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(Announcements)

PROCEDURES RELATING TO THE IMPLEMENTATION OF COMPETITION POLICY

EUROPEAN COMMISSION

STATE AID — POLAND

State aid SA.51502 (2018/N) — Reductions from a capacity mechanism levy for EIUs

Invitation to submit comments pursuant to Article 108(2) of the Treaty on the Functioning of the European Union

(Text with EEA relevance)

(2019/C 200/03)

By means of the letter dated 15 April 2019 reproduced in the authentic language on the pages following this summary, the Commission notified Poland of its decision to initiate the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union concerning the above mentioned measure.

Interested parties may submit their comments on the measure in respect of which the Commission is initiating the procedure within one month of the date of publication of this summary and the following letter, to:

European Commission,
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State Aid Greffe
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These comments will be communicated to Poland. Confidential treatment of the identity of the interested party submitting the comments may be requested in writing, stating the reasons for the request.

Poland has notified reductions for energy intensive users (EIUs) of a levy on electricity supplies financing the Polish capacity mechanism (the 'capacity charge').

The legal basis for the notified measure is the Capacity Market Act of 8 December 2017 and the reductions will be granted by the Energy Regulatory Office. The measure has a duration of 10 years from the date on which the capacity charge starts to be collected.

The measure, as initially notified, was addressed to 52 EIUs with a consumption of at least 100 GWh/year active in sectors included in Annex 3 of the Guidelines on State aid for environmental protection and energy 2014-2020 ⁽¹⁾ (the 'EEAG'). On 5 March 2019, the Polish authorities informed the Commission of their intention to remove this threshold and to amend the Capacity Mechanism Act accordingly. Therefore, the measure will apply to all EIUs who fall into categories specified in Annex 3 of the EEAG and for whom the electro-intensity coefficient of consumption is not less than 3 %.

⁽¹⁾ Communication from the Commission — Guidelines on State aid for environmental protection and energy 2014-2020 (OJ C 200, 28.6.2014, p. 1).

According to the Polish authorities, without the notified reductions, the financing of the capacity mechanism would be unsustainable and the public acceptance to put in place a mechanism to ensure the security of electricity supply would be significantly reduced. In particular, Poland explains that bankruptcy or relocation of EIUs could lead to an erosion of the financial base for the capacity mechanism, exacerbating the burden on other energy consumers and damaging the social acceptance for the mechanism. Therefore, the reductions to the capacity charge would indirectly contribute to ensuring security of supply by diminishing the risk of bankruptcy or relocation of EIUs.

The annual budget of the measure is EUR 287,6 million, as it was initially notified by Poland. However, the budget has not yet been determined following the announced modification of the number of beneficiaries. The TSO is responsible for collecting the capacity charge and it entrusts the payments received from the capacity charge to a public entity, a settlement administrator, which manages these financial resources under the capacity mechanism scheme. Any reduction in the amount of the capacity charge has the effect of reducing the amounts collected from the EIUS and lead to losses in State's revenues. Part of the costs will be ultimately borne by households, by increasing their amount of capacity charge, and the remaining part will be evenly distributed among other electricity consumers, to avoid financing gaps

The level of reductions varies depending on the electro-intensity of the undertaking concerned. The aid intensity will be: 20 % for beneficiaries with an electro-intensity between 3 % and 20 %; 40 % for beneficiaries with an electro-intensity between 20 % and 40 %; and 85 % for beneficiaries with an electro-intensity above 40 % of the amount of electricity taken from the grid and consumed by a given beneficiary during the selected peak hours.

The Commission is of the preliminary view that the reduction in the capacity charge constitutes State aid within the meaning of Article 107(1) TFEU. On the legal basis for the assessment of compatibility, the Commission notes that no guidelines are applicable to reductions to a charge used to finance a capacity mechanism. Thus, the Commission may declare an aid measure compatible directly under Article 107(3)(c) TFEU. At the same time, the Commission considers that the provisions of Section 3.7.2 of the EEAG could be used as guidance in this case. At this stage, the Commission, however, has doubts on whether the notified reductions are needed to secure the financing of the capacity mechanism, and, therefore, on whether they indirectly contribute to the objective of security of supply pursued by the capacity mechanism for the following reasons.

First, the Commission notes that if the costs of security of supply increase to a level that becomes unacceptable for EIUs, then those consumers are in principle free to reduce their consumption to avoid the payments. This is the result of the particular design of the capacity charge that is intended to incentivise industrial customers to shift their electricity demand away from peak times, to moderate demand peaks and alleviate security of supply risks. Second, as regards the notified reductions, the Commission observes that, by being partially exempted from contributing to the financing of the capacity mechanism, EIUs will not face the full cost of the secure electricity they consume, especially in moments of peak demand and scarce supply. As a consequence, the notified reductions may have two negative effects: on the one hand, there is a risk that demand for electricity will be inefficiently higher in periods of scarcity and, on the other hand, the need for extra capacity to ensure secure supply in these periods will be also higher.

The Polish authorities have argued that the consumption pattern of the selected beneficiaries is largely inflexible and that the notified reductions will have, if any, a very limited impact on their behaviour. The Commission however notes that demand for electricity is sensitive to price changes and that cases of complete lack of reaction from demand to prices are exceptional. For this reason, the Commission invites Poland, as well as any interested party, to provide additional evidence in this respect.

TEXT OF LETTER

The Commission wishes to inform Poland that, having examined the information supplied by your authorities on the aid/measure referred to above, it has decided to initiate the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union.

1. PROCEDURE

1. On 26 June 2018, the Polish authorities notified a scheme providing for reductions to energy-intensive users (EIUs) from the capacity mechanism levy.
2. The Commission sent to the Polish authorities requests for information on 24 August 2018, 5 December 2018, and 25 February 2019.
3. The Polish authorities submitted their replies on 5 October 2018 and 10 January 2019, and 5 March 2019.
4. By letter dated 5 March 2019, Poland agreed exceptionally to waive its rights deriving from Article 342 TFEU in conjunction with Article 3 of Regulation 1/1958 ⁽¹⁾ and to have the present decision adopted and notified in English.

2. DESCRIPTION**2.1. The Polish capacity mechanism**

5. On 7 February 2018, the Commission decided not to raise objections to the Polish capacity mechanism (the 2018 Commission decision in case SA.46100) ⁽²⁾. This scheme addresses the issue of the future generation adequacy on the Polish electricity market. It is designed as a capacity market where the Polish Transmission System Operator (TSO), Polskie Sieci Elektroenergetyczne (PSE), is entrusted to organise centrally-managed auctions to procure the level of capacity required to ensure security of electricity supply. The auctions are open to existing and new power generators, demand side response (DSR) and storage operators, located in Poland or in the control area of neighbouring EU TSOs. The first main auction was organized on 15 November 2018 for the delivery year 2021. During this auction power generation operators committed to make available 22.4 GW by means of capacity contracts. The overall costs amount to approx. EUR 1,15 billion (i.e. EUR 50.91/kW/year).
6. The introduction in Poland of the capacity market is further accompanied by several electricity market reforms. In particular, by 1 January 2021, Poland will make sure that DSR is eligible to participate in the wholesale electricity markets (including day-ahead and intra-day) as well as the balancing market and will be treated in a similar way as other market participants and balancing service providers. DSR can be represented either individually (in particular by large consumers) or via aggregators.
7. Poland further committed to introduce reforms to ensure that Polish electricity prices in future rise to reflect the value of electricity at times of scarcity in Poland, including an administrative scarcity pricing mechanism ⁽³⁾.
8. Currently, DSR only plays a relatively limited role in the overall Polish electricity market (in the last DSR specific auction in 2017, the TSO procured approx. 200 MW of capacity). The market reforms referred to in recitals 6 and 7 should increase the role of DSR in Poland in future.

2.2. The capacity charge

9. The Polish capacity mechanism will be financed through a parafiscal levy (the “capacity charge”) on electricity supplies to be levied from 1 October 2020.
10. The capacity charge will be included in the transmission or distribution tariff and collected by the TSO. It will be imposed on of the following entities: final electricity customers connected directly to the transmission grid, electricity distribution system operators, an energy sector undertaking performing economic activities in scope of transmission or distribution of electricity connected directly to the transmission grid and an energy sector undertaking generating electricity and connected directly to the transmission grid. The Polish authorities explained that the charge will be ultimately paid by final electricity customers (see Article 69 (3) of the Capacity Market Act of 8 December 2017) ⁽⁴⁾. The amount of the charge will be dependent on the electricity consumption of the entities from whom the capacity charge will be collected and will be imposed on electricity consumed in Poland regardless of its origin (i.e. including electricity produced outside of Poland) ⁽⁵⁾.

⁽¹⁾ Regulation No 1 determining the languages to be used by the European Economic Community (OJ 17, 6.10.1958, p. 385).

⁽²⁾ Commission decision in case SA.46100 (2017/N) – Poland – Planned Polish capacity mechanism, OJ C/462/2018, 21.12.2018.

⁽³⁾ Decision in case SA.46100, recital 16(e). Following these reforms, the prices can rise up to the maximum price in the CACM network code, which is 9,999 EUR/MWh.

⁽⁴⁾ Journal of Laws 2018, item 9. The Act is available at: <http://prawo.sejm.gov.pl/isap.nsf/DocDetails.xsp?id=WDU20180000009>

⁽⁵⁾ Please see Section 2.5 of the 2018 Commission decision in case SA.46100

11. The Polish authorities explained that the capacity charge will be determined as follows (see Article 70 (1) of the Capacity Market Act):
 - For households: a monthly rate on the basis of the annual electricity consumption;
 - For all other electricity end consumers: a rate applied to the volume of electricity consumed from the network, during expected high demand hours (expressed in zloty per kWh).
12. The Polish authorities explained that the methodology for imposing the capacity charge on the second category of consumers is intended to minimise the size of the capacity mechanism by incentivising those consumers to shift their consumption away from high demand hours and thus reduce the risk of system stress.
13. The Polish regulator, the President of the Energy Regulatory Office (the ERO) publishes in the URE bulletin by 30 September each year the rates of the capacity charge for the next year, and the selected hours of the day falling within the hours of peak demand for power in the system, set separately for each quarter of the supply year, for the purpose of calculating the capacity charge due from customers other than households.

2.3. Objective and beneficiaries of the measure

14. The present notification concerns a scheme providing for reductions of the capacity charge for EIUs.
15. According to the Polish authorities, without the notified scheme, the financing of the capacity mechanism would be unsustainable and the public acceptance to put in place a mechanism to ensure the security of electricity supply would be significantly reduced. In particular, Poland explains that bankruptcy or relocation of large electro-intensive undertakings could lead to an erosion of the financial base for the capacity mechanism, exacerbating the burden on other energy consumers and damaging the public acceptance for the mechanism. Therefore, the reductions of the capacity charge would indirectly contribute to ensuring security of electricity supply.

2.3.1. Beneficiaries

16. The notified reductions scheme will be granted to EIUs active in sectors included in Annex 3 of the Guidelines on State aid for environmental protection and energy 2014-2020 (the “EEAG”) ⁽⁶⁾.
17. Initially, the Polish authorities notified the reductions only for 52 largest EIUs whose energy consumption exceeds a threshold of 100 GWh/year. On 5 March 2019 the Polish authorities informed the Commission of their intention to remove this threshold and to amend the Capacity Mechanism Act accordingly. Therefore, the measure will apply to all EIUs who fall into categories specified in Annex 3 of the EEAG and for whom the electro-intensity coefficient of consumption is not less than 3 %.
18. The Polish authorities have indicated that the majority of EIUs who will be entitled under the scheme as originally notified are consumers connected to the high and the extra high voltage grid. In Poland, those consumers are included in the tariff group “A”, which is characterised by a stable power demand throughout the day and the year. The share of consumption in peak hours of those consumers amounts to approximately 43 % of peak demand.

2.3.2. Arguments provided by Poland on the possibility by EIUs to lower electricity consumption in peak hours

19. The Polish authorities have confirmed that EIUs could avoid paying the capacity charge by shifting their electricity consumption away from peak hours, however, they have explained that this behaviour is unlikely to be possible in practical terms. According to the Polish authorities, if EIUs lower their electricity production at peak hours, that would result in production loss the cost of which cannot be offset by shifting consumption to different hours for the following reasons:
 - a. The EIUs often operate at full or close to full capacity, which is reflected in their around-the-clock work schedule. This depends on the capital-intensive nature of EIUs, combined with the very competitive environment in which they operate.
 - b. For energy efficiency reasons, it is very costly to interrupt and resume the production for a period of few hours. For example, an interruption of the steel production would result in loss of heat, which in turn increases the electricity consumption for the next few hours by roughly 10 %. Stopping production and moving it to other hours in some cases may cause critical damage of production systems.
 - c. Most of the production lines (e.g. steel, copper, chemistry, and especially mining industry) are built around the assumption of continuous operation, not only because of the related technical and safety risks for equipment and labour.

⁽⁶⁾ Communication from the Commission — Guidelines on State aid for environmental protection and energy 2014-2020, OJ C 200, 28.6.2014, p. 1-55

20. The Polish authorities have also provided an analysis of estimated Value of Lost Load (VOLL) ⁽⁷⁾ for EIUs, which is estimated at 7 670 PLN/MWh, which is significantly below the average VOLL of the entire economy (76 530 PLN/MWh). However, the VOLL of EIUs still exceeds considerably the cost of electricity supply as calculated by Poland in Table 1 below.

Table 1

Electricity costs for EIUs (PLN/MWh)			
	Average	Peak	Off-peak
BASE 2019 (TGE)	284,49	351,85	217,13
Distribution	38,44	61,41	15,46
Other regulatory	38,00	38,00	38,00
Total	360,93	451,26	270,59

21. According to the Polish authorities, the high difference between the electricity costs at peak hours and the VOLL of EIUs explains why EIUs are not willing to reduce or shift their consumption away from those hours. The Polish authorities also argue that that will not change as a result of the additional capacity charge that will be imposed as of October 2020. The average value of the capacity charge calculated under the assumption that the total amount of electricity consumed is subject to the capacity charge has been estimated by the Polish authorities at 45 PLN/MWh on the basis of the recently concluded auctions for the delivery periods in 2021-2022 and the estimated results of future additional auctions in 2020-2021. Since non-households consumers will pay only on the electricity taken off the grid and consumed during selected hours of the day, which are not yet determined, the Polish authorities have provided a simulation of the amount of the capacity charge imposed only on those peak hours, which is estimated at 89 PLN/MWh. That increase of the total cost of electricity would still be below the VOLL of EIUs and would therefore not incentivise them to shift their stable electricity consumption away from the majority of historic peak hours.
22. The Polish authorities added that the above-mentioned arguments are further demonstrated by the fact that in spite of already existing incentives to shift production to off-peak hours few companies are interested in providing DSR in Poland. The incentives apply to electricity prices on the wholesale market and electricity distribution costs. Most industrial customers use the A23 distribution tariff, which differentiates rates for peak and off peak demand hours. Despite the existing incentives, the electricity demand profile of EIUs is constant throughout the day.
23. The Polish authorities have explained that in the first main capacity auction which occurred in December 2018, only 18 winning offers were submitted by DSR units out of 160, with a total volume of capacity obligations offered of approximately 600 MW (around 2,7 % of the total volume of capacity obligations for the delivery period in 2021). All of those DSR units are unconfirmed, which means that they have not yet performed the mandatory capacity reduction test aimed at verifying their ability to respond to a stress event ⁽⁸⁾. Out of the 18 offers, 16 were submitted by DSR aggregators, and only 1 offer by an EIU for an offered capacity of only 10 MW ⁽⁹⁾. Similarly, the participation of EIUs and DSR aggregators in the Guaranteed Program of Emergency DSR (Gwarantowany Interwencyjny Program DSR) currently run by PSE S.A. is also limited. In 2017, 9 companies applied with offers ranging between 3 000 PLN and 13 777 PLN per 1 MWh of actual reduction (on top of the availability fee they also receive). In 2018, 10 companies applied with offers ranging between 10 000 PLN and 13 815 PLN per 1 MWh of actual reduction.
24. Poland submits that because of the reasons explained above the possibility of industrial electricity consumers to shift their production in order to avoid the obligation to pay the capacity mechanism charge will be very limited.

2.3.3. Capacity charge reductions

25. The level of reductions varies depending on the electro intensity of the undertaking. The reductions rates will be:
- 20 % for beneficiaries with an electro-intensity between 3 % and 20 %,
 - 40 % for beneficiaries with an electro-intensity between 20 % and 40 %, and
 - 85 % for beneficiaries with an electro-intensity above 40 %

of the amount of electricity taken from the grid and consumed by a given beneficiary during the selected peak hours (see Article 70 (3) of the Capacity Market Act) ("the basis for calculating the capacity charge").

⁽⁷⁾ The value of lost load (VOLL) expresses the value attached by consumers to uninterrupted electricity supply.

⁽⁸⁾ For more information, see recitals 27 and 28 of the 2018 Commission decision in case SA.46100.

⁽⁹⁾ According to Poland, the price of 240 320 PLN/MWh covering both the availability to perform the reduction as well as the actually reduction was probably insufficient to cover the fixed and operating costs of DSR units.

2.4. Legal basis, duration, financing, and budget

26. The legal basis for the notified scheme is the Capacity Market Act of 8 December 2017 ⁽¹⁰⁾.
27. The scheme is notified for a period of 10 years from the date on which the capacity charge starts to be collected, namely from 1 October 2020 (see recital 9 above). The Polish authorities have also confirmed that should the measure continue to apply after that period, it will be re-notified.
28. The Polish authorities have confirmed that the scheme will not enter into force before it has been approved by the Commission.
29. As regards the financing of the scheme, the Polish authorities explained that part of the costs will be ultimately borne by households, by increasing their amount of capacity charge, and the remaining part will be evenly distributed among other electricity consumers, to avoid financing gaps.
30. As explained in recital 17, the measure was initially addressed to 52 EIUs with largest energy consumption in Poland covering 43 % of peak demand. On 5 March 2019 Poland has communicated that it intends to abolish the threshold of 100 GWh/year energy consumption. Therefore, the estimated number of beneficiaries would be between 300 and 350.
31. The annual budget of the scheme, as it was initially notified by Poland, is EUR 287,6 million. However, the budget has not yet been determined following the announced modification of the number of beneficiaries.

2.5. Other elements

2.5.1. Transparency

32. The Polish authorities have confirmed that the transparency requirements set out in paragraphs 104 to 106 of the EEAG and the reporting and monitoring requirements referred to in Part 6 of the EEAG will be complied with respect to the reductions for EIUs.

2.5.2. Cumulation

33. The Polish authorities have confirmed that the reductions granted under the notified scheme cannot be cumulated with other types of aid to cover the same eligible costs, namely the capacity charge.

2.5.3. Firms in difficulty

34. The Polish authorities have committed not to grant reductions from the capacity charge to an undertaking in difficulty.

2.5.4. No new aid as long as past incompatible aid has not been recovered

35. The Polish authorities committed to not grant reductions from the capacity charge to an undertaking, which has benefitted from an earlier unlawful aid that was declared incompatible by a Commission Decision, until that undertaking has reimbursed the total amount of unlawful and incompatible aid and the corresponding recovery interest.

3. ASSESSMENT

3.1. Existence of aid

36. A measure constitutes State aid in the meaning of Article 107(1) Treaty on the Functioning of the European Union (the “TFEU”) if it is “aid granted by a Member State or through State resources in any form whatsoever, which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods [...] in so far as it affects trade between Member States”.
37. In determining whether a measure constitutes State aid within the meaning of Article 107(1) of the Treaty, the Commission has to verify whether the measure ⁽¹¹⁾:
 - confers an advantage on certain undertakings or certain sectors (selective advantage);
 - is imputable to the State and involves State resources;
 - distorts or threatens to distort competition; and
 - is liable to affect trade between Member States.

⁽¹⁰⁾ Journal of Laws 2018, item 9. The Act is available at: <http://prawo.sejm.gov.pl/isap.nsf/DocDetails.xsp?id=WDU20180000009>

⁽¹¹⁾ See judgment of 21 December 2016, *Commission v World Duty Free Group and Others*, C-20/15 P and C-21/15 P, EU:C:2016:981, paragraph 53 and the case-law cited.

3.1.1. *Selective advantage*

38. By limiting the basis for calculating the capacity charge to the range between 20 % and 85 % depending of the electro-intensity of the EIUs the scheme reduces the burden the undertakings qualifying as EIUs would normally have to bear without the reductions. Therefore, the Commission concludes that the measure constitutes an advantage.
39. The Commission concludes that the advantage is also selective, as it applies only to EIUs active in sectors included in Annex 3 of the EEAG.

3.1.2. *State resources and imputability*

40. According to settled case-law, only advantages which are granted directly or indirectly through State resources are to be regarded as aid within the meaning of Article 107(1) TFEU. The distinction between aid granted by the State and aid granted through State resources serves to bring within the definition of aid not only aid granted directly by the State, but also aid granted by public or private bodies designated or established by the State⁽¹²⁾. Thus, resources do not need to transit through the State budget to be considered as State resources. It is sufficient that they remain under public control⁽¹³⁾.
41. As results from established case-law and constant Commission decisional practice, proceeds of levies imposed by the State, which are then managed and apportioned by a public or private body in accordance with the provisions of the domestic legislation, constitute State resources⁽¹⁴⁾.
42. The reductions from the capacity charge are imputable to the State, as they are established by law, the Capacity Market Act. Poland has established the rules for calculation of the capacity charge in Article 70 of the Capacity Market Act. Pursuant to Article 69 (1) of the Capacity Mechanism Act, the TSO, a 100 % State-owned entity, is responsible for collecting the capacity charge. The TSO entrusts the payments received from the capacity charge to a public entity, a settlement administrator, which manages these financial resources under the capacity mechanism scheme. Furthermore, the administration of the reductions is also imputable to the State, as the eligible EIUs submit an application to the ERO, which verifies the request, and finally grants the reductions to them.
43. As stated in the 2018 Commission decision in case SA.46100⁽¹⁵⁾, the capacity mechanism is financed from State resources. Any reduction in the amount of the capacity charge has the effect of reducing the amounts collected from the consumers concerned and lead to losses in State's revenues.
44. The reduction of the capacity charge thus involve State resources. The Commission observes in particular that the State can control, direct and influence the administration of the capacity charge reductions at stake: the State intervenes both at the level of the advantage and its financing. The State has defined in legally binding provisions to whom the advantage is to be granted, the eligibility criteria and the level of support, but it has also determined the financial resources to cover the costs of the support (in form of the increased costs for the remaining consumers not fulfilling the definition of an EIU).

3.1.3. *Effect on trade and impact on competition*

45. The beneficiaries are active in sectors with high international trade exposure (like chemical, fertilizers, cement or aluminium production), and as such, the Commission concludes that the measures at stake are likely to distort the competition on the markets, in which they are active, and affect trade between Member States.

3.1.4. *Conclusion*

46. For the reasons set out in sections 3.1.1 to 3.1.3 above, the Commission concludes that the reduced capacity charge constitutes State aid within the meaning of Article 107 (1) TFEU.

3.2. **Lawfulness of the aid**

47. Poland has notified the scheme providing for reductions for EIUs from the capacity charge and has subjected its implementation to the approval by the Commission. Poland has thus fulfilled its obligations under Article 108 (3) TFEU (see Article 104 (2) of Capacity Market Act).

⁽¹²⁾ To this effect, see case C-78/76 March 1977 *Steinike & Weinlig* EU:C:1977:52, paragraph 21, joined cases C-72/91 and C-73/91 *Sloman Neptun* EU:C:1993:97, paragraph 19, and the case-law cited in the EEG 2014 Decision, paragraph 81.

⁽¹³⁾ See case C-482/99 *France v Commission* EU:C:2002:294, paragraph 37, and the case-law cited, in the EEG 2012 Decision, paragraph 83.

⁽¹⁴⁾ See case C-262/12 *Vent de Colère* EU:C:2013:851, paragraph 25.

⁽¹⁵⁾ See recital 117 of the 2018 Commission decision in case SA.46100.

3.3. Compatibility of the aid

48. The Commission may declare State aid compatible with the internal market. In order to determine the applicable compatibility assessment rules, the Commission observes that the objective of the capacity charge is to ensure the financing of the Polish capacity mechanism ⁽¹⁶⁾. The reason for the introduction of the Polish capacity mechanism is to ensure a level of electricity capacity, which is deemed adequate to meet demand levels in Poland ⁽¹⁷⁾. Therefore, in contrast to environmental taxes within the meaning of paragraph 167 and point 19(15) of the EEAG ⁽¹⁸⁾, the capacity charge does not aim to increase the level of environmental protection, but predominantly to ensure security of electricity supply in Poland.
49. The Commission also notes that the particular methodology for calculating the capacity charge on all consumers except for households is intended to minimise the size of the capacity mechanism by incentivising those consumers to shift their electricity consumption away from high demand hours and thus reduce the risk of system stress (see recitals 11 and 12 above). Although that methodology aims to change the behaviour of those electricity consumers and can therefore be considered to have a behavioural steering effect, that consideration does not change the objective of the capacity charge, which is to ensure the financing base for the Polish capacity mechanism and contribute to the security of electricity supply.
50. Therefore, the Commission preliminarily concludes that the capacity charge does not qualify as an environmental tax as defined in the EEAG (see paragraph 19(15) of the EEAG).
51. The aid scheme under assessment concerns reductions of capacity charge. Reductions of capacity charges are not foreseen in the EEAG and no other Commission guidelines are applicable to reductions of a parafiscal charge aiming at financing a capacity mechanism.
52. However, in such a case, the Commission may declare an aid measure compatible directly under Article 107(3)(c) TFEU if it pursues an objective in the common interest, is necessary and proportionate and if the positive effects of the common objective outweigh the negative effects on competition and trade ⁽¹⁹⁾. The Commission also notes that this is the first time the compatibility with the internal market of the reductions for EIUs from capacity charges is being assessed.
53. The Commission considers that the conditions for compatibility with the internal market under Article 107(3)(c) TFEU are met if the measure satisfies the following conditions: (i) it aims at an objective of common interest ⁽²⁰⁾; (ii) it is necessary to attain the objective of common interest pursued; (iii) is appropriate (iv) it has an incentive effect; (v) it is proportional to the needs based on which it is deployed; and (vi) it does not unduly distort competition and trade between Member States.

3.3.1. Objective of Common Interest

54. As referred to in recital 15 above, Poland submits that the reductions for EIUs from capacity charge are necessary to maintain a stable financing basis for the capacity market, and hence contribute to the achievement of the objective of ensuring the security of electricity supply. According to Poland, an exposure of the EIUs to the full capacity charge would put the EIUs at a significant competitive disadvantage, which would result in the bankruptcy or delocalisation of undertakings liable to pay capacity charge using significant amounts of electricity and thus would undermine the public acceptance of the capacity mechanism.
55. Since the capacity charge is dedicated to the funding of capacity mechanism, it therefore indirectly contributes to the achievement of the objectives pursued by the latter, namely generation adequacy, which is an objective of common interest under section 3.9. of the EEAG. The Commission has found in its 2018 decision in case SA.46100 that the Polish capacity mechanism pursues an objective of common interest by contributing to generation adequacy / ensuring security of supply ⁽²¹⁾.
56. On the basis of the information available at this stage, the Commission however has doubts on whether the notified scheme contributes to the objective of ensuring security of electricity supply / generation adequacy pursued by the capacity mechanism, for the reasons explained below.
57. First, the Commission notes that the beneficiaries of the scheme can choose to pay for the level of security of supply they prefer as they are liable to pay the capacity charge only if they consume electricity in selected peak hours (see recitals 11 and 12 above), and are charged only for the electricity they consume. To the extent they have a lower need for security of electricity supply and therefore a lower VOLL, they can also sell their ability to reduce demand as DSR in the capacity mechanism ⁽²²⁾. Therefore, if the costs of security of electricity supply increase to a level that becomes unacceptable for EIUs, then they are in principle free to optimise their electricity consumption in order to reduce the payment of the capacity charge. This would reduce the demand for electricity and thus the necessary size (necessary capacities to be made available) of the capacity mechanism. The current capacity charge design is intended to incentivise industrial customers to shift their electricity demand away from the peak hours ⁽²³⁾, to moderate demand peaks and thus alleviate security of supply risks.

⁽¹⁶⁾ See also Article 69 of the Capacity Market Act.

⁽¹⁷⁾ See also the 2018 Commission decision in case SA.46100, recitals 142 and 143. See also Article 1 of the Capacity Market Act.

⁽¹⁸⁾ Communication from the Commission — Guidelines on State aid for environmental protection and energy 2014-2020, OJ C 200, 28.6.2014, p. 1-55

⁽¹⁹⁾ See Case T-177/07, *Mediaset/Commission*, paragraph 125, EU:T:2010:233; case T-356/15, *Austria/Commission*; EU:T:2018:439, paragraph 83.

⁽²⁰⁾ Case T-162/06 *Kronopoly v Commission* EU:T:2009:2, especially paragraphs 65, 66, 74 and 75.

⁽²¹⁾ See footnote 2 above.

⁽²²⁾ The overall effect of these incentives in the electricity market and capacity mechanism should be that consumers pay for the level of security of supply that they require. Since theoretically the capacity mechanism is only needed to the extent that consumers wish to pay for security of supply, its financing base is in principle dynamic and should automatically adjust to match the need for (and size of) the measure.

⁽²³⁾ See recital 50 above.

58. Second, the Commission observes that the notified scheme provides for reductions of up to 85 % of the full amount of the capacity charge for EIUs, and therefore the latter will not pay the full costs of the availability of electricity they consume, especially in moments of peak demand and scarce supply. In fact, the key aspect of the current design of the capacity charge is to amplify the difference between the higher cost of electricity in peak hours (higher wholesale price plus the charge) and the lower cost in non-peak hours (lower wholesale price and no charge). The reductions from the capacity charge would reduce this difference and may consequently lower the incentives towards efficient consumption patterns ⁽²⁴⁾.
59. In the same vein, the reductions might also lower the above-mentioned incentives for the beneficiaries to participate in the electricity market and in the capacity mechanism as remunerated DSR.
60. As a consequence, the notified reductions might have two negative effects on the objective of common interest pursued (security of electricity supply): on the one hand, there is a risk that demand for electricity will be inefficiently higher in periods of peak hours /capacity scarcity and, on the other hand, that the need for extra capacity to ensure secure supply in these periods will be also higher. Thus, the reductions for EIUs might increase the need for more capacities to be auctioned and ultimately the size and the costs of capacity mechanism.
61. As regards the above-mentioned concerns, the Polish authorities have argued that the consumption pattern of the EIUs that would benefit from the measure is largely inflexible and that the notified reductions will have, if any, a very limited impact on their behaviour (see paragraph 2.3.2 above). This statement is consistent with the data provided by Poland showing that the VOLL of EIUs is significantly above the total cost of electricity including the capacity charge ⁽²⁵⁾. This evidence seems to suggest that those EIUs value the provision of secure electricity more than the amount of capacity charge that they would face.
62. On the other hand, the Polish authorities have also explained that some beneficiaries have a relatively low VOLL compared to other consumers (ten times lower than the average consumer) and will be at significant competitive disadvantage if required to pay the full cost of ensuring secure electricity supplies.
63. In light of the considerations above the Commission has doubts about the consistency of the arguments of the Polish authorities and therefore invites the Polish authorities to provide further clarifications on this issue.
64. The Commission further notes that demand for electricity, as for most products and services, is sensitive to price changes. While the price elasticity of the demand can vary significantly across products, markets and customers, cases of complete lack of reaction from demand to prices are exceptional. For an industrial electricity customer, the price elasticity of its demand for a certain productive input is likely to be related to the weight of that input in its cost structure. The larger the weight of a certain input, the stronger the incentive to take into account its cost when structuring the production process and hence the more responsive its demand will be to the price of that particular input.
65. In the case of EIUs, electricity can be considered as a particularly important production input. EIUs' demand for electricity would thus in principle tend to be relatively elastic to electricity price and they would have higher incentives to optimise their production schedules accordingly. There may be in certain cases some technical limits to shifting production and electricity consumption, which may imply that the electricity consumption is not fully flexible. However, given that the beneficiaries account for a significant share of peak consumption, their shifts of consumption can be also significant even when their consumption is not fully flexible.
66. The Commission therefore considers that to assess the extent of a potential effect of the notified reductions scheme on the beneficiaries' behaviour, more detailed empirical data and a thorough assessment of these considerations is needed. For this reason, the Commission invites Poland, as well as any interested party, to provide comments and additional evidence in this respect. That data also appear necessary to justify the number of EIUs that will benefit from the measure. At this stage, the Commission does not have sufficient elements to conclude on whether the scope of the measure is justified.
67. Finally, the Commission notes that Poland has also confirmed that some EIUs have successfully participated in the introduced Guaranteed Program of Emergency DSR and some DSR units have also successfully participated in the first auctions for the capacity mechanism in November and December 2018. However, the Commission does not have information on possible unsuccessful bids. Even if at the moment that participation is low ⁽²⁶⁾, this may indicate that some EIUs might have differing individual VOLLs and will react appropriately to the incentives provided by full exposure to the costs – in terms of both capacity and electricity prices – of providing secure electricity supplies, particularly when market reforms enabling appropriate scarcity pricing have been implemented (see recital 6 above) ⁽²⁷⁾. The Commission notes that potential scarcity prices after these reforms (see recital 7 and footnote 3 above) should far exceed the demand response activation offers received in the 2017 Guaranteed Program of Emergency DSR (see recital 23 above).

⁽²⁴⁾ As explained in recital 26, Poland suggests this incentive exists for other consumers, but not for the proposed EIU beneficiaries of the measure.

⁽²⁵⁾ A high VOLL also seems to be implied by the arguments presented by Poland on the alleged inability of EIUs to reduce their demand for electricity because of, among other things, the potential for 'critical damage of production systems' and 'risks for equipment and labour', which potentially may have very significant consequences for EIUs.

⁽²⁶⁾ In this respect, the Commission observes that the insufficient development of a flexible demand side is one of the main reasons capacity mechanisms are required and the Final Report of the Sector Inquiry on Capacity Mechanisms identified the importance of ensuring incentives for the development of DSR.

⁽²⁷⁾ Moreover, the fact that the Capacity Mechanism Act already contains provisions concerning the envisaged reductions for EIUs (which create certain expectation on the side of the EIUs) makes it more difficult to assess to willingness of the EIUs to participate as DSR in the capacity market based on the empirical data from the first three auctions.

68. At this stage, for the reasons explained above, the Commission doubts as to whether it can be considered that the notified scheme pursues an objective of common interest. In fact, at this stage, the Commission does not have the necessary evidence to conclude on whether the notified reductions would actually have an impact on the beneficiaries' incentives for efficient electricity consumption. In particular, the Commission welcomes any data on possible unsuccessful bids that the EIUs made in the context of the capacity auctions as demand response or in the context of the guaranteed programme of emergency DSR, and any data on the participation of comparable EIUs in interruptibility schemes. Moreover, the Commission cannot take a final position on whether, in the absence of the notified reductions from the capacity charge, the beneficiaries would not be able to sustain the capacity charge in full. The Commission therefore invites Poland and other interested parties to submit comments on this point.

3.3.2. *Need for State intervention, appropriateness of aid, incentive effect, proportionality and no undue distortion of competition*

69. The Polish capacity mechanism will be financed through a capacity charge on electricity supplies. The capacity charge will be calculated for households as a monthly rate on the basis of the annual electricity consumption and for all other consumers as a rate applied to the volume of electricity consumed from the network, consumed during expected high demand hours. The latter is designed to minimise the size of the capacity mechanism by incentivising those industrial consumers to shift their consumption away from high demand hours and thus reduce the risk of system stress.
70. Should the notified scheme pursue an objective of common interest, the necessity of the notified reductions scheme must also be demonstrated. In particular, it needs to be established that it is effectively targeted to address the market failure identified by the Member State ⁽²⁸⁾.
71. In this case, Poland has introduced the capacity charge to finance the capacity mechanism, which addresses the issue of the future generation adequacy. As concluded in the 2018 Commission decision in case SA.46100, the Polish authorities have demonstrated, by way of the probabilistic adequacy assessment, that capacity in the Polish market is expected to suffer from a missing money problem in case they would have to rely on revenues from the energy market only. In addition, the Commission has also concluded that the Polish market-wide capacity mechanism is the appropriate instrument, as a complement to the necessary energy market reforms, to address the security of supply risks identified by the authorities, in view of its wide eligibility requirements, its openness to cross-border participation from the first delivery year onwards, and the remuneration of availability only ⁽²⁹⁾.
72. The Commission observes that if reductions of the capacity charge are too high or awarded to too many sectors or electricity consumers, the overall funding of the capacity mechanism might be threatened as well and the public acceptance for security of supply may be equally hampered. At the same time, distortions of competition and trade may be particularly significant. In order to assess necessity of the reductions the eligibility criteria for reductions from renewable charges can be used as guidance (paragraphs 185-187 of the EEAG).
73. On proportionality, paragraphs 188 and 189 of the EEAG can also be used as guidance. Paragraph 188 of the EEAG provides that the aid is considered proportionate if the aid beneficiaries pay at least 15 % of the additional costs without reduction. The Commission is of the view that in order to be proportionate the reductions cannot correspond to a full exemption or be as significant as to jeopardize the purpose of the support measure because they result in too heavy burden on the other end consumers. Also, too significant reductions would increase the distortion of competition resulting from them and create a disadvantage for energy efficiency measures. This is why the Commission considers important that the reductions do not go below a certain minimum threshold which ensures that the beneficiaries make a financial contribution which secures the financing base for the capacity mechanism and reflects the beneficiaries' ability to accept the additional financial burden in relation to their electro-intensity.
74. At this stage, the Commission cannot take a final position on whether, in the absence of the notified reductions from the capacity charge, the financing of the capacity mechanism and the objective pursued by it would be put at risk. In light of the doubts expressed in Section 3.3.1. above, the Commission invites Poland and any other interested parties to comment also on the necessity, incentive effect and proportionality of the notified reductions.
75. Therefore, at this stage the Commission cannot conclude that the reductions from the capacity charge are necessary, appropriate, and proportionate to the objective pursued

3.3.3. *Transparency*

76. The Commission takes note of Poland's commitment referred to in recital 32 above.

3.3.4. *Duration*

77. Finally, the Commission also takes note of Poland's commitment that it would re-notify the measure at the latest after 10 years.

⁽²⁸⁾ See case C-730/79 *Philip Morris v Commission* EU:C:1980:209.

⁽²⁹⁾ See paragraphs 3.3.2 to 3.3.5 of the 2018 Commission decision in case SA.46100.

3.3.5. *Conclusion regarding compatibility with the internal market*

78. The Commission considers that the measure is novel in terms of both its subject matter and its implications for the future ⁽³⁰⁾. On the basis of the information available at this stage, the Commission has doubts on the compatibility of the notified measure with Article 107(3)(c) TFEU.

4. CONCLUSION

In the light of the foregoing considerations, the Commission, acting under the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union, requests Poland to submit its comments and to provide all such information as may help to assess the aid, within one month of the date of receipt of this letter. It requests your authorities to forward a copy of this letter to the potential recipient of the aid immediately.

The Commission wishes to remind Poland that Article 108(3) of the Treaty on the Functioning of the European Union has suspensory effect, and would draw your attention to Article 16 of Council Regulation (EU) 2015/1589, which provides that all unlawful aid may be recovered from the recipient.

The Commission warns Poland that it will inform interested parties by publishing this letter and a meaningful summary of it in the Official Journal of the European Union. It will also inform interested parties in the EFTA countries which are signatories to the EEA Agreement, by publication of a notice in the EEA Supplement to the Official Journal of the European Union and will inform the EFTA Surveillance Authority by sending a copy of this letter. All such interested parties will be invited to submit their comments within one month of the date of such publication.

⁽³⁰⁾ See Case T-793/14, *Tempus Energy v Commission*, EU:T:2018:790, paragraph 82.