

Guiding principles for the design of Contracts for Difference schemes

Brussels, September 2024

The recently adopted EU Electricity Market Design (EMD) reform places the market at the heart of the energy transition, as a driver for new renewable and low-carbon power generation:

- with a new emphasis on long-term agreements between private parties in the form of Power Purchase Agreements (PPAs) and forward trading,
- and, where public financial support is still needed, the reform foresees that it shall be organised through two-way Contracts-for-Difference (CfD) or equivalent schemes.

As Energy Traders Europe, we propose several recommendations in this paper so that two-way CfD schemes achieve their policy goals most efficiently. **We call on Member States to ensure the highest possible degree of harmonisation of 2-way CfD schemes, and we trust that our guiding principles will improve social welfare for all European consumers.**

This paper discusses 3 main design challenges that need to be addressed in a coherent manner by Member States:

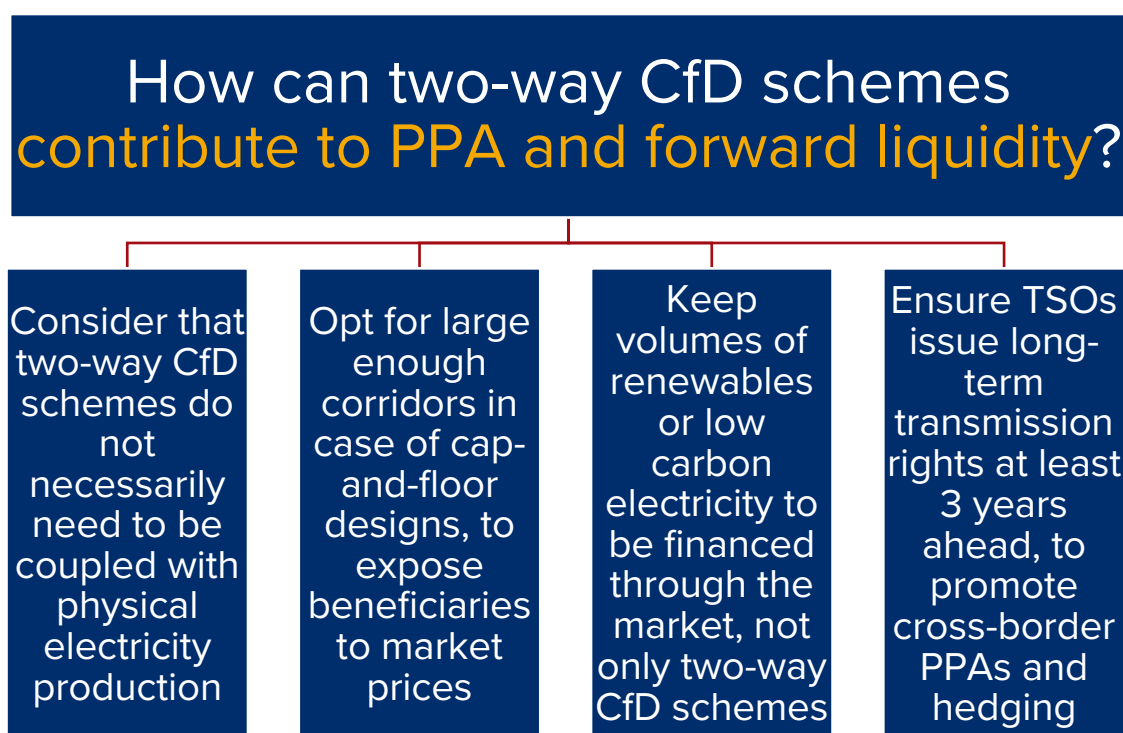


Key guiding principles for two-way CfD design

1. Contributing to market liquidity in PPAs and forward trading

For the greatest societal benefit – and to limit public expenditures – it is important to keep incentives for the market itself to finance the development of renewable and low-carbon power generation. PPAs and forward contracts are an effective means of increasing price transparency, reducing price volatility for consumers and increasing investment stability for new generators¹.

It is important to make sure that two-way CfDs complement, rather than replace, private financing. Here are some guiding principles to do that:



We believe this is the way to keep incentives for market participants to **hedge price volatility for the benefit of consumers**, and to provide the **fastest route to private financing for renewables and low-carbon technologies**.

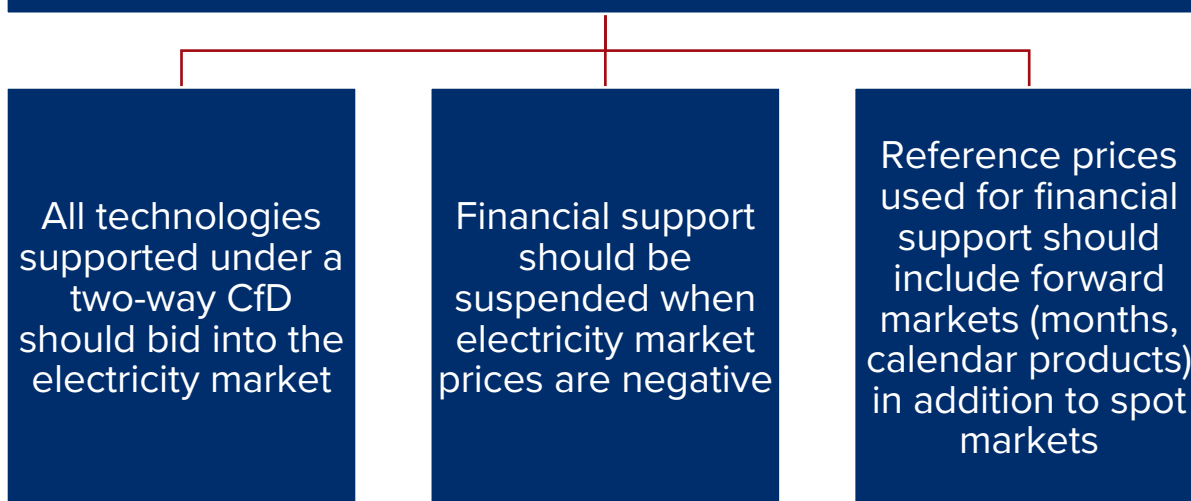
¹ For more details on this, read our two Insight on PPAs: https://www.efet-d.org/files/documents/20220302_EFET_Insight_04_renewable_PPAs.pdf and on forward electricity markets: https://www.efet-d.org/files/documents/20220216%20EFET_Insight_01_forward_trading.pdf

2. Preserving price signals for an efficient dispatch

In European electricity markets, the cheapest resources are activated first to meet consumer demand². Most of the time, these are renewable and low-carbon electricity sources, because the price to activate and dispatch them is lower than that of other power technologies.

To keep this great feature, we need to preserve the price signal from the electricity market. Here are some guiding principles to do that:

How can two-way CfD schemes preserve electricity price signals?



We believe this is the way to keep **reasonable consumer bills**, provide **fair competition** between all power generators, and make sure we keep the **flexibility of our interconnected electricity system**.

² For details on how this works, read our Insight on marginal pricing: https://www.efet-d.org/files/documents/20220222%20EFET_Insight_02_marginal_pricing.pdf

3. Providing better visibility to support investment decisions

When investors apply for public financial support, it is generally when additional certainty is needed to move ahead with their decision. Two-way CfD schemes can provide that. If well-designed, they can even be a booster to attract foreign investment.

The design of two-way CfD schemes and their award process will be a decisive factor in providing the right level of visibility to investors. Here are some guiding principles to do that:

How can two-way CfD schemes provide better visibility to investors?



We believe this is the way to ensure the **right level of comfort for investors** while making sure we maintain **transparent and efficient public expenditures**.

The introduction of two-way CfD schemes and their design will be decided individually by each Member State. The introduction of two-way CfD schemes and their design should therefore be carefully weighed to **preserve incentives to take the market route**.

The pace at which renewable and low-carbon technologies will need to develop in the next 5 years is unprecedented. So, whether financing will come from the market and/or public funds, **strong efforts will be needed to facilitate permitting, develop grids, and maximise cross-border transmission capacity**.