To the attention of:

Mr. Nicolae-Ionel Ciucă
Prime Minister of Romania

Mr. Virgil Daniel Popescu
Minister of Energy Romania

11 March 2022

Dear Prime Minister, Dear Minister Popescu,

EFET[1] concerns around the extension of damaging electricity and gas market measures

Executive Summary

In October 2021 your government introduced a package of measures to address high energy prices[2]. Those measures were intended to last from 1 November 2021 until 31 March 2022. Ahead of the adoption of those measures, we expressed our support for measures which would support customers without distorting markets, but expressed serious concerns about a clawback mechanism for power generators. We argued, and continue to believe, that measures of this type could exacerbate, rather than mitigate, high energy prices. We are therefore extremely concerned to see proposals to extend these measures until 31 March 2023[3] and to introduce other deeply concerning market interventions:

We understand that the package of measures is designed to curb price volatility while being compatible with European law. We consider that neither objective is achieved by the proposals in their current form:

- A wholesale transaction tax provides a strong disincentive to trade in the Romanian market. If traders leave the market, then liquidity will fall and price volatility will increase. If parties are subject to a tax, they will seek to recover the additional costs in the way they trade. This is likely to increase price.

- The European Commission published its "*REPowerEU: Joint European Action for more affordable, secure and sustainable energy*" consultation on Tuesday. That document outlines measures which it considers Member States can implement to deal with rising prices. Transaction taxes are not included in that document. The document does include criteria for the design of measures similar to the proposed clawback. However, the current clawback mechanism does not meet these criteria.

- We are also concerned that the wholesale transaction tax will have negative impacts on the Romanian and regional market and will prove incompatible with the system of

[1] The European Federation of Energy Traders (EFET) promotes competition, transparency and open access in the European energy sector. We build trust in power and gas markets across Europe, so that they may underpin a sustainable and secure energy supply and a competitive economy. We currently represent more than 100 energy trading companies, active in over 27 European countries. For more information: www.efet.org.

[2] Via GEO 118/2021

[3] Via draft GEO available at https://www.focus-energetic.ro/wp-content/uploads/2022/03/PROIECT-OUG-1-aprilie-2022.pdf

Day Ahead Electricity Market Coupling which has proved so successful in Europe. This is the cornerstone of the Internal Energy Market which contributes to security of supply, affordability and decarbonisation.

These proposals do not meet their stated objectives and will have a damaging impact on local and regional markets and on customers. We strongly urge you to withdraw these measures or, at a minimum, reconsider their design

The counter-productive impact of the proposals

Here we outline, in more detail, our concerns about the potentially counter- productive impacts of the proposals.

Wholesale Transaction Tax (**as per art. 17[4])**

We note the following concerns about the proposed wholesale transaction tax.

1. *Reducing liquidity* – A well-functioning market relies on liquidity. Liquidity allows buyers and sellers to trade when they need to and to respond to unexpected events. A tax on transactions will clearly reduce incentives to trade. Parties may trade less or not trade at all.

2. *Increasing volatility* - Illiquid markets are more risky and tend to be more volatile. You cannot be sure that you will be able to find a trading partner when you need to, so need to include a risk premium to cover that. A consequence of less liquidity is likely to be more volatility.

3. *Increasing price* – Parties may seek to compensate for the additional tax by raising prices. This will ultimately be passed on to customers – as will additional premiums resulting from lower liquidity and a risk of future intervention.

4. *Cross border and regional impacts* – The European Day Ahead market is coupled – meaning that bids, offers and transmission capacity are optimised across Europe. This contributes to security of supply, affordability and decarbonisation. A transaction tax will distort this mechanism.

5. *Discouraging future new entry* – The tax sends a negative signal about the attractiveness of the European market. Encouraging market exit or deterring market entry will have negative longer-term impacts.

6. *Practicality of implementation* – We understand the details of the policy will be in place 15 days after the decree is agreed. This clearly makes it impossible for someone to reflect it in their trading strategy and means they must plan for the worst. More generally, it looks extremely difficult to design and implement given, for example, rules regarding double taxation.

7. *Incompatibility with European law* – The proposal is, in our view, fundamentally incompatible with European law. These measures were not mentioned in the Commission's recent communication – implying that it is not something they consider

[4]Full text of Article 17: *(1) During the period of application of this emergency ordinance, the income earned by the holders of the licenses of electricity / natural gas trader as well as by the non-resident economic operators participating in the electricity and natural gas markets, resulting from the sales on the centralized / organized markets, shall be taxed with 10% of the value of the transactions. (2) The method of application of the tax provided for in para (1) shall be established by order of the president of the National Agency for Fiscal Administration within 15 days from the entry into force of this emergency ordinance*.

appropriate. Furthermore, the potential impact on market coupling and on regional markets is also incompatible with the regulations governing the Internal Energy Market.

We therefore strongly recommend the withdrawal of this mechanism.

Extension of the clawback mechanism (as per art 16*[5]*)

We note that the clawback mechanism proposed under article 16 appears to be substantively similar to that implemented under GEO 118/2021, albeit with a lower threshold. We expressed our concerns about this in a joint letter with our colleagues at Eurelectric, Wind Europe, and SolarPower Europe in February 2022. In particular we stressed, and continue to believe, that:

1. The proposal could hinder security of supply:
    a. By hindering wholesale price formation according to the interaction of demand and supply, leading to either:
        i. artificially higher prices to compensate for the taxation imposed; or
        ii. reduced production because the additional taxation would mean that generation costs could not be recovered.
    b. By discriminating between producers with different production costs – potentially leading to the insolvency of producers with higher production costs who would be unable to increase their sale prices to compensate for the additional taxation.
    c. By reducing incentives for domestic production without being able to count on imports.

2. The proposal could create incentives to leave the Romanian market:
    a. By creating additional risk for electricity market participants, which would need to ensure there was no breach of the profit limitation clause.
    b. By introducing a level of uncertainty about policy stability and regulatory risk which may deter future entry.

3. We also consider this aspect of the proposal to be inconsistent with Internal Energy Market Law. We note that the Commission's REPowerEU consultation acknowledges the permissibility of clawback mechanisms (As per its *Annex 2: Guidance on the application of infra-marginal profit fiscal measures)*. That Annex provides several criteria which must be fulfilled by any such mechanism so as "*to avoid unnecessary market distortions, while incentivising additional investments in renewable energy*". It is clear that the current and proposed clawback mechanism does not meet many of these criteria, including in respect of non-discrimination, time and various other design features.

At a minimum, this mechanism should be redesigned to meet the criteria in the Commission's REPower EU communication and should, ideally, be withdrawn.

[5] Full text of Article 16: *(1) During the period of application of the provisions of this emergency ordinance, the additional income earned by the electricity producers resulting from the difference between the average monthly selling price of the electricity produced and the price of 300 lei/MWh shall be taxed with 80%.*
(2) From the provisions of para. (1) electricity producers are exempted for fossil-fuel based capacities, including cogeneration, biomass and for production capacities put into operation after the date of entry into force of this emergency ordinance.
(3) The tax provided for in para (1) shall be declared and paid by the electricity producers, with the exception of energy producers for the capacities referred to in para. (2), monthly, until the 25th inclusive of the month following that for which this tax is due. The payment of the tax is made to the state budget, in a separate budget revenue account.
(3) The method of application of the tax provided for in para. (1) shall be established by order of the president of the National Agency for Fiscal Administration, within 15 days from the entry into force of this emergency ordinance.

The supplier margin limitation

For completeness, we would also like to record our concerns that the supplier margin limitation could have a dampening impact on retail prices, which could distort market functioning and weaken price signals. In the longer term this might discourage energy efficiency or demand side response. We are also concerned that such limitations would dilute incentives for suppliers to hedge, negatively affecting wholesale liquidity and increasing exposure of retailers to market volatility.

Conclusions and recommendations

We understand the rationale for these proposals is to curb price volatility while being compliant with European law. In our view, both the wholesale transaction tax and the continuation of the clawback mechanism will have the opposite effect to that intended. We therefore strongly recommend the withdrawal and redesign of these policies as a matter of priority.

Yours sincerely,
On behalf of the European Federation of Energy Traders

Mark Copley
CEO, EFET