

## Ensuring a level-playing field in the development of Demand Response



### Reaction of EFET, EURELECTRIC and Europex to the Clean Energy Package 16 May 2017

Matching supply and demand at all times is a crucial element for efficient wholesale markets in the planning phase and in particular for real-time power system operation. As a consequence of the EU power mix transitioning away from fossil fuels towards more intermittent renewable energy sources, more flexibility is needed to manage the electricity system and operate the grid. Demand response (DR) can bring a major contribution to meet this challenge, and help build an efficient power system in line with the European energy policy, to the benefit of all consumers.

Demand response can be implemented with two different approaches, either based on direct consumer reaction to time-varying electricity supply prices (*implicit DR*) that consumers are exposed to in the retail market, or based on individual or aggregated flexible demand which is sold in power markets (*explicit DR*). The latter can be performed by large consumers themselves or DR aggregators, a generic name which refers to retailers or independent aggregators which act on behalf of a pool of consumers.

Implicit DR is already a daily reality for many residential customers in Europe with a dual meter and a tariff for peak and off-peak hours, for instance. This form of DR is likely to develop further with the roll-out of smart meters. Explicit DR has also developed among larger industrial customers directly acting on the market, while DR aggregation is only at a nascent stage in many Member States. In several European markets, current electricity prices provide limited incentive for consumers to participate in demand response programmes as the energy component represents on average only 25 to 35% of retail consumers' bill, which in many Member States is heavily burdened with increasing taxes and levies in particular.

In any case, both forms of DR should be enabled by a clear and robust regulatory framework that integrates DR in the current framework of the internal energy market, avoiding undue subsidisation and distortions to wholesale and retail markets.

EFET, EURELECTRIC and Europex fully support the objective, embedded in various provisions of the CEP, that generation, storage and demand response should compete on a level-playing field. **We applaud the overall emphasis of the proposals on the use of market-based mechanisms, on efficiency of price signals and on the creation of a level playing field between the various actors in the electricity sector that should facilitate development of *both implicit and explicit DR*.**

**We also welcome that the Package defines a framework enabling aggregators to participate in all segments of the electricity market**, including balancing and reserves markets, on an equal footing with other market actors. All DR aggregators should be able to act in the market and possible barriers to their participation need to be lifted. Hence, **we recommend reinforcing Article 3.2 of the draft recast Directive by including all DR service providers, including ‘independent DR aggregators’ in the list of actors whose freedom to enter in and exit from the market should be guaranteed, alongside electricity generators and suppliers.**

However, one of the main purposes of the CEP should be a greater participation of demand as a whole in the market rather than identifying specific categories of actors to fulfil that goal. We believe that all DR aggregators should comply with the common market rules and compete on a level playing field with other providers of demand-side flexibility.

Therefore, we regret that the general framework introduced by the draft Internal Market Directive leaves aside some of the fundamental market design principles and is inconsistent with the draft Internal Market Regulation, which could cause future legal and regulatory uncertainty, namely:

- **Exempting aggregators from paying suppliers or generators for energy sourced but not consumed (art. 17.3 (d)):** When an ‘independent DR aggregator’ sells energy on the market, this energy has been sourced by supplier of the involved consumers. This energy is not consumed by the activated customer; this then results in freeing up of energy that is implicitly diverted by the independent DR aggregator and potentially consumed elsewhere in the system. We support the idea that there should not be undue compensations imposed on ‘independent DR aggregators’ beyond the costs of the sourced energy. However, a fair market based remuneration of this sourced energy - by which the ‘independent DR aggregator’ pays the supplier for its sourcing costs - should be required instead of being explicitly excluded. Omitting this adds distortions to free price formation and risks undermining the overall efficiency of the market. As stated in the EC own impact assessment *“the exclusion of any compensation mechanism introduces a possibility of demand aggregators being free riders in the markets and therefore creating inefficiencies. This is not in line with the EU target model and generally not in line with creating a level playing field for competition.”*<sup>1</sup>If this issue is not tackled, other participants in the market will bear the costs of DR activation, with a risk of seeing end-consumer bills increase.
- **Exempting aggregators from well-established market disciplines regarding imbalance settlement (art. 17.4):** The current market model is based on the central principle of balance responsibility, an obligation for anyone connected to the grid to respect its schedules or to be exposed to the financial consequences for deviating from them. This principle would be violated if one category of market participants were exempted from being charged by the TSO the cost of its energy imbalances. The activity of ‘independent DR aggregators’ should not induce distortions for BRPs, which

<sup>1</sup> Impact Assessment, Annexes, end of section 3.1.5.

can for instance be ensured if an imbalance adjustment is applied on impacted BRPs. Also policy makers should beware that creating an enabling framework where specific businesses are immune from balancing responsibility could incentivise the opportunistic establishment of DR activities only according to the requirements of the CEP (explicit DR through an independent aggregator) to the detriment of other DR approaches such as implicit DR or explicit DR in one's own name. Such a development would, as long as the standard discipline of the market would not apply to independent DR aggregators, lead to an ever-increasing share of the overall consumption that would not be subject to balance responsibility in the planning stage. This would have negative economic repercussions among market participants in the wholesale/retail markets and lead to larger real-time imbalances in the power system as schedules provided to the TSOs would lose precision. For all these reasons, and as a fundamental rule, 'independent DR aggregators' should thus be financially responsible for their own imbalances.

As stakeholders actively contributing to the enhancement of electricity market design in Europe, the signatories believe that the principles of balancing responsibility and payment of sourcing cost shall be taken up with no delay. If they remain overlooked, the whole market design could be negatively affected with ultimately increasing costs for consumers. Besides, the legal uncertainty resulting from the overhaul of national market models where DR has been successfully developing would be detrimental to the offtake of DR.

The new European framework should encourage the development of DR by ensuring a level-playing field between market participants, clarifying roles and responsibilities, developing the enabling regulatory, market and technical conditions, rather than introducing distortions detrimental to market efficiency.

We remain committed to finding solutions which will enable European consumers to choose how they can make the best use of their demand flexibility, for their benefit and that of the system. We call for a pragmatic approach that will allow suppliers, aggregators and other service providers to compete on a level-playing field without undue distortions of fair competition or unjustified market entry barriers.