CONSULTATION RESPONSE

Response to the Commission de Régulation de l'Energie consultation on modifications to feed-in tariff and feed-in premium subsidy contracts

Brussels, 6 December 2024

Key messages

We encourage the development of forward markets and increasing their liquidity. Forward markets are more stable but not necessarily cheaper for the State to reduce their exposure to price variability in spot markets.

Following our position about the use of subsidies on a necessary-only basis, we advocate for the use of market-based instruments such as PPAs. There needs to be a balance between market-based and subsidized contracts in forward markets. To further develop forward markets, PPAs can contribute to fostering liquidity if RES producers are aware of the various options available to them. An as-produced PPA also provides risk coverage on price and volume, which can also work together with subsidy contract reforms to better protect the state budget.

Lastly, we remind the CRE to be mindful of the European discussions on virtual trading hubs and their effects on forward markets and reference prices.

Part 1: Obligation d'achat

1. *Do you agree with the positive assessment made by CRE in section 3.1 regarding the forward coverage of volumes supported by the State under the purchase obligation scheme?*

Energy Traders Europe does not have a strong position on the assessment made by the CRE.

We advocate for more wholesale forward market liquidity and recently Energy Traders Europe issued a CfD guiding principles paper. Additionally, we highlight the need to strike a balance between subsidised and non-subsidised market contracts – such as Power Purchasing Agreements that provide price and volume risk coverage – in the development of the wholesale forward markets' liquidity.

Now, recognizing that a significant proportion of Renewable Energy Sources (RES) production currently falls under the Obligation d'Achat (OA) scheme, it is also crucial to manage these volumes properly.

Consequently, we recommend restructuring this other type of support mechanism, the feed-in tariffs, known as the French 'obligation d'achat'. In fact, Energy Traders Europe notes that the current OA framework does not provide incentives to cease production during periods of negative prices on the spot markets. This is particularly concerning given the increasing frequency of negative prices in France and across Europe. Energy Traders Europe therefore strongly recommends restructuring these feed-in tariffs to incentivize stopping production when market prices are negative.

2. *Do you agree with CRE's analysis of the effect on the market of a sale by EDF OA of the Calendar product maturing in N+3, and are you therefore in favour of the introduction of N+3 products in the forward auctions organised by EDF OA?*

Energy Traders Europe acknowledges the significant volumes of Obligations d'achat and emphasizes the importance of enhancing their hedging strategy. To optimize these efforts, it is advisable to distribute these volumes over a period of 3 years instead of 2 years. Therefore, we welcome the proposal to introduce a Calendar N+3 product to facilitate this smoothing process.

Limited liquidity should also be considered when extending further the obligation d'achat calendar product maturity to N+3. The volumes should be gradually put in the market to avoid impacting market prices. At the same time, we recognise that the introduction of the N+3 Calendar product can help to improve liquidity.

3. *How interested are you in longer maturities (4-5 years) and in products other than the Calendar product with maturities of three years or more?*

We recommend analysing the effects of N+3 maturities on long-term markets before expanding to additional Calendar maturities. We suggest accompanying this analysis with a more holistic analysis of the development of forward markets accounting for the interactions between subsidy and market-based contract developments, and the lessons to be learned from their developments.

4. *Are you in favour of selling part of the almost certain production in N+3 from the 2028 delivery year? If so, would you prefer N+3 sales to start on 1 January 2025, i.e. 33% of the Calendar 2028 product to be sold in N+3, or to start on 1 July 2025, i.e. 20% to be sold in N+3 (or some other percentage)?*

Energy Traders Europe supports the sale of the N+3 product, provided that it is progressive and well assimilated into the market, which should be able to absorb the new volumes.

5. *Are you in favour of keeping EDF OA's current tender format and, in particular, the current general terms and conditions of sale? If not, what changes would you recommend?*

No comment.

Part 2: Complément de rémunération

6. *Do you share the view that it is necessary to reduce the State budget's exposure to variations in spot prices with regard to the volumes supported under the remuneration supplement scheme?*

We understand the CRE's dual objectives in the consultation: to minimise the costs of the subsidies on the State budget linked to highly fluctuating prices and to further develop forward markets. We recognise the need to better hedge price risks for the State as long as producers, and renewable energy sources especially, can interact and react to the markets. We remind the CRE that forward markets bring more stability in terms of price fluctuation for subsidies as there is less exposure to variable day-ahead prices, yet, it is not necessarily cheaper. In addition, we advise the CRE to carefully analyse the exact nature of the exposure induced by the "complement de remuneration". Unlike the part under "obligation d'achat", the CR implies an exposure which has an "optional" nature. Identifying the exact exposure it creates is not easy. Therefore, entering into hedging with forward baseload products must be done only after carefully assessing whether these products effectively reduce the CSPE budget exposure to spot prices.

Entering into a hedging position with forward products (being physical products or financial swaps) without actually having exposure to them would actually increase the exposure of the CSPE budget to spot prices and would hence be detrimental to the stability of this budget.

Our position remains focused on fostering forward market liquidity, while striking a balance between subsidised and market-based contracts, such as Power Purchasing Agreements (PPAs). We support the CRE's objective on forward market development and emphasise the role of market-based alternatives in providing price and volume hedges to further liquidity in these markets. Indeed, our CfD guiding principles paper encourages the inclusion of a forward market price in its composition to foster forward market liquidity.

7. *With regard to the flow of new installations under the remuneration supplement, do you consider it preferable 1) to introduce forward market price references at the*

level of each remuneration supplement contract rather than just spot prices, or 2) to introduce centralised forward hedging by the State of the volumes supported under the remuneration supplement? What alternative solution, if any, would you propose?

Our preference remains for market solutions to be proposed to producers to integrate forward markets. We outline below the pros and cons of the CRE's options where we highlight the need for some design clarifications and conclude with market-based alternatives.

Option 1 pros and cons

Aligning with our position paper on CfDs and introducing a forward price element, changing the feed-in premium reference price from spot to forward market price is coherent. We emphasise that this option would be implemented in future contracts and highlight that existing contracts should not be retroactively changed, nor should the future payments be changed before the contract's conclusion. Having a forward reference price would bring both volumes and more participants to the forward markets. An active forward market needs both volumes and market participants. On the other hand, one drawback is that producers, especially renewable energy sources, will have to cover their risk in their business plans as they will have to cover the forward horizon. A forward baseload product might not be a good hedge for their expected production, notably for RES assets with a very profiled shape.

Option 2 pros and cons

We reiterate that an active forward market requires both volumes and market participants. In the centralised forward hedging entity option, only volumes are brought to forward markets, which would only partially meet the objective of increasing forward market liquidity. The option also enables price hedging, but the volume risk exposure for the State – linked to the captured price – would remain. We raise attention to the complexity of the theory elaborated by the CRE, especially the coordination and clear delineations between two actors working under the State: EDF OA and the centralised entity. Additionally, we enquire about the process around the centralised entity – whether it will be created from scratch or if it will be chosen from existing market actors, which would entail clear mandates to avoid market distortions. Indeed, there is a risk that one entity will concentrate substantial volumes to hedge in forward markets, undermining market competition.

Alternatives

Lastly, we reiterate our preference for market-based instruments for fostering forward market liquidity. Existing market solutions provide price signals in the long term through power exchanges. Alternative solutions to reduce the cost of the State budget and incentivise forward market liquidity include PPAs. An as-produced PPA (on a specific asset or a national average), rather than a fixed price, would enable full hedging of both price and volume risks. Thus, PPAs can provide better protection for the State budget and reduce expenditures through additional financing of renewable energy sources by the markets. We highlight and support the French PPA guarantee scheme launched by BpiFrance as a good practice incentivising the uptake of PPAs.

8. *In the scenario of centralised forward hedging by the State, do you agree with CRE's analysis that the market can easily absorb additional volumes by N+1/ N+2 to cover the State's budget? If so, do you think this will continue to be the case in the coming years?*

We restate the need to strike a balance between subsidised and market-based contracts in the forward markets for liquidity and market efficiency. As long as the volumes are gradually sold and there is clear transparency on the process, the market should be able to absorb the volumes. This will also depend on the depth of the French forward markets. While the Cal+1 markets in France are relatively reliable, it is less certain for Cal+2. Lastly, we reiterate the risk of one entity concentrating substantial volume to hedge in forward markets.

9. *Do you think it would be appropriate, initially, to cover the remuneration supplement only via a Calendar product sold over 2 years? If not, do you have any other proposals?*

We recognise that a Calendar product sold over two years could be a potential start for encouraging forward market liquidity. We remind the CRE while Cal+1 forward markets in France are relatively reliable, it is less certain for Cal+2 markets. Reiterating our position for the feed-in tariff segment of the consultation, we recommend thoroughly evaluating the impacts before looking into longer maturities.

Additionally, we suggest that the CRE be mindful of the European discussions around Virtual Trading Hubs linked to any reference price made in the forward markets.

10. *Could you be interested, as part of a competitive procedure, in proposing to carry out the operations required to implement a proposed solution? If so, what information would you need to put together such a service offer?*

We emphasise the need for a competitive procedure in the selection or creation of the centralised entity.

11. *In your opinion, should a centralised entity acting on behalf of the French State adopt a strategy for hedging the volumes covered by a remuneration supplement (choice between transactions in physical or financial products, sale of products via an organised platform or through dedicated auctions)? Which sales methods do you think are most appropriate at this stage?*

We point out to the CRE that its objective to incentivise liquidity in forward markets in the centralised entity option includes a complex set-up that leaves subsidised producers out of the forward market. An active and liquid market requires both volumes and participants. We suggest that for better participation in the forward markets by the centralised entity it should be fully unbundled from the State to act on the market as a market participant.

The centralised entity would act upon the availabilities in the market, rather than using dedicated auctions.

12. *In the context of this competitive procedure, what competitive bidding criteria and what compensation or remuneration arrangements would you consider to be the most appropriate?*

The difference between the CRE's two options is that the centralised entity does not change the contracts for feed-in premiums but adds a State hedging strategy for its budget exposure, while the second option is geared toward new contracts based on a forward reference price. We reiterate our preference for the second option. In the first option and existing feed-in premium contracts, we enquire whether it is worth creating a separate entity. Additionally, the State remains the main actor in the first option, hence why we raise the question of whether the State has already established practices to hedge risks and financial risk management (such as insurance), or if it could develop these practices without creating a new entity.

13. *What do you consider to be realistic implementation timescales? In particular, do you think that the target of 2026 for the introduction of such forward cover centralised by the State (covering the 2027 and 2028 delivery years) is feasible if the regulatory framework is properly adapted by then?*

For the option with a forward reference price, it will include new contracts. We underline the need to account for the transition phase with existing contracts, avoiding retroactive changes that can impact contract parties negatively, such as refused /inaccessible bank loan guarantees, and keeping future payments for existing contracts unchanged until their conclusion. The implementation timescale for this option would depend on the length of the redrafting process.

Concerning the implementation of the centralised entity option, we add in the differentiation between the regulatory and legislative framework depending on the government's decision for implementation. With an adapted regulatory framework, it could feasibly be ready for implementation by 2026. Whereas, with a legislative framework, the current political situation indicates a more complicated and protracted process. This option's implementation will also hinge on the set-up of the centralised entity. Ultimately, it will be up to the State to be ready by 2026.

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