

Consultation of the French Ministry in charge of Energy concerning the new regulatory framework for the marketing of nuclear power production



EFET response – 17 March 2020

We welcome the opportunity provided by the French Government to comment on their ideas for a new regulatory framework for the marketing of nuclear power production.

We generally support the proposal of the Government for the positive impact it should have on the level of liquidity and efficiency in the wholesale traded market. Greater depth and liquidity in the wholesale market will improve conditions for all participants in the French market – both wholesale and supply firms – to the ultimate benefit of end-customers.

While supporting the ARENH evolution, we invite the Ministry to provide a number of clarifications and make some changes to the proposed arrangements. These aim to ensure coherence in the overall regulatory framework, and a true level-playing field between market participants.

1. Do you share the Ministry's assessment on the current regulatory framework for the marketing of nuclear power production?

We generally share the assessment of the Ministry on the purpose and effects of ARENH, although we have some comments on the details of the current arrangements.

The purpose of the ARENH mechanism is quite clear: the establishment of the ARENH mechanism is a direct consequence of the case SA.21918 (C 17/2007) opened by the European Commission's DG Competition in 2007 with regard to the impact of state aid in the form of regulated retail tariffs on competition in the French market. In its decision of 12 June 2012¹, DG Competition considered the ARENH mechanism, enacted via the NOME Act of 2010, as a mitigation measure to favour competition on the French market.

¹ Communication C(2012) 2559 of the European Commission regarding its decision on state aid case N° SA.21918 (C 17/2007) (ex NN 17/2007) regarding regulated electricity tariffs in France, dated 12 June 2012, available at: http://ec.europa.eu/competition/state_aid/cases/220576/220576_1380996_291_2.pdf.

Article 1 of the NOME Act states the purpose of the ARENH mechanism as “to ensure the freedom of choice of electricity supplier while granting the benefit of the competitiveness of the French electro-nuclear fleet to the attractiveness of the territory and all consumers”.

In a 2015 monitoring report of the ARENH mechanism², the French Competition Authority notes that the main added value of the mechanism is to improve competition on the wholesale but especially the retail market. Though the Competition Authority flagged the risk of the mechanism widening the gap between the architecture of the French electricity market model and the energy-only market, it nonetheless supported the mechanism back in 2010 so as to improve competition on the French market.

The conclusions of a CRE report of 2018 on the mechanism are similar, noting minor positive effects on wholesale energy prices, but significant ones on retail competition³.

It is clear for us that, based on all the above, the objective of the ARENH mechanism is primarily to improve competition between market participants on the French retail market. On this, the mechanism has started delivering on its promise, combined with the gradual removal of regulated tariffs for industrial and commercial customers. A more competitive supply market also brings benefits to the wholesale market in terms of greater participation and liquidity.

More recently, the Ministry introduced modifications to the mechanism on the basis of reports from the Auditors Court and CRE, referred to in the consultation document. The Auditors Court and the regulator positioned themselves against the “asymmetric and optional character” of ARENH, which they consider as giving an unfair arbitrage opportunity to alternative suppliers

We commented at length in 2018 on the optional character of the mechanism, and supported the possibility for alternative suppliers to continue optimising their portfolio in the framework of ARENH⁴. We remain of the view that ARENH was never designed as a mechanism that would preclude suppliers from optimising their electricity sourcing on the wholesale market in parallel. With regard to the asymmetric aspect of the mechanism, we would only agree with CRE and the Auditors Court as far as ARENH itself is concerned – which is limited to 100 TWh/year – leaving room for arbitrage opportunities on all sides. **In this sense, we welcome the reform proposal of the Ministry, which shall apply to all the available electricity volumes generated from nuclear energy, and symmetrically expose alternative suppliers and the incumbent to the same opportunities and drawbacks.** We expect this to contribute to improving liquidity and competition on the French market, to the benefit of the end-customer.

² Monitoring report on the ARENH mechanism, dated 18 December 2015, available at: http://www.autoritedelaconcurrence.fr/doc/rapport_arenh.pdf.

³ Impact assessment of the ARENH mechanism between 2011 and 2017, dated 18 January 2018, available at: <http://www.cre.fr/documents/publications/rapports-thematiques/rapport-arenh/consulter-le-rapport>.

⁴ EFET response to the DGEC consultation on possible evolutions of the ARENH mechanism, dated 30 March 2018 and available at: https://efet.org/Files/Documents/Downloads/30032018_EFET%20response%20DGEC%20consultation%20ARENH.pdf.

2. Considering the objectives mentioned above, would a regulatory framework for the marketing of nuclear power production post-2025 be necessary?

For us, **any extension of the regulatory framework should maintain the aim of promoting competition in supply while supporting the evolution of a liquid wholesale market**, in line with applicable European legislation and DG Competition requirements.

In this context, a detailed analysis by the Ministry of where the level of competition on the retail market in France stands compared to similar European markets, and what is the target that the Government would like to reach, would be very useful. The latest CEER retail market monitoring report could serve as a basis for such an analysis⁵. It shows room for improvement in retail competition in France, which could justify the continuation of an ARENH-like mechanism beyond 2025.

On the other hand, **we are surprised of other justifications presented by the Ministry to set up a new regulatory framework development for the marketing of nuclear power production beyond 2025**. These elements seem new and are not mentioned in the NOME act. Most notably, we are concerned with the criticism that French consumers are exposed to a wholesale market price largely determined by the price of fossil-fuelled power generation (including carbon), as well as that of electricity imports. This price would not be representative of the reality of French power generation, and would expose French consumers to the consequences of fuel mix decision made abroad. These considerations seem to forego two basic principles to which France has subscribed to as a member of the internal energy market, and which we are concerned to see challenged by the Ministry: marginal pricing and cross-border markets. These principles do not contradict the objective of helping French consumers benefit from rather cheap energy produced from nuclear energy in France, as the marginal price of electricity in France remains low compared to other EU Member States, partly due to its large, low-operating cost, nuclear fleet. And when the price of electricity in France is set by imports, this means that the price would have been even higher would have France been isolated from other markets.

Concerning **the objective of price stability for consumers, we welcome the approach of the Ministry though we would have liked to see the reform go further**. The regulatory reform proposal would indeed provide all suppliers with a form of price stability on electricity produced from nuclear energy within the price corridor. However, we consider that maintaining regulated retail tariffs would keep an unnecessary second level of price stability. **We therefore reiterate our call on French authorities to do away with regulated tariffs**.

Finally, we support the DGEC objective to incorporate in the new regulatory framework the decarbonisation commitments made by France, including by incentivising demand response. True cross-border, marginal priced markets contribute to sharpening the wholesale price signal. Together with the suppression of retail tariffs, this should help demand response unfold its full potential by exposing consumers to the actual value of

⁵ CEER retail market monitoring report, dated 4 November 2019 and available at: <https://www.ceer.eu/documents/104400/-/-/5c492f87-c88f-6c78-5852-43f1f13c89e4>.

electricity. In this context, the principle of social justice highlighted in the report should of course be upheld, but strictly for those consumers most in need and via measures that do not affect the wholesale or retail market, as per Directive 2019/944⁶.

In conclusion, **we are open to considering a new regulatory framework for the marketing of nuclear power production beyond 2025 to further improve retail competition and support liquidity on the wholesale market in France.** But we would warn the Ministry against establishing this framework as a counterweight to long-agreed principles of the internal electricity market, in contrast with the commitments the French Government took in June 2015 with regard to market prices, market scarcity, and cross-border trading⁷. The Ministry should make sure that the justifications for any new regulatory framework are clear before enacting it, as they will have an impact on the design of the mechanism (see also our answers to question 3 and 4).

3. According to you, which effects would such a regulatory framework have on the functioning of markets?

We understand the proposal of the Ministry as a form of market-making obligation on the side of the incumbent combined with a symmetric compensation mechanism between the incumbent and retail suppliers, defined by a strike price corridor. We understand from the consultation document that the mechanism would apply to all the available electricity produced from nuclear energy in France.

Compared to the current ARENH framework, the new proposal has the advantage of avoiding setting aside large volumes of energy from the market. Currently with ARENH, up to 100 TWh of energy are initially sold outside of the electricity market. **The new proposal would eliminate the ARENH auctions and bring these volumes back to the market.** The volumes of energy concerned by the regulatory framework would be sold on the electricity market according to standard supply and demand fundamentals. We would very much welcome this feature of the new regulatory framework. **It would represent a significant increase in the level of liquidity in the French wholesale market. Increased liquidity will improve the efficient functioning of the market, which should benefit all market participants.** A number of uncertainties remain about the exact model that will be implemented: liabilities from sellers and buyers, information disclosed to the market, way of marketing the volume (auctions vs. continuous, hybrid model), integration in the spot market, etc. **We invite**

⁶ Article 28 of Directive 2019/944: "*Member States shall take appropriate measures, such as providing benefits by means of their social security systems to ensure the necessary supply to vulnerable customers, or providing for support for energy efficiency improvements, to address energy poverty where identified pursuant to point (d) of Article 3(3) of Regulation (EU) 2018/1999, including in the broader context of poverty. Such measures shall not impede the effective opening of the market set out in Article 4 or market functioning and shall be notified to the Commission, where relevant, in accordance with Article 9(4). Such notifications may also include measures taken within the general social security system.*"

⁷ In their Joint Declaration for Regional Cooperation on Security of Supply in the Framework of the Internal Energy Market of 8 June 2015, twelve European governments, including France, stressed that they "*will not restrict cross-border trade of electricity including in times of high prices reflecting market scarcity and [they] will follow EU-regulations on cross-border trade also with respect to ensuring secure system operation*", and that they "*will allow flexible prices; [they] will particularly not introduce legal price caps and [they] will avoid that national measures have the effect of indirect price caps*" (available at: <http://www.benelux.int/files/4414/3375/5898/Jointdeclaration.pdf>)

the Ministry to precise these technical elements. Likewise the timeline for implementation is not defined in the consultation document. Should the Ministry intend to implement the new mechanism before the expiry of ARENH in 2025, this information should be communicated to market participants as soon as possible.

Concerning the strike price corridor, we understand that the proposal foresees both a strike price cap (“*prix plafond*”), above which the incumbent would compensate suppliers of the spread between the cap and the market price, and a strike price floor (“*prix plancher*”), under which suppliers would compensate the incumbent of the spread between the market price and the floor. The strike price cap, on the one hand, would serve a similar purpose as ARENH today, i.e. improving competition by giving retail suppliers an opportunity to purchase energy generated by the historical nuclear fleet of the incumbent below market price. The strike price floor, on the other hand, introduces a second purpose to the mechanism that does not currently exist in ARENH, i.e. providing a minimum return to the incumbent on the energy sold via the mechanism by guaranteeing a minimum price level.

In practice, the strike price floor intended to uphold the new objective of ensuring a minimum return for the nuclear fleet would introduce a form of capacity support in the regulatory framework. **We invite the Ministry to precise in its final proposal how the new regulatory framework would interact with the capacity remuneration mechanism (CRM), so as to ensure that financial support for historical nuclear capacity is only provided once.** For instance, the new regulatory framework could draw on existing rules for the support of renewable power generation, where revenues from the CRM are discounted from renewables feed-in premiums

4. Do you think it appropriate, given the objectives pursued, that this new regulatory framework maintains partial exposure of nuclear power production to the market price, and if so what would be the relevant amplitude for the corridor in €/MWh?

In the new proposal, we welcome the idea of bringing back to the market the volumes currently sold in the separate ARENH auction. Besides the added value of improving liquidity to the wholesale market, it will also expose the concerned volumes to market fundamentals within the strike price corridor.

Regarding the amplitude of the strike price corridor, we invite the Ministry to present more details on its proposal to ensure that the mechanism fulfils its purposes. The price strike floor should reflect the economic conditions of running the nuclear fleet, while the price strike cap should ensure a promotion of competition between all suppliers. We also reiterate our call to clarify how the capacity support objective of the mechanism would not create a form of double capacity remuneration, in addition to the CRM (see our response to Q3). We would only be able to provide a recommendation as to the amplitude of the corridor once all these aspects of the proposal are clear.

5. *Does a mechanism based on financial settlement parallel to the sale of volumes on the market as presented above seem more relevant to you than a physical allocation mechanism?*

If the establishment of a new regulatory framework is indeed warranted (see our response to question 2), **we indeed favour a mechanism of financial settlement**, as proposed by the Ministry. The main value of moving away from the separate physical auction system of ARENH towards a strictly financial compensation mechanism is that it allows bringing the concerned volumes back to the wholesale market, where wholesale transactions for these volumes would not be different from transactions for non-regulated volumes. Once again, a parallel can be drawn with renewable energy support: moving away from power purchase obligations and feed-in tariffs towards direct marketing and feed-in premiums allows for a better inclusion of RES volumes in the market, while avoiding that the financial support mechanism affects the wholesale market. Hence, the **new proposal appears less distortive to the functioning of the market than a physical allocation mechanism**, as currently in place with ARENH.

We would nonetheless welcome clarifications from the Ministry on the prudential aspects of the financial settlement mechanism: since settlement will be performed ex-post, the risk of default/market exit of market participants (incumbent or suppliers) should be factored in in the design of the settlement mechanism. In particular, as the concerned volumes will be transacted in the forward market and the financial settlement would only happen after – possibly long after – these transactions, significant collateral or stringent guarantees would be needed to ensure the financial stability of the mechanism. Therefore, **we invite the Ministry to provide more details in its final proposal on the periodicity of the settlement, and on the prudential rules foreseen**

6. *Since the regulatory framework should guarantee beyond 2025 the protection of consumers against price increases which would be disconnected from the physical reality of French electricity supply by making them benefit from the advantage linked to the investment made in the existing nuclear fleet, while giving EDF the financial capacity to ensure the operation and maintenance of the production tool even in low-cost scenarios, what other devices would you consider suitable to ensure this double protection?*

We refer to our answers to questions 2 to 4. **We are concerned with the idea of the Ministry of wanting to shield consumers from the reality of our cross-border, marginal priced market.** Consumers should not be shielded from market prices unless they are vulnerable, and via measures that do not affect the market, as per Directive 2019/944.

On the capacity support objective of the mechanism, we once again invite the Ministry to present more details on its proposal to ensure that it does not create a form of double capacity remuneration, in addition to the CRM.