They must not be unduly limited to specific customers or groups of customers, including independent aggregators, in accordance with article 17 of Directive (EU) 2019/944;
- They must not unduly prevent the process of replacing fossil fuel technologies with technologies that use electricity.

2. Measures affecting the Market Revenues of certain electricity producers

(i) Mandatory measure: €180/MWh cap on Market Revenues of certain production facilities

This measure applies to producers of electricity from the following sources: wind; solar (solar thermal and solar photovoltaic); geothermal; hydropower without reservoir; biomass fuel (solid or gaseous biomass fuels), excluding biomethane; waste; nuclear energy; lignite; crude oil products; peat.

The measure means that the Market Revenues that these producers obtain for the generation of electricity will be capped at €180 per MWh of electricity produced.

For these purposes, Market Revenues are defined as the realised income received by a producer in exchange for the sale and delivery of electricity in the Union, regardless of the contractual form

3 Peak Hours are defined as the individual times of the day when, on the basis of forecasts of transmission system operators and, where applicable, nominated electricity market operators, day-ahead wholesale electricity prices are expected to be the highest, the gross electricity consumption is expected to be the highest or gross consumption of electricity from sources other than renewable sources as referred to in article 2(1) of Directive (EU) 2018/2001 of the European Parliament and of the Council is expected to be the highest.

4 In Spain, Royal Decree-law 14/2022 of 1 August on economic sustainability measures in the field of transport, grants and funding for study, as well as energy saving and efficiency measures and measures to reduce energy dependence on natural gas, should be taken into account.

in which such exchange takes place, including power purchase agreements and other hedging operations against fluctuations in the wholesale electricity market, and excluding any support granted by Member States[5].

With regard to the application of this mandatory cap, it is important to note that:

- The cap will apply from 1 December 2022 until 30 June 2023.
- Member States will decide whether to apply the Market Revenues cap at the time of settlement of the energy exchange or subsequently, and the European Commission will provide guidance to Member States on the implementation of this measure.
- The Market Revenues cap will not apply to demonstration projects or to producers whose revenues per MWh of electricity produced are already subject to a cap as a result of State or public measures not adopted under the national crisis measures described in the Regulation itself[6].
- Member States may decide not to apply the cap (i) to producers generating electricity from facilities with an installed capacity of up to 1 MW; (ii) to electricity generated in hybrid power plants which also use conventional energy sources; (iii) to revenues from sales of electricity in the balancing energy market and from financial compensation for redispatching and countertrading.
- Member States may decide that the Market Revenues cap will only apply to 90% of the Market Revenues exceeding the cap of €180 per MWh of electricity produced.

By way of derogation, the mandatory cap will not apply to outermost regions which cannot be interconnected with the Union electricity market (in Spain, the Canary Islands).

(ii) Additional non-mandatory measures

In addition to the mandatory cap, Member States are allowed to adopt what the Regulation calls “national crisis measures”, including the following:

- Maintain or introduce measures that further limit the Market Revenues of producers to which the Market Revenues cap applies, including the possibility to differentiate between technologies, as well as the Market Revenues of other market participants, including those active in electricity trading;
- Set a higher Market Revenues cap for producers to which the Market Revenues cap applies, provided that their investments and operating costs exceed the maximum cap of €180 per MWh of electricity produced;
- Maintain or introduce national measures to limit the Market Revenues of producers from sources other than those affected by the mandatory cap of €180 per MWh of electricity produced;

5 In this regard, consideration should be given to recital (30) of the Regulation, according to which “*The cap on market revenues should be set on market revenues rather than on total generation revenues (including other potential sources of revenues such as feed-in premium), to avoid significantly impacting the initial expected profitability of a project. Regardless of the contractual form in which the trade of electricity may take place, the cap on market revenues should apply to realised market revenues only. This is necessary to avoid harming producers who do not actually benefit from the current high electricity prices due to having hedged their revenues against fluctuations in the wholesale electricity market. Hence, to the extent that existing or future contractual obligations, such as renewable power purchase agreements and other types of power purchase agreements or forward hedges, lead to market revenues from the production of electricity up to the level of the cap on market revenues, such revenues should remain unaffected by this Regulation. The measure introducing the cap on market revenues should therefore not deter market participants from entering into such contractual obligations.*”

6 In this regard, and as regards Spain and the reduction mechanism contained in Royal Decree-law 17/2021 of 14 September on urgent measures to mitigate the impact of the escalation of natural gas prices in the retail gas and electricity markets (in force until 31 December 2022), it should be borne in mind that recital (36) of the Regulation provides that “*the cap on market revenues should not apply to producers whose market revenues are subject to other regulatory measures taken by public authorities under which revenues are transferred directly to consumers.*”

- Set a specific cap on the Market Revenues obtained from the generation of electricity using hard coal;
- Subject hydropower units other than hydropower without reservoir to the Market Revenues cap, or maintain or introduce measures that further limit their Market Revenues, including the possibility to differentiate between technologies.

In any event, any additional measures that Member States decide to take must be proportionate and non-discriminatory; must not jeopardise investment signals; must ensure that investments and operating costs are covered; must not distort the functioning of electricity wholesale markets and, in particular, must not affect the merit order and price formation on the wholesale market; must be compatible with Union law.

As regards the destination of surplus revenues from the application of the Market Revenues cap, they should be earmarked by Member States to finance support measures for final electricity customers to mitigate the impact of high electricity prices for such customers, in a targeted manner.

3. Distribution of surplus congestion income revenues resulting from the allocation of cross-zonal capacity

The Regulation provides that Member States will be able to use the surplus congestion income revenues resulting from the allocation of cross-zonal capacity to finance measures to support final electricity customers[7]. In this regard, the following should be considered:

- The use of surplus congestion income revenues will be subject to the approval of the regulatory authority of the Member State concerned.
- Member States must notify the Commission of the use of surplus congestion income revenues within one month of the date of adoption of the relevant national measure.

4. Agreements between Member States

For situations where the net electricity import dependency of a Member State is 100% or more, the Regulation provides that the importing Member State and the main exporting Member State must conclude, by 1 December 2022 at the latest, an agreement to share the surplus revenues adequately. However, all Member States may, in a spirit of solidarity, conclude such agreements, which may also cover revenues from national crisis measures, including electricity trading activities.

5. Retail measures

(i) Temporary extension to SMEs[8] of public intervention in electricity price setting

Member States are allowed to apply public interventions in the price setting of electricity supply to SMEs, which must comply with the following requirements:

- They must take into account the beneficiary's annual consumption over the last five years and retain an incentive for demand reduction;
- They must be configured as a public service obligation fulfilling the conditions set out in article 5(4) and (7) of Directive (EU) 2019/944;

7 As far as Spain is concerned, it should be recalled that Royal Decree-law 10/2022 of 13 May, temporarily establishing a cost of production adjustment mechanism to reduce the price of electricity on the wholesale market, provides in article 14 for the use of congestion rents to pay the total cost of the adjustment mechanism.

8 A small and medium-sized enterprise (SME) is an enterprise as defined in article 2 of the Annex to Commission Recommendation 2003/361/EC.

- Where the price set is below cost, they must comply with the conditions set out in section (ii) below.

(ii) Temporary possibility to set electricity prices below cost

Member States are allowed to set, exceptionally and temporarily, a price for the supply of electricity that is below cost, provided that all of the following conditions are met:

- The measure must cover a limited amount of consumption and retain an incentive for demand reduction;
- There must be no discrimination between suppliers;
- Suppliers must be compensated for supplying below cost; and
- All suppliers must be eligible to provide offers at the price for the supply of electricity that is below cost on the same basis.

6. Review of electricity market measures

It is provided that, by 30 April 2023, the Commission will carry out a review of the above measures, taking into account the overall electricity supply situation and electricity prices in the Union. On the basis of the conclusions reached in that review, the Commission may, in particular and if justified by economic circumstances or the functioning of the electricity market in the Union and in each Member State, propose (i) an extension of the period of application of the Regulation; (ii) an amendment of the level of the Market Revenues cap and of the sources of electricity generation to which it applies; (iii) or any other amendment of the measures.

Measures relating to the crude petroleum, natural gas, coal and refinery sectors

A temporary solidarity contribution has been established for certain companies, in addition to regular taxes and levies, with the following characteristics:

- *Taxable event*: It applies in 2022, 2023 or both years to "surplus profits", defined as profits that are 20% higher than the average profits earned in the years 2018-2021, determined according to national tax rules.
- *Taxpayer:* Companies and permanent establishments in the EU active in the crude petroleum, natural gas, coal and refinery sectors (as defined in article 2(17) of the Regulation).
- *Tax rates and earmarking of income*: As a minimum, the tax rate will be 33% of the surplus profit, and the income will be earmarked for the purposes, in particular solidarity purposes, defined in the Regulation.
- *National legislation*: Member States must adopt and publish implementing measures for this temporary contribution by 31 December 2022.
- Similar national measures: They must meet objectives and be subject to rules that are similar in structure to those regulated in the Regulation, generating comparable or higher revenues.

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