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Proposal for a Council Regulation

on an electricity emergency tool and a solidarity contribution of the fossil sector

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EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

Gas and electricity prices have reached record levels in 2021 and hit all-time highs following the Russian invasion of Ukraine. Over the past year, electricity prices in Europe have rapidly risen to a level much higher than in recent decades. This dynamic is intrinsically linked to the high price of gas, which increases the price of electricity produced from gas fired power plants, which are often needed to satisfy demand. Prices started rising rapidly last summer when the world economy picked up after COVID-19 restrictions were eased. Subsequently, Russia's invasion of Ukraine has exacerbated this situation.

Energy prices are expected to remain high due to uncertainty in the market following a series of gas supply disruptions that can only be explained by a deliberate attempt by Russia to use energy as a political weapon. Further disruptions of Russian gas supplies to the EU in the forthcoming weeks or months may result in even higher levels of gas prices with knock-on effects for the price of electricity, level of inflation, the overall EU financial and macroeconomic stability and on citizens.

The Commission is acutely aware of the impact that the uncertainty around gas supply is having on the electricity market. Member States across Europe have experienced a surge in electricity prices linked to rising gas prices, leading to gas becoming the marginal price setting fuel ahead of coal. At the same time, electricity generation in the EU has been below usual levels in the last months due to increased maintenance works of power stations, lower output from hydropower generation, and closures of some older power plants.

In parallel, record-breaking temperatures this summer have pushed up energy demand for cooling and have added pressure on electricity generation. The extreme weather conditions have thus contributed to energy scarcity and high energy prices, constituting a burden for consumers and industry and dampening the economic recovery. Additional supply pressures on energy and food commodity prices are feeding global inflationary pressures, eroding the purchasing power of households and the economy as a whole.

The dramatic increase in electricity prices that we are observing is putting pressure on households, small and medium enterprises and industry and risks causing wider social and economic harm. Vulnerable customers and the energy poor are hardest hit as was already the case last winter, but the high prices are increasingly affecting middle-income households and businesses that risk not being able to pay their energy bills and are facing the choice between energy and other essential goods or, for businesses, their financial viability is in question.

This economic context requires a rapid and coordinated EU-wide response to mitigate in particular the difficulties that high prices are causing for consumers and, not only energy poor and vulnerable but also middle-income households and businesses. Electricity retail prices have increased by almost half year-on-year from July 2021[1] and the extraordinary increases are expected to continue ahead of the next heating season gradually trickling down to most consumer contracts. The EU response needs to be coordinated in a careful and holistic way. Electricity must continue to flow efficiently around Europe so that Member States can export surplus electricity. The role of the internal energy market in helping mitigate the impact of the current energy crisis cannot be overlooked. ACER’s assessment of the EU Wholesale Electricity Market Design[2] showed that cross-border trade delivered EUR 34 billion of benefits to consumers in 2021 while helping to smoothen price volatility, and that it enhances each Member State’s security of supply and its resilience to price shocks.

At the same time, the very high energy prices currently faced by consumers generate exceedingly large financial gains not only for electricity generators with lower marginal costs, but also for companies in the oil, gas, coal and refinery sectors. These gains are primarily due to favourable external market factors caused by the Russian war and not by companies’ own efforts or investments. These high energy prices create hardship for EU households and businesses, drive up inflation and necessary support measures raise public expenditure. Therefore, it is opportune to redistribute some of the revenues garnered by companies in the different energy sectors, as a result of these exceptional circumstances, to alleviate difficulties for energy consumers and society in general. Such redistribution can be achieved by different instruments, depending on the circumstances of the sector, with the purpose of making these funds available to consumers or projects to strengthen the Union’s energy autonomy including the possibility for Member States to channel parts of the contribution to Union funds in the spirit of solidarity if they decided to do so or use them on the basis of agreements between Member States.

Currently, extremely high energy prices for the consumers generate exceeding financial gains for energy companies in a short amount of time, due to favourable market factors instead of due to their

1 Source: VAASAETT

2 https://acer.europa.eu/Official_documents/Acts_of_the_Agency/Publication/ACER's%2520Final%2520Assessment%2520of%2520the%2520EU%2520Wholesale%2520Electricity%2520Market%2520Design.pdf

own investment. At the same time, the high energy prices create hardship for EU households and businesses, drive up inflation and raise public expenditure. Therefore, it is necessary to redistribute some of these revenues of the energy companies to alleviate difficulties for the energy consumers and society in general.

Several Member States of the Union have already adopted or are currently considering the adoption of such measures. However, measures adopted solely at the national level risk to create uneven conditions for companies operating on the EU energy market. In order to create a level playing field, the Commission proposes to establish a measure that temporarily reduces electricity revenues and profits in the fossil sector falling within the scope of this Regulation. By reducing the revenues of producers, the measure proposed in the Regulation aims to mimic the market outcome that producers could have expected if global supply chains would function normally, in the absence of the gas supply disruptions that have taken place since the invasion of Ukraine in February 2022. Conversely, as the temporary solidarity contribution targets the rentability of legal entities active in the oil, gas, coal and refinery sectors, which has significantly increased compared to prior years, it is necessary for it to apply to their profits.

The Member States will use proceeds from the solidarity contribution to provide support to households and companies and to mitigate the effects of high energy prices, as well as finance measures for the reduction of energy consumption and support industries, thus develop EU energy autonomy.

Against such environment adaptations to the long-term market design as announced in the Communication on Short-Term Energy Market Interventions and Long-Term Improvements to the Electricity Market Design that was issued alongside the Repower EU Plan of 18 May 2022. The proposed Regulation preserves the benefits of the internal electricity market in terms of dispatch efficiency and security of supply while, at the same time, lowering electricity demand and the impact of high gas prices on consumers' electricity bills.

2. ELECTRICITY EMERGENCY TOOL

Reduction in demand for electricity

In response to the heightened risk for the coming winter and the need to lower overall electricity demand, to preserve fuel stocks for electricity generation and take targeted action to reduce electricity prices in the most expensive hours, in a spirit of solidarity, the proposed Regulation sets out two electricity demand reduction targets.

The first requires Member States to put measures in place to lower overall electricity consumption from all consumers, including those who are not yet equipped with smart metering systems or devices enabling them to adjust their consumption during the day. The measures should be sufficiently ambitious and could include, for example, targeted consumer information and communication campaigns. In addition, to specifically target most expensive hours of electricity consumption when gas generally sets the marginal price, the Commission proposes a mandatory target of at least a [xxx]% reduction in gross electricity consumption during selected peak price hours covering at least [xxx]% of the hours of each month where prices are expected to be the highest. This mandatory target would result in selecting on average 3 to 4 hours per weekday, which would normally correspond to peak load hours, but can also include hours where electricity generation from renewables is expected to be low and the generation from marginal plants is necessary to cover the demand. To account for this, Member States have a certain margin of discretion when identifying these hours. The binding target specifically addresses consumers who can deliver flexibility through demand reduction or demand shifting offers on an hourly basis. Member States should be free to choose the appropriate measures to achieve the demand reduction targets and should, in particular, consider economically efficient and market-based measures such as auctions or tender schemes for demand side response or electricity not consumed. This may include expanding existing schemes or national incentives to develop demand response. This may also include financial incentives or compensation to participating market parties in cases when this is paid for additional electricity not consumed compared to the expected consumption in the hour without the tender. The introduction and implementation of such measures should be without prejudice to the application of State aid rules.

Based on observed hourly generation during the period between January and August 2022, a reduction of [xxx]% during the [xxx]% hours displaying the highest level of demand for electricity would bring the average demand during these hours to the level of the first non-selected peak hours. This would therefore result in a smoothening of the hourly consumption profile. Moreover, since gas is generally the marginal technology during the hours with the highest demand, this targeted [xxx]% reduction can lead to a reduction of gas consumption estimated around 1.2bcm over a 4-month period. This represents around 3.8 % of gas consumption for power over the same period. Recent studies[3] show that the current potential of demand response could fulfil the mandatory target, having a positive impact on electricity prices and on volumes of gas savings.

[3] Study on the quantification of Demand Response (DR) benefits to electricity suppliers and consumers in Europe in 2030 on its way to achieve deep decarbonisation, Compass Lexecon, January 2021; Demand Side Flexibility potential contribution to 2023 gas reduction, DNV, September 2022

Cap on market revenues for the generation of electricity from inframarginal technologies

Secondly, the proposed Regulation sets out an approach to recover excess revenues from generators with lower marginal costs such as renewables, nuclear, and lignite ("inframarginal technologies") by setting an ex-post cap on revenues per MWh of electricity produced.

In the day-ahead market, electricity prices are determined by the variable cost of the marginal technology, i.e. the last and most expensive plant that is needed to meet demand (marginal pricing). In view of the role that the electricity prices in the day-ahead market have as a reference for the pricing of electricity across all the other market timeframes, this measure reduces the impact that the margin-setting technology (typically coal, today often gas-fired power plants) has on the revenues of other generators with lower marginal costs such as most renewables, nuclear, and lignite. It mimics the market outcomes for these technologies that could be expected were global supply chains functioning normally and not subject to the weaponisation of energy through gas supply disruptions.

Through this Union-wide approach, based on the principle of solidarity, the electricity wholesale markets would function and clear as they do today, thereby ensuring that the cheapest and most efficient power plants around the EU are dispatched always first, and that Member States can rely on imports when needed. This preserves the incentive for technologies such as coal and gas-fired power plants, storage facilities and demand response to be available to run when needed, ensuring the stable operation of the electricity system throughout the winter season 2022-23.

<u>The level of the cap on market revenues</u>

The revenue cap prescribed in this Regulation should be set at a level that encompasses the majority of inframarginal generators in the EU and avoids jeopardising the availability and profitability of existing plants and future investment decisions for new inframarginal generation.

While occasional and short-term peaks on prices can be considered a normal feature in an electricity market and may be useful for some investors to recover their generation investment, the extreme and lasting price increase since February 2022 is markedly different from a normal market situation of occasional peak prices.

In order not to undermine the assessment of profitability when investments decisions were made, the cap should not be set below the expectations of market participants as to the average level of electricity prices in the hours during which the demand for electricity was at its highest, before the invasion of Ukraine by Russia. The average market price expectations for peak hours were consistently and significantly below [xxx] EUR/MWh during the past decades, despite price differences across regions in the Union. Moreover, simulations based on observed prices over January through August 2022 show that a cap set at [xxx] EUR/MWh would have resulted in stabilising the average revenue around [xxx] EUR/MWh. This average revenue level is consistently higher than the current levelised cost of energy (LCOE) for the inframarginal technologies targeted by the application of the cap on revenues[4], allowing producers to which it applies to cover their investments and operating costs. The cap should therefore not impair the investment in new inframarginal capacities. Therefore, the Commission proposes to set the revenue cap at [xxx] EUR/MWh, which incorporates the necessary security margin.

Such a cap should be limited to market revenues rather than encompassing total generation revenues (including for instance those stemming from support schemes), to avoid significantly impacting the initial expected profitability of a project.

Having a uniform cap on revenues across the Union is necessary to preserve the functioning of the internal electricity market as it would maintain price-based competition between electricity producers based on different technologies, in particular for renewables. As the cap will apply on the revenues per MWh of electricity produced, price formation in electricity wholesale markets will not be affected. The dispatch of power plants will continue to take place based on their level of efficiency, with those with lower marginal costs being dispatched first, and the cross-border trade of electricity will not be affected.

Member States will need to put appropriate procedures in place to recover the surplus revenues from generators, as the revenue cap may be applied at the moment when transactions are settled or, if not possible, thereafter. This depends on differences in the way wholesale electricity markets function in different timeframes and how they are organised in Member States.

<u>Scope of the cap</u>

The market revenue cap would apply to revenues from the generation of electricity for all inframarginal generators as defined in the Regulation and cover all market timeframes, regardless of whether the trading of electricity takes place bilaterally (over-the-counter) or in centralised marketplaces. If the cap was to apply only to certain timeframes or only to exchanges and other organised marketplaces, inframarginal generators could have an incentive to trade electricity in the

[4] Energy costs, taxes and the impact of government interventions on investments: final report, Trinomics, October 2020.

timeframes and marketplaces not covered by the measure. On the other hand, the proposed wide application of the revenue cap would preserve incentives to conclude long-term power purchase agreements, which are crucial for consumers to hedge against price volatility and important tool to stimulate investments in inframarginal technologies, especially renewables. Given that the revenue cap does not interfere with the formation of prices, consumers would have an interest to conclude long-term power purchase agreements which allow them to benefit directly from prices lower than those observed in the market.

The cap on revenues will apply per MWh of electricity produced. Regardless of the contractual form in which the trade of electricity may take place, the cap should apply to realised market revenues only. This is necessary to avoid targeting producers who do not actually benefit from the current high electricity prices due to having hedged their revenues against fluctuations in the wholesale electricity market at a price below the cap level. Hence, to the extent that existing or future contractual obligations, such as renewable power purchase agreements and other types of power purchase agreements or forward hedges, lead to market revenues from the production of electricity up to the level of the cap, they would not be caught by its application.

Definition of relevant inframarginal technologies

The revenue cap is applicable to market revenues from the sale of electricity produced from technologies the marginal costs of which are lower than the cap, such as wind, solar, geothermal, nuclear energy, biomass, oil and oil-related products, hydropower installations without reservoir, etc.

The cap on market revenues should however not apply to the technologies with input fuel costs leading to break-even level above the cap level, as this would jeopardise these activities and, ultimately, security of supply. This is for instance the case of gas-fired and coal-fired power plants. Since the invasion of Ukraine, the prices of natural gas and hard coal have increased sharply[5] , leading to break-even generation price above the cap level. If gas-fired and coal-fired power plants were subject to the revenue cap, they would not be able to cover their operating costs and would be pushed out of activity.

In line with the objectives of the REPowerEU Communication, the application of the cap should not hamper incentives in investments in flexible generation technologies (e.g. demand-response and all types of storages), and the production of electricity from sources that directly compete with natural

[5] Natural gas price increased above 200 eur/MWh, and coal prise above 300 eur/MWh.

gas and gas-fired power plants. Accordingly, the cap should not apply to power plants using biomethane.

This is necessary in order to preserve the incentives for these technologies and generation types to decrease gas consumption, as highlighted in RePowerEU Communication.

In order to preserve the incentives for the development of innovative technologies, the revenue cap should not apply to demonstration projects. In practice, this is already usually the case, as the remuneration of demonstration projects is typically set out of the market (e.g., fixed revenues through feed-in-tariffs).

In some Member States, the revenues obtained by some generators are already capped by way of State measures. As such these generators do not benefit from increased revenues resulting from the recent spike of electricity prices. Therefore, existing producers subject to this type of State measures should be excluded from the application of the cap.

With a view of avoiding an excessive administrative burden and ensuring an efficient application of the proposed measure, Member States should be allowed to exclude producers generating electricity from installation facilities with a capacity below 20 kW from the application of the revenue-limitation measure.

Redistribution to final customers

The surplus revenues resulting from the application of the cap will have to be channelled to final electricity consumers, be it private or commercial ones, who are exposed to high electricity prices, in line with the measures set out in the Energy Prices Toolbox[67] ("Toolbox") adopted on 13 October 2021 and in the Communication on Short-Term Energy Market Interventions and Long Term set out in the Repower EU Plan of 18 May 2022. The amount of revenues will be related to the amount of electricity generated from inframarginal technologies and the level of gas price, which varies depending on the energy mix and the design of RES support schemes of each Member State. Member States are free to choose how best to use these additional resources to support consumers at national level, without prejudice to the application of State aid rules.

6 COM (2021) 660 final of 13 October 2021: Tackling rising energy prices: a toolbox for action and support

7 COM (2022) 236 final

Addressing difficulties faced by consumers

Finally, the proposed Regulation contains key provisions to address the difficulties being faced by consumers as a result of very high energy prices. The current crisis represents the challenge of ensuring adequate support so that household consumers continue to have access to necessary energy, while not undermining the incentive to save energy. The starting point for action is full recognition of the hardship risk that households are facing, including middle income households and need for support measures at national level.

A wide range of support measures have already been put in place by Member States, including measures based on the Toolbox. These have included direct income support, reductions in taxes, and levies and rebates on consumers energy bills, as well as measures to support energy efficiency and on-site renewable production. Member States have also intervened in price setting in the supply of electricity – that is establishing regulated prices for end-consumers.

All of these tools will remain important. Member States should be able to choose those which best suit their national circumstances. As far as possible, support to consumers will also need to support demand reduction. However, it is also important to recognise that some consumers may already be close to the minimum essential level of consumption necessary to safeguard their well-being.

The Commission provided Guidance on the application of State intervention into price setting in the Communication REPowerEU: Joint European Action for more affordable, secure and sustainable energy[8] in the design of public interventions in price setting for the supply of electricity, ensuring they benefit consumers during this current crisis and enhance competition to the benefit of consumers over the longer term. However, under Directive (EU) 2019/944 such regulated prices may not cover small and medium enterprises and must not be below cost.

Consumers' right to choose the energy supplier who offers them the best price and service lies at the heart of the internal electricity market. The resulting competition has put downward pressure on prices and increased choice, as consumers no longer had to rely on incumbent monopolists. Competition and choice of suppliers and offers will also be a key part of realising the European Green Deal, as they allow consumers to benefit from the internal market for electricity and to contribute to attaining the Union's energy efficiency and renewable energy targets.

[8] COM(2022) 108 final

As set out in the Communication on Short-Term Market Interventions and Long-Term Improvements to the Electricity Market Design, the Commission considers that it could be acceptable in the current context to extend price regulation to small and medium-sized enterprises (SMEs). Given that the EU energy legislation does not envisage any specific framework for these consumers, allowing Member States to extend regulated prices to small and medium enterprises during this crisis would give them another tool to manage its impact. This approach reflects the fact that the current energy market situation with high and volatile wholesale gas and electricity prices may be restricting competition and harming customers in the SME segment. However, such a possibility should maintain the incentive to reduce consumption and thus be limited to 80% of their historical consumption.

Public interventions in price setting for electricity which is below cost could be a way for some Member States to directly alleviate the impact of the crisis on consumers. Nonetheless, such measures also have significant impacts on the functioning of competition in the retail market, on innovation, and on the incentive to reduce demand. This is why, even as an emergency measure, they need to be accompanied by safeguards to ensure non-discriminatory treatment of suppliers and an incentive for demand reduction.

Ensuring that the internal electricity market gives Member States the tools and flexibility needed to respond to the crisis is a critical part of the solidarity needed. However, whether to use these possibilities should remain the choice of Member States who are best placed to determine the efficacy of such measures, particularly compared to other tools, and to match them to the need to target support to where it most needed.

Solidarity between Member States for the coming winter

With a view to avoiding the significant distortions of the internal market, potentially accentuating the security of supply risk for this winter, it is crucial that all Member States act jointly and in a spirit of solidarity as soon as possible. All Member States have been negatively affected by the current crisis, but not all are equally financially able to support consumers. This may lead to a situation in which some Member States provide support to consumers while others may not be able to afford or might hesitate to intervene with measures that may negatively affect the internal electricity market.

A coordinated effort to reduce demand and redistribute excess revenues to struggling consumers is the best way to navigate the challenges ahead this winter. By coordinating demand reduction, preserving the ability to import electricity when needed and using surplus revenues to support consumers, Member States will be able to cater for better support to consumers and businesses, therefore mitigating the impact of inflation in the whole economy and strengthening the resilience of the EU internal market. A coordinated action is also necessary to contribute to better solvency for citizens and businesses, therefore mitigating the impact of inflation on the whole Union economy. All Member States should share the burden and contribute to the joined effort of supporting customers to avoid undermining the principles of the single market.

While Member States are differently affected by the impact of the gas supply shortages on electricity prices, all Member States commit with this measure to reducing their electricity consumption at the same level. Coordinated efforts at EU level to reduce electricity demand EU-wide will lower overall consumption of electricity in the entire Union, leading to lower wholesale electricity prices and subsequent lower prices for consumers. The reduction of electricity demand during peak hours will also result in a reduced need for gas-fired power plants as there will be less overall demand for electricity. Such coordinated response will tap the potential of electricity savings in the EU, which would not be possible to the same extent absent coordinated action of all Member States at EU level. All Member States contribute to the joint effort of bringing the prices down and preventing security of supply risks. Since in the internal electricity market the Member States' electricity systems are coupled, the measure could be effective only if all Member States play their part in reducing demand in order to be able to benefit from it.

Contribution of the measures to solidarity

While Member States are differently affected by the impact of the gas supply shortages on electricity prices, all Member States commit with this measure to reducing their electricity consumption at the same level. Coordinated efforts at EU level to reduce electricity demand EU-wide will lower overall consumption of electricity in the entire Union, leading to lower wholesale electricity prices and subsequent lower prices for consumers. The reduction of electricity demand during peak hours will also result in a reduced need for gas-fired power plants as there will be less overall demand for electricity. Such coordinated response will tap the potential of electricity savings in the EU, which would not be possible to the same extent absent coordinated action of all Member States at EU level. All Member States contribute to the joint effort of bringing the prices down and preventing security of supply risks. Since in the internal electricity market the Member States' electricity systems are coupled, the measure could be effective only if all Member States play their part in reducing demand in order to be able to benefit from it.

Only Union action can ensure that the impact of high prices on consumers bills are minimised in a uniform way and that the current crisis does not lead to lasting harm for citizens and the economy. This is because uncoordinated national measures could affect the functioning of the internal energy market thus endangering security of supply, possibly leading to further price increases in the Member States most affected by the crisis. Safeguarding the integrity of the internal electricity market is therefore crucial to preserve and enhance solidarity between Member States. Furthermore, not all Member States can support consumers to the same extent due to limited financial resources, while at the same time, some electricity generators enjoy excessively high revenues.

In the same vein, the solidarity between Member States, through a uniform cap on the revenues of inframarginal generation technologies will generate revenues for Member States to finance measures in support of electricity final customers, while at the same time preserving the price signals on the markets across Europe, and preserving cross-border trade. Therefore, it will ensure that electricity in Europe continues to flow to where it is most needed and that cheaply produced electricity is exported to Member States where the electricity production is more expensive. Such a coordinated effort by Member States therefore enshrines the principle of energy solidarity between Member States and citizens of the Union.

Furthermore, this measure is compatible with the current way of trading and pricing electricity around Europe, thereby ensuring that energy trading and sharing remains intact, that Member States can continue to rely on their neighbours for imports and that those Member States with less domestic generation and limited natural resources are more protected from the risks of supply disruptions. It is therefore justified to base the proposed instrument on Article 122(1) TFEU.

The extreme price increase has led to a situation where not only many households face a significant challenge to pay their bills, but which constitutes also a serious risk for the economy. As the extent of the current problems has not been anticipated in the current regulatory framework, it is therefore appropriate to allow state interventions into retail prices which are in favour of small and medium-sized enterprises and, subject to certain conditions, interventions which lead to price levels below the costs of energy suppliers. However, the impact of the gas supply shortages on electricity prices, as well as the possibilities to finance support measures from State budget differ between Member States. As a result, there are disproportionate effects of the crisis in some parts of the Union, where customers are not able to access the energy, they need as suppliers withdraw from the market. Absent the proposed measures, there is a risk that only wealthier Member States could have the resources to protect these customers and suppliers, leading to severe distortions of the internal market. The uniform obligation created by this regulation to pass on the excess revenues to final consumers will ensure that, in principle, all Member States will be able to protect their customers and to use these additional resources for the same purpose.

3. Solidarity Contribution

Not only electricity generating companies, but also the fossil fuel sector is benefiting from the current market situation and the extreme price increases and generating profits that go beyond the result of ususal business activities. In order to financially support the measures that are necessary to react to current crisis situations for household and industry and that those that generate surplus profits need to contribute parts of them in the spirit of solidarity.

As soaring electricity prices put a significant burden on authorities, consumers, and industry alike. action is needed to avoid the risk that prices reach unsustainable levels, with far greater knock-on effects and widely detrimental social and economic implications.

These developments represent an exceptional event, entailing a massive and disruptive impact on Member States' authorities, businesses and households., which calls for a collective response at Union level. EU leaders and the Commission have therefore identified an urgent need for additional measures to mitigate the impact of these events on EU citizens and economic operators, and to stave off an even more acute crisis.

Member States will introduce together a solidarity contribution for the fossil industry. This solidarity contribution is an exceptional and temporary measure appropriate to the current situation that Member States would take in a spirit of solidarity to mitigate the direct economic effects of the soaring energy prices for public authorities' budgets, consumers and companies across the Union.

Introducing a temporary solidarity contribution will ensure that also those sectors contribute in proportion to the profits generated by the crisis situation. At the same time the design of the contribution will ensure that there are sufficient funds available to finance the investments necessary to invest in the transition to new energy sectors and technologies including at EU level.

To that end, this Regulation also establishes a measure that consists of a temporary, solidarity contribution based on taxable surplus profits made in the fiscal year 2022 from companies and permanent establishments active only in the oil, gas, coal and refinery sectors that is commensurate and appropriate to the current socio-economic situation. The contribution will allow to finance measures that help mitigatee the current crisis, in a spirit of solidarity between Member States. The measure will enable a redistribution of resource and financial support to households and companies to mitigate the effects of sustained high energy prices, reduce energy consumption, support energy intensive industries and develop the Union's energy autonomy, to the benefit of all Member States. Moreover, the current disruption to gas supplies and resulting impacts on gas and electricity prices, higher demand for energy resulting from record-breaking temperatures, combined with reduced availability of certain power generators constitutes a severe difficulty in the supply of a specific – in this case energy – product. The measure will help preserve the smooth functioning of the internal market and ensure the necessary solidarity between Member States.

The collective establishment, by Member States, of a coordinated, one-off, temporary solidarity contribution based on taxable surplus profits made in the fiscal year 2022 on energy undertakings in the oil, gas, coal and refinery sectors in the Union governed by common framework is needed to help protect consumers and businesses against soaring energy prices across the whole Union while preserving the smooth functioning of the internal market and ensuring the necessary solidarity between Member States. It is therefore justified to base the proposed instrument on Article 122(1) TFEU. The establishment of a solidarity levy adds an element of fairness to the package of measures to be launched in the context of the Emergency intervention on energy.

This proposal therefore ensures that all Member State coordinate their efforts. It reflects the principle of energy solidarity, which has recently been confirmed by the Court of Justice as a fundamental principle of EU law[9].

Consistency with existing policy provisions in the policy area

The proposed instrument sets out temporary, proportionate and extraordinary measures. It complements existing relevant EU initiatives and legislation and is complementary to the initiatives already taken by the Commission to respond to the current crisis in energy markets. It flows logically from existing initiatives, such as the Energy Prices Toolbox adopted on 13 October 2021 and the "REPowerEU" Plan of 18 May 2022, which contains a list of measures that Member States can use to support consumers and complementary to the "Save Gas for a Safe Winter" initiative.

[9] Judgment in Case C-848/19 P (Germany v Poland).

In addition, the demand reduction elements of the proposed Regulation will support the recently adopted Storage Regulation (EU) 2022/1032[10] by reducing the need for electricity production from gas, thereby helping Member States to preserve gas stocks obtained through the storage filling obligations and safeguard supply for the winter of 2022–2023.

Extending the scope of State interventions in line with the measures proposed in the Regulation is justified by the gravity of the current situation on electricity markets.

The proposed initiative responds to the increased retail price burden being felt by all electricity consumers and the need to reduce demand and save gas this winter as a result of Russia's war against Ukraine.

Consistency with other Union policies

The proposal is an extraordinary measure, to be applied for a limited time, that is consistent with a broader set of initiatives to enhance the Union's energy resilience and to mitigate the risk or impact of possible emergency situations. The proposal preserves the functioning of the internal market and does not compromise its integrity, as functioning cross-border energy markets are key to ensure security of supply in a situation of supply shortages. Providing for more coordinated electricity demand reductions, it is also in line with the Commission's Green Deal ambition and it follows the same principles and objectives as outlined in the "Save Gas for a Safe Winter" initiative. Finally, the proposal is in line with the consumer protection principles, aiming to ensure affordable energy prices for consumers across the EU.

[10] Regulation (EU) 2022/1032 of the European Parliament and the Council of 29 June 2022 amending Regulation (EU) 2017/1938 and (EC) No 715/2009 with regard to gas storage, OJ L 173/17 of 30 June 2022.

4. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY

Legal basis

The legal basis for this instrument is Article 122(1) of the Treaty on the Functioning of the European Union ('TFEU').

The current disruption to gas supplies and resulting impacts on gas and electricity prices, and higher demand for energy resulting from record-breaking temperatures this summer combined with reduced availability of certain power generators constitute a severe difficulty in the supply of energy products pursuant to Article 122 TFEU. Soaring electricity prices are putting a significant burden on consumers and businesses, and if no action is taken, they risk reaching unsustainable levels, which could have significant wider social and economic implications. EU leaders and the Commission have identified the urgent need for additional measures to mitigate the impact on EU citizens and be better prepared for the coming winter.

The temporary measures under the proposed Regulation embody the principle of solidarity in the area of energy and allow Member States to have a coordinated approach to protecting consumers without compromising the functioning of the internal electricity market.

Subsidiarity (for non-exclusive competence)

The planned measures of the present initiative are fully in line with the subsidiarity principle. Because of the significant uncertainty in the Union electricity market and the resulting extraordinary high prices caused by the weaponisation of gas supply by Russia, there is a need for EU level action. A coordinated approach through Union-wide electricity demand reduction, in the spirit of solidarity, is necessary to minimise the risk of potential major disruptions during the winter months when electricity consumption and electricity production from gas will be higher.

Given the unprecedented nature of the gas supply crisis and the role of gas as a key technology to meet electricity demand, action at Union level regarding electricity markets is also warranted. Member States must be able to rely on imports if and when needed this winter, underlining the importance of the internal electricity market. Power must continue to flow around Europe to avoid a high-price crisis becoming a security of supply crisis. However, this must be affordable and the disproportionate effects on consumers' electricity bills should be tackled. To preserve the functioning of the electricity system and cross-border trade and investments, a common approach to revenue limitations for inframarginal technologies is both reasonable, appropriate and proportionate.

As concerns electricity, this proposal sets the final result to be achieved with the measures, in the form of setting out demand reduction measures and legally binding obligations on energy reduction when electricity prices are at their highest and the limitation of the revenues of inframarginal technologies. At the same time, it gives Member States full autonomy in choosing the most effective means to meet these obligations according to their national specificities and widens the possibility for Member States to intervene in price regulation. More specifically:

- Regarding demand reduction for electricity, the proposed Regulation sets binding targets to be achieved while leaving Member States the choice of the means to achieve those targets.
- Regarding the cap on revenues to fund support to consumers, the proposed Regulation sets a uniform cap applicable in the Union. However, Member States retain the right to introduce further limitations, as long as they are proportionate, do not distort the functioning of electricity wholesale markets, do not jeopardise investment signals and they are in line with Union Law. The surplus revenues will be used to support consumers, but have full autonomy regarding the means of ensuring that the surplus revenues reach consumer.
- Regarding measures of public intervention in retail prices, the proposed Regulation actually enlarges Member States' scope to take such measures compared to the current legislative framework at Union level, which is in line with the principle of subsidiarity.

As concerns the measure in the fossil sector, the temporary solidarity contribution tackles the challenge faced by all Member States which is currently being addressed in disparate ways with a framework governing a solidarity contribution at the European level. The common initiative at Union level, consisting of the mandatory introduction of solidarity contributions in each Member State for certain undertakings only active in oil, gas, coal and refinery sectors. This problem cannot be appropriately addressed by Member States alone.

Solidarity contributions introduced by Member States founded in this Regulation will increase revenues for the State budget and enable them to finance measures aimed at alleviating the burden of high energy costs for consumers, in particular vulnerable persons and companies. Some Member States have already adopted taxes and levies on windfall profits of energy companies. However, not every Member State has introduced such measures, and the content of the already adopted measures varies from Member State to Member State.

Hence, a mandatory solidarity contribution on windfall profits governed by a common Union framework will ensure a sufficient level playing field across the Union and a situation where all Member States' authorities can reap the proceeds from such surplus profits that would enable them to better tackle the exceptional event of soaring energy prices, which requires urgent action in all Member States. Therefore, an EU initiative would add value, as compared to what a multitude of actions taken at national level can attain.

Therefore, by reason of its scale and effects, the measure can be better achieved at Union level, hence the Union may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union.

Proportionality

The initiative complies with the proportionality principle. It falls within the scope of Article 122(1) TFEU. The policy intervention is proportional to the dimension and nature of the problems defined and the achievement of the set objectives.

In view of the unprecedented geopolitical situation and the significant threat for citizens and the EU economy, there is a clear need for coordinated action. Coordinated efforts at reducing overall electricity consumption as well as electricity consumption at peak hours, capping the revenues achieved by inframarginal electricity producers and giving Member States more scope for public intervention in retail price-setting are suitable means to reduce the existing upward pressure on electricity prices to the detriment of consumers. At the same time, no other, less intrusive measures can be envisaged that would as effectively achieve that objective.

The proposed solidarity contribution respects the proportionality principle in that it does not go beyond what is necessary to achieve the objectives. It is based on a calculation base and rate, which ensure that profits are partly subject to such a contribution without unnecessarily impeding the energy companies in the oil, gas, coal and refinery sectors to use such surplus profits for future investment or for ensuring their viability. That is why the rate proposed in the regulation is limited to one third of the surplus taxable profits, after a buffer is applied to the tax base. However, and to ensure that Member States' specific circumstances are safeguarded, the proposed rate is a minimum rate and Member States may apply a higher rate in case they deem it is necessary.

The solidarity contribution is also of a temporary nature and limited to those surplus profits made in the fiscal year 2022, and is applied only to surplus profits of the oil, gas, coal and refinery sectors, taking into consideration the unexpected profits earned as a result of unpredictable circumstances. Those Member States that have a domestic levy or tax already in place exceeding the proposed rate of the solidarity contribution, may continue to apply the existing higher rate to cater for the national specificities that led them to adopt such rate.

Hence, the proposal does not go beyond what is necessary to achieve the objectives laid down in the current instrument. The proposed measures are considered proportionate and build to the extent possible on existing initiatives, which have been welcomed by Member States.

Choice of instrument

Taking into account the scale of the energy crisis, the potential of its social, economic and financial impacts and the urgency to mitigate them, the Commission deems it suitable to act by way of a regulation which is of general scope and directly and immediately applicable. This would result in a swift, uniform and Union-wide cooperation mechanism.

5. STAKEHOLDER CONSULTATIONS AND IMPACT ASSESSMENTS

Stakeholder consultations

Due to the politically sensitive nature of the proposal and urgency to prepare the proposal so that it can be adopted on time by the Council, a dedicated stakeholder consultation and a formal impact assessment could not be carried out.

Fundamental rights

No negative impact has been identified on fundamental rights. The measures under this instrument will not affect the rights of customers who are categorised as protected under Regulation (EU) 2017/1938, including all household customers. Furthermore, the provision on revenue limits in the proposed Regulation fully takes into account the need to protect existing investments and therefore will not jeopardise the right to own and use lawfully acquired possessions. The instrument will enable Member States to reduce the risks associated with gas shortage that would otherwise have major implications on the economy and society. By ensuring that suppliers who are required to sell electricity below cost are compensated this ensures that such persons are not deprived of their fundamental rights, albeit without prejudice to the application of State aid rules.

6. BUDGETARY IMPLICATIONS

This proposal does not require additional resources from the EU budget.

7. OTHER ELEMENTS

Not relevant.

2022/[…] (NLE)

Proposal for a Council Regulation

on an electricity emergency tool and a solidarity contribution of the fossil sector

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 122(1) thereof,

Having regard to the proposal from the European Commission,

Whereas:

(1) [background] Very high prices in electricity markets have been observed since September 2021. As set out by ACER in its assessment of EU wholesale electricity market design in April 2022[1], this is mainly a consequence of the high price of gas, which is used as an input to generate electricity. Natural gas fired power plants are often needed to satisfy the demand for electricity when the demand is at its highest during the day or when the volumes of electricity generated from other technologies such as nuclear, hydro or variable renewable energy sources do not suffice to cover demand. The escalation of the Russian military aggression against Ukraine, a Contracting Party of the Energy Community, since February 2022 has led to gas supplies declining markedly, in a deliberate attempt to use gas supply as a political weapon. The Russian invasion of Ukraine has also caused uncertainty on the supply of other commodities, such as hard coal and crude oil, used by power-generating installations. This has resulted in substantial additional increases in the volatility of price levels of electricity.

(1) [background] The recent substantially lower levels of gas delivery and increased disruptions of gas supply from Russia point to a significant risk that a complete halt of Russian gas supplies may materialise in the near future. To increase the Union's security of energy supply, the Council adopted Regulation (EU) 2022/1369[2] that provides for a voluntary reduction of natural gas demand by 15% this winter and grants the possibility for the Council to declare a Union alert on security of supply, in which case the gas demand reduction would become mandatory.

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1 https://acer.europa.eu/Official_documents/Acts_of_the_Agency/Publication/ACER's%2520Final%2520Assessment%2520of%2520the%2520EU%2520Wholesale%2520Electricity%2520Market%2520Design.pdf

2 Regulation (EU) 2022/1369 of 5 August 2022 on coordinated demand-reduction measures for gas (OJ L 206, 8.8.2022, p. 1).

(2) [background electricity] In parallel, the exceptionally high temperatures observed during the summer of 2022 have pushed up demand for electricity for cooling, adding pressure on electricity generation while, at the same time, electricity generation from certain technologies has been significantly below historical levels due to technical and weather-dependant circumstances. This is due mainly to an exceptional drought which led to (i) a shortfall in the production of electricity by nuclear power plants in different Member States caused by the lack of available cooling water, (ii) scarce hydropower generation and (iii) low water levels in major rivers which have adversely affected the transport of commodities used as input fuel for generation. This unprecedented situation means that the volumes of electricity generated from natural gas-fired power plants have stayed persistently high, contributing to exceptionally and abnormally high wholesale electricity prices. Despite the reduced availability of generation capacities in some Member States, electricity exchanges between Member States have helped to avoid security of supply incidents and contributed to mitigating price volatility on the EU markets, thereby enhancing each Member State's resilience to price shocks.

(3) [background electricity] The price surge in wholesale electricity markets has led to sharp increases in electricity retail prices, which are expected to continue ahead of the next heating season gradually trickling down to most consumer contracts.

(4) [background] All Member States have been negatively affected by the current energy crisis, albeit to a different extent. The stark increase of energy prices is substantially contributing to the general inflation in the euro area and slowing down economic growth in the Union.

(5) [background] A rapid and coordinated response is therefore needed. The deployment of an emergency tool would allow to mitigate, on a temporary basis, the risk that electricity prices and the cost of electricity for final customers reach even less sustainable levels and that Member States adopt uncoordinated national measures, which could endanger security of supply at Union level and put an additional burden on the Union's industry and consumers. In a spirit of solidarity between Member States, a coordinated effort by Member States during the next winter season 2022-23 should allow to mitigate the impact of high energy prices and ensure that the current crisis does not lead to lasting harm for consumers and the economy.

(6) [background – rather electricity] The current disruptions to gas supplies, reduced availability of certain power generating plants, and the resulting impacts on gas and electricity prices, constitute a severe difficulty in the supply of gas and electricity energy products within the meaning of Article 122(1) of the Treaty on the Functioning of the European Union. There is a serious risk that the situation could deteriorate further in the coming winter season in case of further disruptions of gas supplies and of a cold winter season driving up the demand for gas and electricity. Such further deterioration could lead to more upward pressure on the price of gas and other energy commodities prices with a resulting impact on electricity prices.

(7) [Solidarity reasoning] A united and well-coordinated Union-wide response is needed to tackle the stark increase of electricity prices and their impact on households and industry. This is, because uncoordinated national measures could affect the functioning of the internal energy market, endangering security of supply and leading to further price increases in the Member States most affected by the crisis. Safeguarding the integrity of the internal electricity market is therefore crucial to preserve and enhance the necessary solidarity between Member States.

(8) [solidarity – demand reduction] While some Member States might be more exposed to the effects of a disruption of Russian gas supplies and the resulting price increases, all Member

States can contribute to limiting the economic harm caused by such disruption by appropriate demand reduction measures. Reducing electricity demand at national level can have a positive, Union-wide effect on electricity prices, as electricity markets are coupled and savings in one Member State thus benefit also other Member States.

(9) [solidarity – cap] Uncoordinated caps of revenues from electricity produced from generators with lower marginal costs such as renewables, nuclear, and lignite (inframarginal generators) may lead to significant distortions between generators in the Union, as generators compete EU-wide on a coupled electricity market. A commitment to a joint Union-wide cap on surplus revenues will avoid such distortions. Furthermore, not all Member States can support consumers to the same extent due to limited financial resources, while at the same time, some electricity generators may continue enjoying significant surplus revenues. Solidarity between Member States, through a uniform cap on the revenues of inframarginal generation technologies will generate revenues for Member States to finance measures in support of electricity final customers, such as households, SMEs and energy intensive industries, while at the same time preserving the price signals on the markets across Europe, and preserving cross-border trade.

(10) [solidarity – retail] With a view to the extreme increase of retail gas and electricity prices State interventions to protect retail consumers are of particular importance. However, the impact of the gas supply shortages on electricity prices, as well as the possibilities to finance support measures from State budget differ between Member States. If only some Member States with sufficient resources can protect these customers and suppliers, this would lead to severe distortions of the internal market. The uniform obligation created by this regulation to pass on the excess revenues to final consumers allows all Member States to protect their customers. The positive effect on energy prices will have a positive impact on the interconnected EU market and will also help dampening the inflation rate. Therefore, national measures will, in the interconnected Union economy, also have a positive effect in other Member States.

(11) [solidarity – fossil] Fossil companies will have to make a solidarity contribution, which is an exceptional and temporary measure appropriate to the current situation that Member States would take in a spirit of solidarity to mitigate the direct economic effects of the soaring energy prices for public authorities' budgets, consumers and companies across the Union.

(12) The solidarity contributions are justified by the fact that such companies make unpredictable surplus profits, which are due to unforeseen circumstances. Those profits do not correspond to any regular profit that these entities would or could have expected to obtain in normal circumstances should the unpredictable events in the energy markets would not have taken place. Therefore, the introduction by Member States of solidarity contributions reflect a measure they jointly take in a coordinated manner and in a spirit of solidarity to generate across the Union additional proceeds for authorities to provide financial support to households and companies heavily affected by the soaring energy prices while ensuring a level playing field across the Union and the internal market. They should be applied in parallel to the regular corporate taxes levied by each Member State on the companies concerned.

(13) [background - measures] To ensure coherence across energy policy areas, the measures set out should work as an interdependent package reinforcing each other. All Member States should be able to support consumers the cap on market revenues for inframarginal electricity generation and reduction of electricity demand contributes to

lowering energy prices and impose a solidarity contribution on fossl companies. At the same time, lower demand should have positive effects in terms of reducing the risks to security of supply, in line with the objectives of Directive (EU) 2019/944.

(14) [demand reduction] Member States should therefore endeavour to reduce their total gross electricity consumption from all consumers including those who are not yet equipped with smart metering systems or devices enabling them to monitor their consumption during specific hours of the day.

(15) To preserve fuel stocks for electricity generation and to specifically target the most expensive hours of electricity consumption, when gas-fired power generation has a particularly significant impact on the marginal price, each Member State should reduce its gross electricity consumption during identified peak price hours.

(16) A binding target of [xxx]% during peak price hours would ensure that Member States address more specifically consumers who can deliver flexibility through demand reduction offers on an hourly basis, including via aggregators, based on the typical electricity consumption profile within peak hours. On average, the electricity consumption over selected peak price hours often exceeds the usual consumption during other peak hours by more than [xxx]%. Therefore, an active electricity demand reduction of at least [xxx]% during selected hours should lead to a reduced gas consumption and to a smoother repartition of demand across hours, impacting hourly market prices.

(17) Member States should have the discretion to choose the appropriate measures to achieve the demand reduction targets so that they can reflect national specificities. When designing electricity demand reduction measures Member States should ensure that such measures are designed so as not to undermine the Union electrification objectives as set out in the Communication on Powering a climate-neutral economy: An EU Strategy for Energy System Integration. Electrification is key to reduce EU dependence on fossil fuels and ensure long-term strategic autonomy of the European Union as this leads to limiting the magnitude of this energy crisis and preventing future energy crisis. Measures to reduce the gross electricity consumption may include national awareness-raising campaigns, publishing targeted information on the forecasted situation in the electricity system, regulatory measures limiting non-essential energy consumption, and targeted incentives to reduce the electricity consumption.

(18) When identifying appropriate demand reduction measures in the peak price hours, Member States should in particular consider market-based measures such as auctions or tender schemes, by which they could incentivise a reduction of consumption in an economically efficient manner. To ensure efficiency and fast implementation, Member States could use existing initiatives and expand existing schemes to develop demand response. The measures taken at national level could also include financial incentives or compensation to market participants affected, if a tangible demand reduction is achieved in addition to potential demand reduction due to the high costs electricity (additionality).

(19) Given the extraordinary surge in electricity prices and the imminent risk of further increases, it is necessary for Member States to immediately establish the measures needed to achieve reductions of the gross electricity consumption in order to facilitate rapid price reductions and to minimise the use of fossil fuels.

(20) In the day-ahead wholesale market, the least expensive power plants are dispatched first but the price received by all market participants is set by the last plant needed to cover the demand, i.e., that with the highest marginal costs, when the market clears. The recent surge in the price of gas and hard coal has translated into an exceptional and lasting increase of the prices at which the gas and coal-fired power generation facilities bid in the day-ahead wholesale market. That in turn has led to exceptionally high prices in the day-ahead market across the Union, as those are often the plants with the highest marginal costs needed to meet the demand for electricity.

(21) Given the role of the price in the day-ahead market as a reference for the price in other wholesale electricity markets, and the fact that all market participants receive the clearing price, the technologies with significantly lower marginal costs have consistently recorded high revenues since the invasion of Ukraine by Russia in February 2022, well above their expectations when deciding to invest.

(22) In a situation where consumers are exposed to extremely high prices which also harm the Union's economy, it is necessary to limit, on a temporary basis, the extraordinary market revenues of producers with lower marginal costs by way of application of a cap for such market revenues achieved through the sale of electricity within the Union.

(23) The level at which the cap on the revenues is set should not jeopardise the ability of the producers, including renewable energy producers, to which it is applied to recover their investment and operating costs and should preserve and incentivise future investments in the capacity needed for a decarbonised and reliable electricity system.

(24) While occasional and short-term peaks on prices can be considered a normal feature in an electricity market and may be useful for some investors to recover their generation investment, the extreme and lasting price increase observed since February 2022 is markedly different from a normal market situation of occasional peak prices. Therefore, the cap should not be set below the expectations of market participants as to the average level of electricity prices in the hours during which the demand for electricity was at its highest, before the invasion of Ukraine by Russia. Before February 2022, the average peak prices in the electricity wholesale market were significantly and consistently expected below [xxx]Euros per MWh across the Union in the last decades, despite the differences in electricity prices between regions in the Union. Since the initial investment decision of market participants was taken based on an expectation that, on average, the prices would be lower than that level during peak hours, setting a cap at a [xxx] EUR per MWh constitutes a level above those initial market expectations and should not counteract the initial assessment of investment profitability.

(25) Moreover, the cap of [xxx] EUR per MWh is consistently higher than the current LCOE for all the relevant technologies, allowing producers to which it applies to cover their investments and operating costs. The cap should therefore not impair the investment in new inframarginal capacities.

(26) The cap should be set on market revenues rather than on total generation revenues (including other potential sources of revenues such as feed-in premium for example), to avoid significantly impacting the initial expected profitability of a project. Regardless of the contractual form in which the trade of electricity may take place, the cap should apply to realised market revenues only. This is necessary to avoid lessening producers who do not actually benefit from the current high electricity prices due to having hedged their revenues

against fluctuations in the wholesale electricity market. Hence, to the extent that existing or future contractual obligations, such as renewable power purchase agreements and other types of power purchase agreements or forward hedges, lead to market revenues from the production of electricity up to the level of the cap, they would not be caught by its application. The measure introducing the cap on revenues should therefore not deter market participants from entering into renewables power purchase agreements. Given the direct benefits that they provide to end-consumers, Member States should continue to promote them, making use of the Commission Recommendation of 18 May 2022 on speeding up permit granting procedures for renewable energy projects and facilitating Power Purchase Agreements as well as practices described in Chapter II of the guidance in the Annex to this Recommendation.

(27) Having a uniform cap on revenues across the Union is necessary to preserve the functioning of the internal electricity market as it would maintain price-based competition across the Union between electricity producers based on different technologies, in particular for renewables.

(28) While applying the revenue cap at the time when transactions are settled may be more efficient, it could not always be possible, for instance due to differences in the way wholesale electricity markets are organised in the Member States and across different timeframes. To account for national specificities and to facilitate the application of the cap on revenues at national level, Member States should have the discretion to decide whether to apply it either when the settlement of the exchange of electricity takes place or thereafter.

(29) Given that the generation mix and the cost-structure of power-generating facilities differ greatly among Member States, they should retain the possibility to further limit the revenues of producers, provided that such measures are compatible with Union law.

(30) The cap on revenues should apply to technologies with marginal costs lower than the cap, such as for instance wind, solar or nuclear energy.

(31) The cap should not apply to technologies with high marginal costs relating to the price of the input fuel necessary to produce electricity, such as gas and coal-fired power plants, as their operating costs would be significantly above the level of the cap and its application would jeopardise their economic viability. To maintain the incentives to overall decrease of the consumption of gas, the cap on revenues should not apply either to technologies which directly compete with gas-fired power plants to offer flexibility to the electricity system and bid in the electricity market based on their opportunity costs, such as demand-response and storage.

(32) The revenue cap should not apply to technologies using as input fuels that are substitutes for natural gas, such as bio-methane, so as not to jeopardise the conversion of existing gas-fired power plants in line with the REPowerEU objectives.

(33) To preserve the incentives for the development of innovative technologies, the cap on revenues should not apply to demonstration projects.

(34) In some Member States, the revenues obtained by some generators are already capped by way of State measures. As such they generators do not benefit from increased revenues resulting from the recent spike of electricity prices. Therefore, existing producers subject to that type of State measures should be excluded from the application of the cap on revenues.

Any new measure should be in line with the principles of the internal market, shall not limit cross-border trade and shall not lead to an increase of gas consumption.

(35) Given that by application of the cap on revenues not all Member States can support their final customers to the same extent, due to circumstances relating to their dependence on imports of electricity from other countries, their geographical and electricity system operation specificities, it is necessary to provide for a possibility for coordinated action by Member States, whereby they may conclude agreements to share the surplus revenues. The surplus revenues can be shared between neighboring Member States based on imports and exports.

(36) Commercial and trading practices as well as the regulatory framework in the electricity sector are markedly different from the fossil sector. Given that the cap aims to mimic the market outcome that producers could have expected if global supply chains would function normally, in absence of the gas supply disruptions since February 2022, it is necessary for this measure to apply to the revenues of producers resulting from the generation of electricity. Conversely, as the temporary solidarity contribution targets the rentability of undertakings active in the oil, gas, coal and refinery sectors which has significantly increased compared to prior years it is necessary for it to apply to their profits.

(37) [retail measures] As the revenue cap does not directly benefit consumers, Member States should ensure that the surplus revenues resulting from its application are passed on to final electricity customers to mitigate the impact of the exceptionally high electricity prices. Final electricity customers include both households and businesses. Without the proposed measures, there is a risk that only wealthier Member States will have the resources to protect their consumers, leading to severe distortions in the internal market.

(38) The revenues from the cap will help Member States to finance measures such as income transfers, rebates on bills, compensating suppliers for supplying below cost, as well investments that would lead to a structural reduction of consumption, in particular from electricity produced from fossil fuel sources. When support is granted to non-household customers, they should commit to undertake to meet a certain share of energy consumption needs by renewable energies, for example through power purchasing agreement or direct investments in renewables generation, or to undertake investments in energy efficiency. The distribution the revenues as set out in this instrument is without prejudice to the application of Article 107 and Article 108 TFEU.

(39) [Solidarity Contribution Part] Without substantially changing their cost structure and increasing their investments, EU companies and permanent establishments generating revenues exclusively in the oil, gas, coal and refinery sector, have seen their profits spike due to the sudden and unpredictable circumstances of the war, reduced supply of energy and increasing demand due to record high temperatures.

(40) The temporary solidarity contribution will act as a redistributing measure to ensure that the undertakings/legal entities which have earned surplus profits as a result of the unexpected circumstances, contribute in proportion to the improvement of the energy crisis in the internal market.

(41) On the basis of available data, the Commission estimates that a [XX%] increase in profits took place in the energy sector in 2021, when comparing those profits with the average profit increase in the period taking place between the fiscal years 2019 and 2020. This roughly

constitutes an amount of X billion euros. An increase of XX% happened in the same period for energy undertakings in the oil, gas, coal and refinery sectors.

(42) Even though this is a rough estimate, the data collected by the Commission show a clear tendency for unexpected profits not resulting from any economic or investment choices by those companies. The Commission estimates that a 5-fold increase in profits of the oil, gas, coal and refinery sectors will happen until the end of 2022.

(43) The basis for calculating the temporary solidarity contributions, are taxable profits of the energy undertakings in oil, gas, coal and refinery sectors as determined in Member States national tax laws for the fiscal year starting on or after 1 January 2022. The Member States, which tax only distributed corporate profits, shall apply the temporary solidarity contribution to the calculated profits irrespective of their distribution. The fiscal year is determined by reference to the rules in place under Member States' national laws.

(44) Only surplus profits in 2022 over a [XX]% increase in comparison to the average taxable profits generated in the three fiscal years starting on or after 1 January 2019 will be subject of the Member States' solidarity contributions.

(45) This approach ensures that part of the profit margin, which is not due to the unpredictable developments in the energy markets following the ongoing illegal war in Ukraine could be used by the energy undertakings concerned for future investment or for ensuring their financial stability during the ongoing energy crisis including for the energy intense industry. This approach to determining the calculation base ensures that the solidarity contributions that Member States would have to introduce are established on a proportional basis.

(46) The solidarity contribution […] should be used for i) financial support measures to households and companies to mitigate the effects of high energy prices; ii) financial support measures to help reducing the energy consumption; iii) financial support measures to support companies in energy intensive industries such as fertiliser production provided that the conditions for transformation are fulfilled iv) financial support measures to develop the energy autonomy of the Union. Surplus profits will be subject to a solidarity contribution at a minimum rate of [XX]%. By proposing a rate at this level a significant part of companies' profits within the scope of this Regulation may not be subject to the solidarity contributions companies to allow those companies to reinvest those profits or to constitute reserves to ensure financial stability throughout this energy crisis. This will depend on whether Member States apply a higher rate.

(47) At the same time this approach of setting a minimum rate ensures that the solidarity contributions are both fair and proportional. Member States remain free to apply a higher rate in case they already introduced a solidarity contribution, levy or tax on surplus taxable profits of the energy undertakings within the scope of this Regulation that would exceed this rate of [XX] % before this Regulation entered into force. This enables such Member States to maintain their preferred rate they deemed acceptable and appropriate under their national legal systems.

(48) The use of the proceeds for those purposes reflects the solidarity contributions' exceptional nature as an instrument that intends to reduce and mitigate the harmful effects of the energy crisis for households and companies across the Union. Member States should in particular target such financial support measures to the most vulnerable households and

companies, which are most affected from the soaring energy prices. Member States are free to decide on the most appropriate form of support measures. The focus shall be on support for both firms and households. This would preserve the price incentive to reduce demand and save energy. In addition, targeting most vulnerable and liquidity-constrained households would have a positive effect on overall consumption (by averting excessive crowding out of spending on non-energy goods) given the high-income propensity to consume for this group of households.

(49) Regular and effective monitoring and reporting to the Commission are essential for the assessment of progress made by the Member States in the achievement of the demand reduction targets, the implementation of the revenue cap and the use of captured revenues, and the application of regulated prices. The Electricity Cross-Border Committee should assist the Commission in monitoring the application and implementation of this Regulation.

(50) Member States should report to the Commission on the introduction of the solidarity contributions in their respective territories, as well as on any amendments they make to such contributions.

(51) Member States should also report on the use of the proceeds arising from the solidarity contributions. In particular, this is to ensure that Member States use the proceeds in line with the usage provided for in this Regulation.

(52) The solidarity contributions and the EU legal framework governing them should be of a temporary nature to address the exceptional and urgent situation that has emerged in the Union with respect to the soaring energy prices. The solidarity contribution will be applicable on a one-off basis to cover surplus profits generated in 2022 to address and mitigate the harmful effects of the current ongoing energy crisis for households and companies

(53) Even though the solidarity contribution is designed to apply to only one fiscal year, the unpredictable nature of the ongoing developments in the energy markets may however reveal the need to extend the application of the Regulation to other fiscal years beyond 2022. Following a review of the situation by the end of the first quarter of 2023, the Commission may propose to the Council, on the basis of a report, whether the application of the framework governing surplus profits should be extended.

(54) Considering the scale of the energy crisis, the level of its social, economic and financial impact and the need to act as soon as possible, this Regulation should enter into force as a matter of urgency on the day following that of its publication in the Official Journal of the European Union.

(55) Given the exceptional nature of the measures set out in this Regulation, and the need to apply them in particular during the winter season 2022-23, the Regulation should apply for a period of one year after its entry into force.

(56) Since the objectives of this Regulation cannot be sufficiently achieved by the Member States, but can rather be better achieved at Union level, the Union may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union. In accordance with the principle of proportionality, as set out in that Article, this Regulation does not go beyond what is necessary to achieve that objective.

HAS ADOPTED THIS REGULATION:

CHAPTER I

SUBJECT MATTER AND DEFINITIONS

Article 1

Subject matter

This Regulation establishes rules for exceptional, targeted and time-limited measures to reduce electricity consumption, to cap the market revenues that certain producers receive from the generation of electricity and redistribute those revenues to final electricity customers to mitigate the effects of the high electricity prices, to enable Member States to apply public interventions in price setting for the supply of electricity for households and small and medium-sized enterprises.

This Regulation also establishes a temporary solidarity contribution for EU companies with activities exclusively in the oil, gas, coal and refinery sectors to contribute to the affordability of energy for households and companies.

Article 2

Definitions

1. For the purposes of this Regulation, the definitions in Article 2 of Directive (EU) 2019/944 and Article 2 of Regulation (EU) 2019/943 apply.

2. The following definitions also apply:

(1) ‘small and medium-sized enterprise’ means an enterprise as defined in Article 2 of the Annex to Commission Recommendation 2003/361/EC[1] ;

(2) ‘gross electricity consumption’ means overall supply of electricity for activities on the territory of a Member State;

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[1] Commission Recommendation 2003/361/EC of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises (OJ L 124, 20.05.2003, p. 36).

(3) ‘reference period’ means the period from 1 November to 31 March in the five consecutive years preceding the date of entry into force of this Regulation, starting with the period from 1 November 2017 to 31 March 2018;

(4) ‘peak price hours’ means hours of the day where day-ahead wholesale electricity prices are expected to be the highest, based on forecasts by Transmission System Operators and Nominated Electricity Market Operators;

(5) ‘market revenue’ means realised income a producer receives in exchange for the sale and delivery of electricity in the Union, regardless of the contractual form in which such exchange takes place, including power purchase agreements and other hedging operations against fluctuations in the wholesale electricity market and excluding any support granted by the State;

(6) ‘settlement’ means a payment that is made and received between counterparties, against delivery and receipt of electricity where applicable, in fulfilment of the counterparties’ respective obligations pursuant to one or more clearing transactions;

(7) ‘competent authority’ means an authority, as defined in Article 2(11) of Regulation (EU) 2019/941;

(8) ‘surplus revenues’ means a positive difference between the market revenues of producers per MWh of electricity and the cap of [xxx] Euros per MWh of electricity;

(9) ‘waste’ means any substance or object which the holder discards or intends or is required to discard, as defined in Article 3 (1) of Directive 2008/98/EC.

(10) ‘net imports of electricity’ means, for the period between 1 January 2021 and 31 December 2021, the difference between the total electricity imports and total electricity exports divided by the total gross production of electricity in a Member State.

(11) ‘fiscal year’ means a tax year, calendar year or any other appropriate period for tax purposes as defined in national law;

(12) ‘customer’ means a wholesale or final customer;

(13) ‘final energy customer’ means a customer who purchases energy for own use;

(14) ‘final electricity customer’ means a customer who purchases energy for own use;

(15) ‘activities in the field of oil, gas, coal and refinery sectors’ means any economic activity performed by an EU company or permanent establishment generating at least 75% of turnover in the field of the extraction, mining, refining of petroleum or manufacture of coke oven products;

(16) ‘surplus profits’ means profits that were generated by undertakings with activities in the field of oil, gas, coal, and refinery sectors due to unpredictable circumstances that lead to a spike in profits, without any particular changes to the cost or investment structure of a given entity. Surplus taxable profits are calculated based on a formula that considers the substantial differences in the profits of entities in the oil, gas, coal, and refinery sectors, when comparing to previous periods.

(17) 'solidarity contribution' means a temporary measure intended to address surplus profits of companies and permanent establishments with activities in the field of oil, gas, coal and refinery sectors to mitigate exceptional price developments in the energy markets for Member States, consumers and companies.

CHAPTER II

MEASURES CONCERNING THE ELECTRICITY MARKET

Section 1

Demand Reduction

Article 3

Reduction of gross electricity consumption

Member States should seek to implement measures to reduce their total monthly gross electricity consumption by [X]% compared to the average of gross electricity consumption in the corresponding months of the reference period.

Article 4

Reduction of gross electricity consumption during peak price hours

1. For every month, each Member State shall identify peak price hours corresponding to a minimum of [xx]% of all hours of the month.

2. Each Member State shall reduce its gross electricity consumption during the identified peak price hours. For every month, the reduction achieved over the identified peak price hours shall reach at least [xx]% on average per hour. The reduction shall be calculated as the difference between the actual gross electricity consumption for the identified peak price hours and the gross electricity consumption forecasted by the transmission system operators, without taking into account the effect of the measures put in place to reach the target set in this Article.

Article 5

Measures to achieve the demand reduction

1. Member States may choose the appropriate measures to reduce gross electricity consumption to meet the targets set in Articles 3 and 4. The measures shall be clearly defined, transparent, proportionate, non-discriminatory and verifiable and shall, in particular:

   (a) be market-based, with compensation where applicable established through an open competitive process, including tenders in which successful bidders receive compensation;

   (b) only involve financial compensation when such compensation is paid for additional electricity not consumed compared to the expected consumption in the hour concerned without the tender;

   (c) not unduly distort competition or the proper functioning of the internal market in electricity;

   (d) not be unduly limited to specific customers or customer groups, including aggregators, in accordance with Article 17 of Directive (EU) 2019/944;

   (e) not unduly prevent the process of replacing fossil fuel technologies with technologies using electricity.

Section 2

Cap on market revenues

Article 6

Mandatory cap on market revenues

1. Market revenues of producers obtained from the generation of electricity from the sources referred to in Article 7(1) shall be capped to a maximum of [xxx] EUR per MWh of electricity produced.

2. Member States shall ensure that the cap targets all the market revenues of producers, regardless of in which market timeframe the transaction takes place and of whether the electricity is traded bilaterally or in a centralised marketplace.

3. Member States shall decide whether to apply the cap on revenues at the settlement of the exchange of energy or thereafter.

4. Without prejudice to paragraph 1, Member States may maintain or introduce measures that further limit the market revenues of producers, provided that these measures are proportionate, do not distort the functioning of electricity wholesale markets, do not jeopardise investment signals, are compatible with Union law and ensure that investment costs are covered.

Article 7

Application of the cap on market revenues to electricity producers

1. The obligation in Article 6 shall apply to the market revenues obtained from the sale of electricity produced from the following sources:

   (a) wind energy;

   (b) solar energy (solar thermal and solar photovoltaic);

   (c) geothermal energy;

   (d) hydropower without reservoir;

   (e) biomass fuel (solid or gaseous biomass fuels), excluding bio-methane;

   (f) waste;

   (g) nuclear energy;

   (h) lignite;

   (i) oil shale; and

   (j) crude oil and other oil products.

2. The cap provided for in Article 6(1) shall not apply to demonstration projects or to producers whose revenues per MWh of electricity produced are capped as a result of State measures.

3. Member States may, notably in cases where the application of the cap provided for in Article 6(1) leads to a significant administrative burden, decide that the cap does not apply to producers generating electricity with power-generating facilities with an installed capacity of maximum 20 kW.

Article 8

Incentives for renewables power purchase agreements

1. Member States shall swiftly remove any unjustified administrative or market barriers to renewables power purchase agreements. They shall take measures to accelerate the uptake

of renewables power purchase agreements, in particular by small and medium-sized enterprises.

2. Member States shall design, schedule and implement support schemes – and guarantees of origin – in such a way that they are compatible with, complement and enable renewables power purchase agreements.

Article 9

Distribution of the surplus revenues

1. Member States shall ensure that all surplus revenues are employed to finance measures in support of final electricity customers that mitigate the impact of high electricity prices on those customers.

2. The measures referred to in paragraph 1 shall be clearly defined, transparent, proportionate, non-discriminatory and verifiable and shall not counteract the reduction obligation of gross electricity consumption in Article 3.

3. The measures referred to paragraph 1 may for example include:

(a) granting a financial compensation to final electricity customers for reducing their electricity consumption, including through demand reduction auctions or tender schemes;

(b) direct transfers to final electricity customers;

(c) compensation to suppliers who have to deliver electricity to customers below costs following a State intervention in price setting pursuant to Article 11;

(d) lowering the electricity purchase costs of final electricity customers for a limited volumes of the electricity consumed;

(e) promoting investments by final electricity customers into renewable and structural energy efficiency investments.

Article 10

Agreements between Member States

In a spirit of solidarity, Member States may conclude agreements to share the surplus revenues.

Such agreements shall be concluded in situations where a Member State’s net imports of electricity are equal or higher than [X]%.

Section 3

Retail measures

Article 11

Temporary extension to small and medium-sized enterprises of public interventions in electricity price setting

Notwithstanding existing EU rules on public interventions in price setting, Member States may apply public interventions in price setting for the supply of electricity to small and medium-sized enterprises. Such public interventions shall

- [be limited to [XX]% of the beneficiary's historical consumption and] retain an incentive for demand reduction]
- be subject to the conditions of Article 5(4) and (7) of Directive (EU) 2019/944
- where relevant, comply with the conditions of Article 12 of this Regulation.

Article 12

Temporary possibility to introduce below cost price regulated prices

Notwithstanding existing EU rules on public interventions in price setting, when applying public interventions in the price setting for the supply of electricity pursuant to Article 5(6) of Directive (EU) 2019/944 or Article 10 of this Regulation, Member States may set a price for the supply of electricity which is below cost provided that all of the following conditions are fulfilled:

1. The measure covers a limited amount of consumption and retains an incentive for demand reduction.
2. There is no discrimination between suppliers.
3. Suppliers are compensated for supplying below cost.
4. All suppliers are eligible to provide offers at the regulated price on the same basis.

CHAPTER III

MEASURES CONCERNING THE OIL, COAL, GAS AND REFINERY SECTORS

Article 13

Mandatory temporary solidarity contribution

1. Surplus profits generated from activities in the oil, gas, coal and refinery sector as defined in Article 2 (11) shall be subject to a temporary solidarity contribution introduced by Member States.

2. Member States shall ensure that existing or planned national measures sharing similar objectives as the temporary solidarity contribution under this Regulation comply with the rules governing temporary solidarity contributions set by this Regulation.

3. The mandatory temporary solidarity contribution referred to in paragraph 1 shall be introduced by Member States at the latest [31] December 2022.

Article 14

Base for calculating the temporary solidarity contribution

For the purpose of calculating the temporary solidarity contribution, Member States shall use the taxable profits, as determined under national corporate income tax rules, of the activity referred to in Article 2 (11) in the fiscal year starting on or after 1 January 2022, which are above [XX]% of the average taxable profits, as determined under national corporate income tax rules, generated in the period [taking place between the three fiscal years starting on or after 1 January 2019. If the average annual result from the period covering the three fiscal years starting on or after 1 January 2019 is negative, the average annual result shall be set to zero for the purpose of calculating the temporary solidarity contribution.]

Article 15

Rate for calculating the temporary solidarity contribution

1. For the purpose of calculating the temporary solidarity contribution, a Member State shall apply a rate of [at least XX%] to the base referred to in Article 14.

2. The solidarity contribution shall apply in addition to the regular taxes and levies which are applicable under each Member State's national laws.

Article 16

Use of proceeds from the temporary solidarity contribution

Member States shall use the proceeds from the temporary solidarity contribution with sufficiently timely impact for the following purposes:

1. financial support measures to final energy consumers, and notably vulnerable households, to mitigate the effects of high energy prices;

2. financial support measures to help reducing the energy consumption such as through demand reduction auctions or tender schemes, lowering the energy purchase costs of final energy customers for limited volumes of consumption, promoting investments by final energy customers into renewable and structural energy efficiency investments;

3. financial support measures to support companies in energy intensive industries such as fertiliser production, provided that they are made conditional upon appropriate investments into renewable energies or energy efficiency.

4. financial support measures to develop the energy autonomy in particular investments in line with REPowerEU objectives notably projects with a cross-border dimension.

5. In a spirit of solidarity between Member States, Member States may assign a share of the proceeds of the temporary solidarity contribution to the common financing of measures to reduce the harmful effects of the energy crisis or to promote investments in energy efficiency and renewable energy including in cross-border projects.

Article 17

Temporary nature of the solidarity contribution

The temporary solidarity contributions adopted by Member States in application of this Regulation shall be of a temporary nature. They shall only apply to surplus profits generated in the fiscal year that started on or after 1 January 2022.

CHAPTER IV

FINAL PROVISIONS

Article 18

Monitoring and enforcement

1. The competent authority of each Member State shall monitor the implementation of the measures referred to in Articles 3, 4, 5, 6, 7 and 11 on its territory.

2. As soon as possible after the entry into force of this Regulation and at the latest by 1 December 2022, Member States shall report to the Commission the planned measures required pursuant to Article 5.

3. By 15 January 2023 and every month thereafter until 15 April 2023, Member States shall report to the Commission on:

   (a) the demand reduction achieved pursuant to Articles 3 and 4 and the measures put in place to achieve the reduction pursuant to Article 5;

   (b) the surplus revenues generated pursuant to Article 6;

   (c) he measures applied to mitigate the impact of high electricity prices on final customers in application of Article 11;

   (d) any public interventions in price setting for electricity referred to in Articles 11 and 12;

4. By 31 March 2023 Member States shall report to the Commission on:

   (a) the introduction of the temporary solidarity contribution and any subsequent amendments to such measures;

   (b) any subsequent amendments to said measure one month of the publication in the national official journal;

5. Member States shall report to the Commission on the use of the proceeds from said measure within one month from the moment the proceeds have been collected by Member States in accordance with national law.

Article 19

Review

By 28 February 2023, the Commission shall carry out a review of this Regulation in view of the general situation of electricity supply and electricity prices in the Union and present a report on the main findings of that review to the Council. Based on that report, the Commission may in particular propose, where it deems it appropriate, to prolong the period of application of this Regulation or amend it otherwise.

By 30 June 2023, the Commission shall carry out a review of this Regulation in view of the general situation of the fossil fuel sector and surplus profits generated and present a report on the main findings of that review to the Council. Based on that report, the Commission may in particular propose, where it deems it appropriate, to prolong the period of application of this Regulation or amend it otherwise.

Article 20

Entry into force and application

1. This Regulation shall enter into force on the day following that of its publication in the Official Journal of the European Union.

2. It shall apply for a period of one year from its entry into force.

3. However, Articles 3, 4, 6 and 11 shall be applied as soon as possible after the entry into force of this Regulation, but not later than 1 December 2022 and until 31 March 2023.

4. This Regulation shall be binding in its entirety and directly applicable in the Member States in accordance with the Treaties.

Done at Brussels,

For the Council

The President