



## **POLICY GUIDELINES**

*by the Energy Community Secretariat*

### **on Reform of the Support Schemes for Promotion of Energy from Renewable Sources**

PG 05/2015 / 21 Dec 2015



## I. Purpose

The renewable *acquis* under Title II of the Treaty establishing the Energy Community encompasses the Renewable Energy Directive 2009/28/EC ('RE Directive') as adopted and adapted by the Ministerial Council in October 2012<sup>1</sup>. With its adoption, the Contracting Parties of the Energy Community committed themselves to achieving binding national overall renewable energy targets and a separate 10% target of renewable energy used in transport by 2020.

Promoting investments in energy from renewable sources is not only a legal obligation for the Contracting Parties of the Energy Community. It stimulates development of the aging and outdated facilities of their energy sectors while responding to requirements for environmental protection, reducing dependence on energy imports and creating premises for sustainable development and growth.

In order to ensure meeting the policy objectives in renewable energy, Article 3 of RE Directive claims for introduction of support schemes for energy produced from renewable sources or measures of cooperation between Contracting Parties, with EU Member States or with third countries. The introduction of support schemes or cooperation in renewable energy is foreseen to ensure reaching the renewable energy targets in 2020 given the fact that the energy market alone cannot deliver the required investments to meet these objectives and, therefore, a form of state intervention is necessary.

At the same time, the Contracting Parties of the Energy Community are bound to comply with the *acquis* on Competition and State aid under Title II (Article 18, 19 and Annex III) of the Treaty establishing the Energy Community.

In April 2014, the European Commission issued the "*Guidelines on State aid for environmental protection and energy 2014-2020 (EEAG)*"<sup>2</sup> spelling out the conditions to be met, *inter alia* by the support schemes to ensure compatibility with the rules on State aid with a view to strengthen the internal market, promote more effectiveness in public spending, introduce a greater scrutiny of the incentive effects and limit the aid to the minimum necessary so as to avoid the potential negative effects of the aid on competition in the internal market.

The same principles apply to the Energy Community under the Article 18 of the Treaty.

On 24 November 2015, the Secretariat published the Policy Guidelines on the Applicability of the Guidelines on State Aid for Environmental Protection and Energy 2014-2020 to the Contracting Parties of the Energy Community<sup>3</sup>. The Contracting Parties should comply with the EEAG and a new approach for the design of the support schemes for renewable energy is required to be implemented and scrutinised.

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<sup>1</sup> Acquis on renewables

[https://www.energy-community.org/portal/page/portal/ENC\\_HOME/ENERGY\\_COMMUNITY/Legal/EU\\_Legislation#RES](https://www.energy-community.org/portal/page/portal/ENC_HOME/ENERGY_COMMUNITY/Legal/EU_Legislation#RES)

<sup>2</sup> Commission Guidelines on State aid for environmental protection and energy 2014-2020 (2014/C 200/01)

<sup>3</sup> PG 04/2015 / 24 November 2015

[https://www.energy-community.org/portal/page/portal/ENC\\_HOME/DOCUMENTS?library.category=1257&back\\_page\\_url=&library.offset=10](https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCUMENTS?library.category=1257&back_page_url=&library.offset=10)

**These Policy Guidelines go beyond applying the EEAG and include some recommendations based on best practices tested in the implementation of the support schemes by EU Member States.**

## **II. Rationale**

According to the definition in Article 2(k) of the RE Directive, a support scheme is “an instrument, scheme or mechanism applied by a Contracting Party or a group of Contracting Parties, that promotes the use of energy from renewable sources by reducing the cost of that energy, increasing the price at which it can be sold, or increasing, by means of a renewable energy obligation or otherwise, the volume of such energy purchased.” The support can be granted in the form of **operational aid** (feed-in tariffs, feed-in premiums, green certificates) **or investment aid** (grants, preferential loans, tax exemptions, tax refunds). Tendering schemes can be implemented for granting operational aid or investment aid as well.

All Contracting Parties have implemented schemes for the promotion of energy from renewable sources in the form of operational aid, which in some cases were complemented by investment support offered to renewable energy producers. Initially, support schemes based on feed-in tariffs were introduced as most suitable for ensuring investor confidence and initiating deployment of renewable energy potential. Nevertheless, due to the inappropriate design of the support schemes not taking into account the decrease of the costs of renewable technologies as well as the high administrative barriers stemming from the authorisation, permitting and connection procedures, such measures did not lead to significant investments in renewable energy.<sup>4</sup> On the contrary, in some Contracting Parties they even led to eroding investor confidence and creating an unnecessary burden for end-consumers that has led or might lead to investment disputes and prevent new entrants to enter the market.

In order to address the shortcomings of the existing schemes for the promotion of energy from renewable sources and to reduce the risks for investors while maintaining public acceptance for renewable energy development, the European Commission issued the Communication “*Delivering the internal market in electricity and making the most of public interventions*”<sup>5</sup> in November 2013. The Communication includes four specific guidance documents, one of which is addressing the design and the need for reform of renewable energy support schemes. The guidance calls for flexible and market-based solutions in order to avoid market distortions through overcompensation by responding to decreased production costs.<sup>6</sup>

## **III. Policy Guidelines for the reform of the support schemes for energy from renewable sources**

Legal, regulatory, administrative and financial measures are needed to support renewable energy uptake in all Contracting Parties to ensure that the 2020 renewable energy targets are

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<sup>4</sup> First Report of the Secretariat on the Progress on renewable energy in the Energy Community to the Ministerial Council, [https://www.energy-community.org/portal/page/portal/ENC\\_HOME/AREAS\\_OF\\_WORK/Obligations/Renewable\\_Energy](https://www.energy-community.org/portal/page/portal/ENC_HOME/AREAS_OF_WORK/Obligations/Renewable_Energy)

<sup>5</sup> C(2013) 7243 final, accompanied by SWD(439) Guidance for the design of renewables support schemes and other 3 Guidance documents on cooperation mechanisms, <http://ec.europa.eu/energy/en/topics/renewable-energy/support-schemes>

<sup>6</sup> The Commission guidance on support schemes was presented to the Contracting Parties in the context of the 2014 Renewable Energy Workshop, held in Vienna, on 10-11 June 2014. See: [https://www.energy-community.org/portal/page/portal/ENC\\_HOME/CALENDAR/Other\\_Meetings/2014/10\\_Jun](https://www.energy-community.org/portal/page/portal/ENC_HOME/CALENDAR/Other_Meetings/2014/10_Jun)

met. The support schemes have to be part of a long-term, predictable and stable policy and strategic framework in order to reach the 2020 policy objectives for the promotion of energy from renewable sources.

The support schemes for promotion of energy from renewable sources are a form of public intervention in the market needed to be implemented to achieve the policy objectives in renewable energy while correcting market failures. At the same time, the schemes require scrutiny to ensure they are proportionate and do not create undue distortions in the market.

When reforming the support schemes, in order to reach the 2020 policy objectives and at the same time bring their support schemes in line with the EEAG, the Contracting Parties should follow these Policy Guidelines issued by the Secretariat.

**1. Forecast and approve annual fixed budgets for promotion of energy from renewable sources to ensure that the Contracting Party is in line with the trajectory for meeting its legally binding 2020 renewable energy target**

The overall national cost for meeting the 2020 renewable energy targets could be imposed on all final energy customers or on all taxpayers through the public budgets. The costs for ensuring support for electricity produced from renewable sources is usually applied as an uplift charge, separately calculated and disclosed in the electricity bill to all final customers. Alternatively, it could be included in the transmission network charges, thus socializing it through the transmission tariff which is part of the overall cost of energy supplied to final customers by any supplier. When the support for renewable energy is part of the State budget, it could be imposed on all taxpayers through a renewable energy tax.

The annual expenditures for supporting the electricity produced from renewable sources in the Contracting Parties was assessed in the 2015 study on the progress in renewable energy for all Contracting Parties in three different policy scenarios<sup>7</sup>. This study determined the support expenditure for electricity produced from all renewable sources in the power sector expressed as a premium per unit of electricity demand in three policy scenarios. The study concluded the premium could reach up to 1,9 € per MWh electricity demand between 2015-2020 in the third (alternative) policy scenario with optimisation of resource allocation at regional level. This assessment gives an indication to the policy makers that the cost of supporting renewable energy would not create a significant burden on electricity consumers.

However, this low level of the uplift charge derived in the study can only be expected if wholesale prices are transparently transferred to end-users. The first Policy Guidelines issued by the Secretariat in 2013<sup>8</sup> called for reform of the electricity end-users prices, abandoning cross-subsidies and ensuring cost-reflectivity. However, despite commitments taken by the Contracting Parties, the wholesale electricity market price is not entirely transferred to all end-users, still requiring significant cross-subsidies between non-household and household customers.

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<sup>7</sup> Study on the Assessment of Renewable Energy Action Plan Implementation and Progress in the Promotion and Use of Renewable Energy in Energy Community, *ECN et al*, 2015, pages 62-70

[https://www.energy-community.org/portal/page/portal/ENC\\_HOME/DOCUMENTS/Studies/Sustainable](https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCUMENTS/Studies/Sustainable)

<sup>8</sup> Retail market policy guidelines for reforms of electricity market model, regulated electricity prices and electricity tariff reform, 5 June 2013

[https://www.energy-community.org/portal/page/portal/ENC\\_HOME/DOCUMENTS?library.category=1257](https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCUMENTS?library.category=1257)

Fixed annual budgets to support electricity from renewable sources could be determined and approved *ex-ante* in order to minimize the impact in the electricity price for final customers while keeping the countries on the trajectory to 2020. The recommendation is based on the existing practice in Austria, where a fixed annual budget for promotion of electricity from renewable sources is provided in the legislation.

**2. Public consultation with relevant stakeholders should be conducted at national level and draft support schemes should be notified to the State aid enforcement authorities.**

At national level, proper consultation with stakeholders and transparency of the support schemes' development process are very important elements during their design and implementation.

Moreover, before adoption, each support scheme should be notified to the national State Aid Commission as well as to the Energy Community Secretariat for assessment of compliance with the Energy Community State aid rules, including the EEAG.

Article 2 of the Rules of Procedure for Dispute Settlement<sup>9</sup> explicitly requires that each State Aid enforcement authority in the Contracting Parties should notify the Secretariat concerning the application or interpretation of Energy Community Law, in the case of EEAG in relation to the support schemes for renewable energy. Decisions of the State aid enforcement authorities on compliance of the support scheme with EEAG, as well as the support schemes, should be submitted to the Secretariat before adoption.

**3. Grant any type of support to renewable energy producers through a competitive bidding process**

The design of the tender for selecting the beneficiary of the support is very important and requires careful consideration of several aspects before it is launched to ensure it achieves its objective for driving the cost of supporting renewable down while allowing the most competitive technology to be selected by the market.

Starting from 2017, EEAG are requiring that any type of support in the form of operational support or investment-based should be granted through competitive procedures based on clear, transparent and non-discriminatory criteria unless it is demonstrated that a competitive bidding process would lead to higher support levels or low projects realisation rates (underbidding). To counteract strategic bidding, floor and ceiling prices could be introduced in the tenders.

Technological and location-neutral tendering will allow selection of the most competitive bid in order to limit the support needed to the minimum and therefore ensuring cost-effectiveness of the scheme. However, if needed to achieve diversification, address network constraints, stability of the grid or system integration costs, tenders supporting specific technologies might be suitable to correct the suboptimal results reached through technology neutrality.

Moreover, a simplified and inclusive tendering process to support small scale technologies and to minimise the administrative burden for small renewable energy producers should be envisaged to enable that the needed capacity is actually built. Therefore, penalties for non-delivery are appropriate. The results of the tenders should be made available to the public.

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<sup>9</sup> Published on 19 October 2015, [https://www.energy-community.org/portal/page/portal/ENC\\_HOME/ENERGY\\_COMMUNITY/Legal/Acts](https://www.energy-community.org/portal/page/portal/ENC_HOME/ENERGY_COMMUNITY/Legal/Acts)

#### **4. Introduce support schemes based on feed-in premium**

Operational support based on feed-in tariffs is no longer compliant with State aid rules from beginning of 2016 if it is opened to all market participants and it is not granted through a tendering process.

A feed-in premium for the operational support is most suitable to replace the existing feed-in tariffs granted on the first-come, first-served basis. A feed-in premium, with the premium granted through a tendering process, is compatible with the internal market principles and will lead to a phase-out of the subsidies needed overtime while several technologies will reach market parity.

The introduction of feed-in premiums in order to replace the feed-in tariffs currently in place goes along the introduction of competitive electricity markets and establishment of trading platforms for day-ahead markets in the six Contracting Parties of the Western Balkans as of mid 2016.<sup>10</sup> The renewable energy producers would sell electricity on the market either through bilateral contracts or at power exchange and receive a premium (which could be granted as fixed or flexible) in addition to the electricity price. Ukraine is expected to follow after the introduction of the day-ahead trading platform in July 2017, as envisaged in the draft Electricity Market Law. Moldova is the only Contracting Party which already envisages the introduction of tendering schemes as instruments for promotion of renewable energy in the draft Law on renewable energy; the start of the implementation is subject to the adoption of the Law by the Parliament.

With the coupling of the electricity markets of the Contracting Parties and those with the European markets, a joint support scheme based on a feed-in premium at regional level could be considered as the most appropriate form of cooperation mechanism to ensure cost-effectiveness of development of renewable energy at regional level.

#### **5. Establish a renewable energy operator which will manage the support scheme**

The appointment of an institution to manage the support scheme for renewable energy producers is instrumental in ensuring the viability of the scheme. In many countries, this central counterparty role is entrusted to either the market operator, transmission system operator or to an institution legally separated from the transmission system operator and created especially for this purpose. Whereas, the electricity market operator has a specific role in the electricity market and for market coupling or in the case of the transmission system operator in managing the access to the grids, it is important to legally unbundle from the very beginning the institution assigned to manage the support scheme for renewable energy from any other activity performed in the electricity market. This measure is necessary to ensure the ring-fencing of the financial management of the support scheme and, where appropriate, the introduction of an incentive mechanism to keep the variable costs of balancing under control.

#### **6. Consider “shallow” approach for the charging regime related to connection to the grids**

The cost for connection to the grids is an important part of the overall investment decision an investor in renewable energy has to take into consideration. It goes beyond the costs of connection and involves the ownership of assets, cost of operation and maintenance, *etc.*

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<sup>10</sup> Western Balkans Summit and the Energy Community  
[https://www.energy-community.org/portal/page/portal/ENC\\_HOME/AREAS\\_OF\\_WORK/WB6](https://www.energy-community.org/portal/page/portal/ENC_HOME/AREAS_OF_WORK/WB6)

The Directive calls on the Contracting Parties to develop transmission and distribution grid infrastructure in terms of intelligent networks, storage facilities and the electricity system in order to allow the secure operation of the electricity system as it accommodates the further increase of electricity production from renewable energy sources. Furthermore, transparency towards applicants has to be ensured and the rules for connecting to the power grid have to be based on objective and non-discriminatory criteria.

In order to make sure producers can generate electricity where renewable resources are available, producers should be charged with the cost of connection to the nearest point in the public electricity network only ("shallow" connection cost) and not with the costs for reinforcement or expansion of the networks ("deep" connection costs). The transmission and distribution system operators are the appropriate undertakings to create an optimal infrastructure by investing in grids reinforcement or expansion of the grids and socialize the cost for the ownership and maintenance of the network assets with all network users through regulated network tariffs.

## **7. Introduce balance responsibility for large renewable energy producers**

Exemption from balance responsibility for renewable energy producers was initially introduced as part of the support scheme when support was granted in the form of feed-in tariffs. The EEAG require that more market based exposure with an obligation of balance responsibility for renewable energy producers should be gradually introduced for new medium and large renewable energy producers<sup>11</sup> starting in 2016. This could be introduced subject to emergence of competitive power and balancing markets in the Contracting Parties that will enable price signals from power and balancing markets to reach producers. Standard<sup>12</sup>, non-discriminatory balance responsibility introduced for all market participants is key to enable transition to flexibility and cost-efficiency in use of the resources in a regional energy market.

The insufficient level of competition in the national balancing markets of the Contracting Parties dominated usually by a single balance service provider coupled with discriminatory balancing regimes and regulation of balancing capacity and energy prices<sup>13</sup> is going to be addressed with the implementation of a cross-border balancing regime in the six Contracting Parties in the Western Balkans in 2016. While in Ukraine there is more competition in the electricity market, market coupling and cross-border balancing implemented between Ukraine and Moldova could emerge, pending Ukraine's approval of the Electricity Market Law.

Gate closure times should also be harmonised across borders and brought closer to real-time to allow integration of renewable energy producers with high volatile generation like wind and solar and to minimise the costs with deviations due to forecasting errors.

## **8. Avoid any retroactive changes in the support that alter the return on investments already made and undermine investors' legitimate expectations**

Investors' confidence is threatened by disruptions of the support scheme or retroactive changes that affect their legitimate expectations. This should be avoided as it usually leads to legal disputes increasing the risks in those markets and deterring new investors. Moreover, the

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<sup>11</sup> Projects with installed electricity capacity of less than 500 kW or demonstration projects, and projects using wind energy of less than 3 MW or 3 generations units should be exempted, EEAG, paragraph (125)

<sup>12</sup> Transfer of balance responsibility to a balance responsible group should be allowed

<sup>13</sup> Regional Balancing Integration Study 2014,

[https://www.energy-community.org/portal/page/portal/ENC\\_HOME/DOCUMENTS/Studies/Electricity](https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCUMENTS/Studies/Electricity)

increasing cost of developing new projects will undermine public acceptance of renewable energy.

The Renewable Energy Coordination Group established by the Ministerial Council in 2015 will start working in 2016 on the reform of the support schemes for renewable energy producers to enable reaching the renewable energy targets by 2020 in the most cost-efficient way and in compliance with the principles of the internal market. The Renewable Energy Coordination Group will benefit from best practices and lessons learned through the EU experience towards transition to market based support schemes for renewable energy, adapting it to the specific needs of the Contracting Parties.

Vienna, 21 December 2015

A handwritten signature in blue ink, reading "Janez Kopač".

Janez Kopač,

Director