



European Economic and Social Committee

TEN/547
Energy prices and costs

Brussels, 4 June 2014

OPINION

of the

European Economic and Social Committee

on the

Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions

Energy prices and costs in Europe

(COM(2014) 21 final)

Rapporteur: **Mr Adams**

On 15 January 2014 the European Commission decided to consult the European Economic and Social Committee, under Article 304 of the Treaty on the Functioning of the European Union, on the

Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions - Energy prices and costs in Europe
COM(2014) 21 final.

The Section for Transport, Energy, Infrastructure and the Information Society, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 21 May 2014.

At its 499th plenary session, held on 4 and 5 June 2014 (meeting of 4 June), the European Economic and Social Committee adopted the following opinion by 140 votes to 10 with 13 abstentions.

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1. Conclusions and recommendations

- 1.1 Energy prices, taken as a whole, have reached and are likely to further exceed current historically high levels. Many domestic consumers across the EU are experiencing this as a severe impact on their budgets, industrial consumers are often similarly affected. This Communication stresses the need for greater understanding in civil society of how the composition of energy prices can reconcile our climate targets with our need for energy security. Without this understanding neither political will nor consumer acceptance can be forthcoming.
- 1.2 Energy prices can comprise an important competitiveness factor for industry. However, an economic analysis of industrial competitiveness should not be limited to energy prices. Other key factors such as energy intensity and the share of energy costs in total production costs as well as in profit margins should also be considered. It is essential to have global coherence in limiting climate change. Leadership by Europe may risk consequences of uncompetitiveness, industrial relocation and carbon export.
- 1.3 Energy efficiency, renewable energy, and other indigenous sources of energy can all improve security of supply but each have factors of cost, risk, environmental impact and social acceptance attached. As national approaches and attitudes will vary transparent cost analysis and a revision and better coordination of support instruments (like feed-in regulations and tariffs) are vital in determining an acceptable energy mix in each Member State and cooperation with neighbouring countries is equally important.

- 1.4 It is necessary to secure the capacity of industry to adapt in the future as it did in the past and bolster the capacity of the energy sector in particular to carry out the necessary investment in the energy system. This will require firm governmental commitments which must be consistent with a European internal energy market (IEM).
- 1.5 The IEM must be completed but to deliver its full potential it needs to be backed by appropriate Market Based Instruments (MBIs), a genuine coordination of national energy policies at EU level and a clear common direction. A renewed emphasis on transparent and accurate data is a necessary precondition. The specific situation of the individual Member States – for example in relation to existing "energy islands" – should be taken into account. Price reviews should bear in mind that without properly developed infrastructure, something which requires significant investment, the internal energy market cannot be completed, nor can its benefits be enjoyed by the Member States.
- 1.6 Cost-optimisation through closer EU coordination and solidarity is vital especially as the levers of energy policy remain under the direct control of Member States. Such coordination has been weak in the past; a new approach is needed. Solidarity by Member States in the face of increasing uncertainties about supply is also vital together with an increased emphasis on further joint research and development to solve the problems apparent in the energy production and supply chain.
- 1.7 The development of liquid gas hubs among groups of Member States can optimise and reduce costs by contributing to decoupling oil and gas prices and improving flexibility for generators.
- 1.8 To enhance coordination, the EESC urges action on and direct support for an extensive programme integrating dialogue about energy at a European level. This should involve energy consumers, domestic and industrial, and the commercial and institutional stakeholders in the energy chain, alongside local, regional and national authorities.
- 1.9 This European Energy Dialogue (EED), inclusive, representative, independent and transparent, should also provide the basis for the new governance process proposed by the Commission to deliver the energy and climate targets proposed in the framework package for 2030.

2. **Introduction and background**

- 2.1 For several years energy prices, especially electricity, for most EU domestic and industrial consumers have risen at a rate in excess of inflation. Households across Europe have seen an impact on their domestic budgets and there has been a significant increase in energy poverty in some Member States. The competitiveness of some industries has also been affected, especially that of energy intensive industry. In the past industry has often responded to high prices by improving energy efficiency and specialising in high value-added production but it

can be argued that the scope for doing this is decreasing. The economic downturn has added further pressure and, in spite of energy efficiencies and cut-backs, costs continue to increase for most consumers.

- 2.2 Two major reports directly relevant to prices and costs are contained in the package presented by the European Commission in January 2014. One is the staff working document on Energy Prices and Costs, the other is on Energy Economic Developments in Europe. The package sets energy and climate objectives for the period to 2030 and proposes that climate protection, maintaining industrial competitiveness and offering the citizen affordable energy can be reconciled. This will require a shared understanding, recognition and communication of the concrete economic, social and environmental benefits that come from reducing emissions and greening the economy. Implicit in the package is a recognition that public support will be vital and that a more realistic approach to the challenges, particularly financial, will be required. The Commission argues that "the objectives send a strong signal to the market, encouraging private investment in new pipelines and electricity networks or low-carbon technologies"¹.
- 2.3 The communication on energy prices and costs, the subject of this Opinion, indicates, as does the IEA², that a combination of world market prices, vital large scale investment in infrastructure and energy efficiency, together with climate-related levies, will see the price of energy continue at its current historically high level. Not only can this have a severe impact on consumers but also the current wholesale electricity price for the power sector of around 40 EUR per MWh will not allow the sector to undertake the necessary investments required for both replacing aging assets and to address climate change. This Opinion concentrates on the likely response of civil society and the degree to which strong market signals and political responsiveness can be established to achieve policy targets.

3. **Summary of the Commission's Communication**

- 3.1 In the five years following 2008 retail energy prices in Europe rose, in some Member States quite significantly, despite relatively stable wholesale electricity prices and steady wholesale gas prices. The impact on domestic and industrial consumers, particularly during the period of economic downturn, was considerable and is likely to continue. There is also wide variation between Member States with some consumers paying 250-400% more than others. A significant part of these increases have been due to rises in transmission and distribution costs and increases in taxes and levies. Nevertheless the cost of primary energy remains the single largest factor in the price composition.
- 3.2 EU governments need to complete the internal energy market in 2014. Liberalising the market will boost investment and competition and improve efficiency in several areas, with possible

¹ Introduction: http://ec.europa.eu/energy/2030_en.htm.

² World Energy Outlook, IEA, 2013.

benefits in the form of lower prices. Consumers and industry (particularly small and medium-sized businesses) can lower the price they pay by switching to cheaper energy suppliers, where suppliers are sufficiently numerous.

- 3.3 EU governments also need to develop energy infrastructure further, diversify energy supplies and supply routes, and take a unified stance when negotiating with major energy partners.
- 3.4 Member States should also ensure that energy policies funded by end-users and taxpayers are applied as cost-effectively as possible and follow best practice.
- 3.5 The EU and the governments of member countries need to do more to compare network costs and practices. The convergence of network practices across Europe has the potential to improve efficiency and cut the network cost element of prices.
- 3.6 Domestic consumers and industry can, to some extent, keep energy costs down by improving energy efficiency. Voluntary actions by consumers to adjust the amount or timing of their energy consumption (demand response) and innovative energy technologies can help save energy and money.
- 3.7 The EU must continue its efforts with international partners on energy subsidies and export restrictions and help protect certain industrial consumers through fiscal transfers and exemptions and cuts in taxes and levies.
- 3.8 In essence, the Commission argues for the completion of a single market for energy in the EU and suggests that action should be taken by households and industry alike to improve their energy efficiency, adopt demand response and other novel energy technologies and innovations to save energy and money and that Member States need to significantly upgrade transmission and distribution. It is noted that the growth in renewables can have a direct impact on improving energy security. It is also recognised that for domestic consumers in some Member States energy poverty will need action, primarily through social policy measures. Should the anticipated declining competitive situation in energy for industry develop it could also be addressed, primarily through the WTO, by minimising subsidies for energy by international competitor countries and also by other fiscal transfers.

4. General comments

- 4.1 There are three vital aspects to the strategic response proposed by the Commission. Irrespective of the completion of the internal energy market, can a strong case be made for a continued or enhanced approach to a "green" economy as stressed in the 2030 framework and what would this involve for energy prices and costs? Secondly, can civil society be convinced through an effective social dialogue that such an approach is valid and acceptable? Thirdly, will it be possible to stimulate the market to generate private investment in Europe in new pipelines and electricity networks and low-carbon technologies.

- 4.2 Energy as a whole, in its various forms, is easily the most widely traded global commodity by value. The central role of energy in economic development ensures that research, exploration, development and the production and transmission of energy will demand massive investment for the foreseeable future. This also applies to the need, recently highlighted, to obtain a secure supply of energy. This is usually characterised by the phrase, "The lights must be kept on", "light" being understood as the standing for the indispensable role of energy in modern society. It is necessary to recognise that, at present, other objectives in energy policy, whether national or at EU level, are likely to be contingent on security of supply, a factor which needs greater recognition in the communication, and that ensuring this may also carry additional costs.
- 4.3 At the same time, if the short to medium term costs of transition to low-carbon energy production are to be met several important factors at a global level must also continue to be recognised and re-emphasised.
- Energy production is creating a significant environmental impact on our planet and ourselves, primarily through climate change but also through adverse health effects.
 - 82% of our current global energy demand is supplied by fossil fuel, a long term finite resource.
 - The assumed constraint of resource availability (peak oil, etc.) is less applicable due to new exploration or development of new extraction processes and market pressures to use unconventional fossil fuel resources will be considerable.
 - Exploiting just one third of the known resources of fossil fuels is more than sufficient to push the planet beyond the GHG 450 ppm (i.e. 2°C) level yet new exploration and extraction techniques continue to receive huge investments³.
- Inevitably, an energy-transition out of fossil fuels has to be accomplished. The speed of transition is vital – quick enough to prevent excessive climate impact whilst maintaining stable economic and social structures. A joint global effort will be critical and maintaining the EU's economic capacity to contribute to this transition will be essential. It is essential to have global coherence in limiting climate change. Leadership by Europe may risk consequences of uncompetitiveness, industrial relocation and carbon export.
- 4.4 To date it is clear that markets on their own often fail to address social and environmental issues – this is not their role. The EESC believes that markets, good though they often are at delivering short-term cost and efficiency objectives, have to be transformed by effective

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The Burning Question, Mike Berners Lee, Greystone Books, 2013.

Market-Based Instruments to enable them to deliver social priorities⁴. This requires good regulation, the support and engagement of civil society and the development of a robust commitment to corporate social responsibility.

- 4.5 Without the understanding by society of the dilemma that both the EU and the world is facing neither political will nor consumer acceptance can be forthcoming. In all probability prices will continue to rise. Consumers will continue to strongly object to such rises. The challenge is to reduce the political and social impact.
- 4.6 The EESC believes that the most effective approach is to fully engage European energy consumers, domestic and industrial, and the commercial and institutional stakeholders in the energy chain in an active and creative dialogue about these issues, which will lead to action.
- 4.7 There is little evidence of this approach in the current Communication. Although "markets" are referenced 41 times there are only three insignificant references in total to "involvement", "citizen", "dialogue", or "consultation". A similar pattern is also found in the 2020-2030 policy framework document.
- 4.8 Consistency and action is vital on this topic. The 2011 framework document "Energy Roadmap 2050" recognised and expanded on this point – "Engaging the public is crucial" (para.3.4) but little action has been taken.
- 4.9 The EESC therefore urges the EU institutions and Member States to adopt and act on, as a matter of urgency, the framework for a European Energy Dialogue adopted by the Committee in 2013 in its Opinion on "Needs and methods of public involvement in the energy policy field"⁵. Such a dialogue would play a formative role in establishing and maintaining an EU-wide governance process for delivery of energy and climate targets.
- 4.10 Such a process should emphasise:
 - a much greater emphasis on transparency, firm regulation and governance at all levels
 - greater citizen/consumer understanding of and trust in the operation of the energy market with appropriate training and advice
 - greater public involvement in determining the national and EU energy mix
 - the flexibility of Member States to choose policies best-matched to national energy mix and preferences, whilst moving towards convergence at EU level

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[OJ C 226, 16.7.2014, pp. 1-9.](#)

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[OJ C 161, 6.6.2013, pp. 1-7.](#)

- achieving national targets (GHG, RES and energy efficiency) in the context of market integration
- 4.11 The variation in energy prices across the EU has previously been noted. Although variability in production and supply costs play a part in this the wide range of imposed taxes and levies on energy is a significant contributing factor. In all Member States energy taxes form a significant part of government revenue and even when taxation on oil is excluded the challenge of finding other revenue sources to replace any tax reduction would be substantial⁶.
- 4.12 However, it should also be noted that a high tax regime on some types of energy has come to be accepted, albeit grudgingly. In the EU oil taxes constitute over 55% of the price compared with, for example 14% in the USA and 41% in Japan.
- 4.13 The specific situation of the individual Member States – for example in relation to existing "energy islands" – should be taken into account. Price reviews should bear in mind that without properly developed infrastructure, something which requires significant investment, the internal energy market cannot be completed, nor can its benefits be enjoyed by the Member States.

5. Specific comments

- 5.1 The "internal energy market" is particularly problematic because security of energy supply is a vital national interest, which, in spite of progress towards an internal energy market, remains largely under direct state control or influence. Technical, resource and geographic factors have also contributed to the difficulty of market delivery, compared, for example, with many categories of consumer goods.
- 5.1.1 The target of completing a single market for electricity and gas, set in the 2009 third energy package, will not be met and major aspects of energy liberalisation have proved hard to deliver. Achieving the benefits of market integration has met government, corporate and societal resistance. In some Member States it is perceived that the comprehensive changes in which energy is produced, distributed and consumed may have unacceptable effects.
- 5.1.2 Although wholesale price convergence is generally taking place in Central and Western Europe retail prices are not converging due to Member States applying varying national schemes to support investments in the energy sector and due to implementing varying national policies on how to distribute these support costs across final consumers. Consequently, a "shallow" electricity market is developing that merely optimises the usage of the existing European system. However, this is insufficient as a "deep" market that incentivises optimal investments on a European scale is required both to allow these

⁶ Energy Policy and Energy Taxation in the EU: IREF Europe.
http://www.irefeurope.org/en/sites/default/files/Energy_policy_EU.pdf.

investment to happen and to make sure they are cost-efficient. For example a revision and better coordination of support instruments (like feed-in regulations and tariffs) is vital.

- 5.1.3 This requires increased market liquidity and hub-pricing, in particular for gas. Gas markets have been established in some Member States but they are still not liquid enough to offer a viable alternative to – expansive – oil-indexation and provide the market-based pricing. It is therefore essential to develop regional gas hubs and improve the interconnectivity between them in terms of transmission capacity, contractual arrangements and access to the market, particularly flexible tranches of supply. Granting power generators access to gas markets gives them more flexibility to optimise generation periods. They can avoid generation during loss-making periods and preserve the competitiveness of the plants, thus reducing uncovered costs to be passed on to consumers.
- 5.1.4 There is still uncertainty about the in-depth composition of energy prices across Member States. The detailed research that is ongoing by the Commission on making both energy price composition and the extent and impact of energy subsidies less opaque is critical in establishing the basis for a level playing field for energy production and pricing. There is a need to continuously acquire data on energy prices and costs at plant level in order to improve transparency on the operating conditions that industry sectors deal with but also to base policy on sound data. It is crucial to ensure transparency as a first step towards cost-efficient policy choices and a meaningful political discussion with the public. This also applies to the composition of profit levels of energy suppliers. The absence of appropriate statistics may undermine the credibility of decisions presented as evidence-based. Such statistics should be made available at each governance level.
- 5.1.5 Industry can make investments and has done so in the past to reduce the intensity of energy use. Such investments, however, require an acceptable pay-back and these investments tend to become more expensive over time.
- 5.1.6 In the past the EU and Member States have helped to protect vulnerable industries by a mix of free allocation, exemptions from taxes and levies and, in some limited cases, by compensation. Given that the gap between the costs for climate policy in the EU and some of its major trading partners will not reduce any time soon, the European Commission should assess the existing framework and examine new approaches, which are more internal market compatible to address vulnerable industries.
- 5.1.7 As energy security is a vital state interest governments will accept contingent extra costs to ensure supply. Also because Member States, for reasons of sovereignty, find it difficult to agree a satisfactory EU-level governance process this leads to them being willing to tolerate sub-optimal market design. Nevertheless in situations of energy uncertainty solidarity is crucial to sustained energy provision.

5.1.8 Overall, there is little sign that the widely varying national energy policies being pursued by Member States recognise the need for deeper integration at EU level. This undermines the internal energy market and sends confusing investment signals. The EESC believes that a decisive step towards a real European Energy Community is necessary to coordinate national energy strategies, particularly with a view to securing the EU's energy supply at the lowest cost.

5.2 The greening of the economy

5.2.1 In principle the move to a more sustainable, resource efficient economy is well established. In practice, economic downturn, global competition and disagreement about priorities between Member States have affected the speed and effectiveness of the transition⁷.

5.2.2 Political statements on greening the economy have often paid lip service to the EU's sustainable development objective, recognising neither the scope of economic and societal change that this would imply nor the structural obstacles.

5.2.3 This objective has often been misinterpreted as making existing economic activities "greener" i.e. lower carbon, and maintaining the hope that this would result in more growth and jobs. However greening the economy requires much deeper transformations of production and consumption patterns – and lifestyles – than are probably socially acceptable within a decade. Virtually all economic activities would need to be transformed and in the transition period from the traditional to the green economic pattern the level of growth and jobs creation is uncertain. This should be backed by coordinated efforts in research and development.

5.2.4 Similarly the obstacles to a swift, effective and virtuous greening of the economy have been drastically downplayed. Pricing plays a part in the following issues for example:

- reluctance of economic sectors (vested interests) and therefore of politicians
- the advantages that existing technologies have due to paid down infrastructures
- lack of effective carbon pricing
- effective regulation of green claims
- technology and political risk of new low-carbon technologies
- job losses and possible reluctance in retraining workers
- issues of industrial transformation and their social impacts
- funding issues in a context of low (or negative) economic growth and "budget consolidation"
- intense international competition
- the low carbon economy would need strong social and political consensus, massive private and public investments backed by easy access to funding and a clear strategic vision, in effect a planned "green" economy.

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[OJ C 271, 19.9.2013, pp. 18-22.](#)

- 5.2.5 Nevertheless the greening of the economy will need to happen. The scope is considerable and highly demanding but there is no choice if we are to secure a sustainable future. To achieve this goal will require setting a pace which recognises the balance between political credibility, economic power, stable social systems and citizen choice. However the preconditions are not being met, particularly in terms of public engagement to address the obstacles. It is also true that clear benefits can accrue such as developing market leadership in sustainable and low carbon energy. The EU is well advanced in introducing low carbon electricity into various forms of heat substitution and also has a large sector developing sustainable transport innovations.
- 5.2.6 The role of energy savings and efficiency is vital in cost minimisation. Domestically, there are still many benefits to be taken through consumer demand management. Notable examples of efficiency and use reduction are proliferating in public sector buildings (largely confined to new build) and the drive for more industrial energy efficiency, well-established in some sectors, can still achieve savings for many businesses.
- 5.2.7 Market Based Instruments (MBIs) have played a very significant role in encouraging a reorientation of Member States' economies. However, for the most part there has been a lack of consistency across the EU in the scale and use of taxes, levies, subsidies and other MBIs. This has been particularly noticeable in relation to energy. MBIs must therefore advance the transition to a resource-efficient and low carbon economy and support economic recovery⁸.
- 5.3 The indispensable requirement for effective governance in achieving EU energy and climate targets proposed in the climate and energy package has clear links with establishing consistent market parameters through national energy regulators. The EESC firmly advocates a more coordinated energy policy with consistent, convergent governance of national policies as a step towards pan-EU cost optimisation and therefore supports the Commission's initiative. It believes, however, that an in-depth reflection is necessary to make sure the system will truly deliver its objectives and is of the view that the Committee can make a useful contribution to the forthcoming Commission proposals, in particular in terms of:
- balancing flexibility with achieving the energy objectives,
 - strong public involvement and legitimacy for national and EU measures,
 - promoting Member States' ownership of the process,
 - delivering consistent and trusted convergence at EU level.

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[OJ C 226, 16.7.2014, pp. 1-9.](#)

- 5.4 The Commission faces the task of devising a governance system that is effective in terms of enforcement but flexible enough to secure Member States' backing. The EESC therefore proposes, in close cooperation with the Commission, initiating a politically neutral reflection inclusive of all stakeholder voices. Its objective would be to devise an effective, flexible and inclusive governance system. Both the process of public engagement and the governance system itself are vital in moderating and explaining the challenge of energy prices and costs.

Brussels, 4 June 2014.

The President
of the
European Economic and Social Committee

Henri Malosse
