Energy Challenges for European Competition Policy Action

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The first presentation was given by **Celine Gauer** from the European Commission, DG Competition. She talked about the challenges for the energy sector. She identified 3 main issues: high energy prices, security of energy supply and incomplete internal market. To deal with the issues DG Comp has three main tools which include antitrust enforcement, state aid review and mergers control.

While high prices are not a problem by itself, the big problem is that they are higher than in other parts of the world. Partly this is caused by very ambitious climate change policy. Via antitrust enforcement, DG Comp can tackle excessive pricing, when the high prices arise as a result of market power abuse. In the context of energy markets, DG Comp should also ensure the adequate benchmarking. Merger review should prevent the concentration of firms in the energy markets. The state aid can be used several ways to aid the energy prices. First, the renewable energy systems should be better integrated into the market. They have been developed in a system that was not sufficiently interconnected. Also, further innovation should be ensured by ensuring financing for the renewable energy systems. And finally, the system should be flexible enough to accommodate big, energy-intensive enterprises in order not to make them uncompetitive.

The EU is dependent on the energy suppliers and generally suffers from the lack of investments in generation capacity, which is caused by the fact the prices are generally insufficient to cover the expensive investment made into building up capacity. Also, Europe suffers from network foreclosure. DG Comp's antitrust should deal with the foreclosed networks, prevent incumbents from foreclosing the entrants and ensure that diversification of supplies can take place. Merger control should however preserve the incentives to invest and allow for effective development of renewable energy systems (RES).

The main current shortcoming of the internal market is insufficient cross-border competition. In this respect, antitrust should address the territorial restrictions and prohibit discrimination. State aid is an important tool to promote cooperation mechanisms. Also, it needs to be ensured that every national regulator looks not only at the national capacity, but also how it fits in the general picture and whether capacity cannot be imported from elsewhere.

Wolfgang Weber from the BASF Brussels Office said a few words about BASF and its activities. It is active upstream in exploration and production of gas in Russia, Libya and Norway and is also a large energy demand (higher than Denmark). BASF largely produces energy on its own and is generally a minor electricity buyer.

He also mentioned that subsidies should be kept to an absolute minimum and the largest part of innovation has happened in the markets. However, the new policies can make the innovation difficult, particularly the policies that do not correspond with each other. For example, price-control and quantity-control mechanisms make the benefits of regulation obsolete. Now the big question is whether the Commission's decision will really integrate the renewables into the energy markets properly.

As BASF produces most of the electricity on its own, it is less affected by the EC's decisions. However, the demand is not so huge today. Capacity is there, and the question is how to make sure that there is a fair deal between the public and the operators of the capacity installation. There are three ways to deal with increasing renewables. One option is to go into high generation capacity. Another option is to go into storage. And the other way is to deal with the demand side adjustments.

Michael Pollitt from Judge Business School at the University of Cambridge gave the second presentation. He talked about the energy competition from the UK perspective. The main three challenges for the UK are subsidies for energy generation, capacity mechanisms and competition in the retail market.

He described the system of subsidies (Feed-in Tariff with Contract for Difference) and how electricity is purchased at fixed strike price, with the generator paying back the excesses when the spot price overtakes the strike price. Apart from that he described the recent public-private partnership with Hinkley C that was worth $25.6 billion and is expected to provide 3,200 MWh.

He also talked about the capacity mechanisms which should ensure the security of supply and would involve payments for available capacity. However, Michael also pointed out that these are mechanisms and not market outcomes and hence are problematic. For one, EU generators may bid into the capacity markets via interconnectors and have their capacity in different countries.

UK has suffered large price increases in the energy sources gas, coal and heating oils in the recent decade. Meanwhile, Ofgem (British energy regulatory authority) proposes a new bill to simplify the tariff menu and make contracts more transparent in the retail market. However, this regulation might lead to suppliers withdrawing their best contracts. Moreover, it would prevent the development of more sophisticated, more complex contracts. Some have argued instead for a 20 month price freeze.

Overall, many countries seem to suffer from pricing the energy below its real cost. UK's challenges to competition in energy markets lie in three areas: single buyer model for large projects, capacity mechanisms rather than markets and government regulation of retail prices.

Notes by Seriy Golovin