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Germany

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Overview of the current energy mix and the place in the market of different energy sources

The Federal Republic of Germany is pursuing rather ambitious goals with its energy transition. For example, renewable energies should account for at least 35% of gross electricity consumption by 2020, and at least 80% by 2050. At present, Germany seems to be on the right track in this respect: by 2018, the share of renewable energies in gross electricity consumption had already reached approx. 37.8%, so that the target for 2020 has already been met.[1]

This trend looks set to continue in 2019. In the first quarter of 2019, 62 billion kilowatt hours of electricity were generated from renewable energies and fed into the German electricity grid;[2] according to preliminary results of the Federal Statistical Office, this was an increase of 13.7% compared to the same quarter of the previous year. Overall, the share of electricity from renewable energies on the production side was 41.1%.

This development is primarily attributable to a very windy first quarter: the volume of electricity from wind power rose from 23.2% to 26.5% during this period. The share of electricity derived from biogas amounted to 5.1%; that of electricity generated from solar energy to 4.1%. On the other hand, the volume of coal produced fell considerably, by 20%. The decline in the amount of electricity produced from coal-fired power plants is due to the fact that coal-fired power plants often had to be ramped up and down in the first quarter of 2019 due to the high feed-in of electricity from renewable energies and their priority position. Nevertheless, coal remained the most important energy source for electricity generation with a share of 32%, followed by wind power (27%) and nuclear power (13%).

In general, wind energy has so far played a major role in the transition of energy systems. At 5,009 MW in 2017, the gross addition of onshore wind turbines significantly exceeded the gross addition path of 2,800 MW per year for the years 2017 to 2019 as specified in the Renewable Energies Act 2017 ("*Erneuerbare-Energien-Gesetz* 2017" – **EEG 2017**). The high increase in 2017 is particularly the result of pull-forward effects due to transitional regulations. In 2018, on the other hand, the net increase in onshore wind turbines fell to 2,273 MW, below the gross addition path anchored in the EEG 2017. The reasons for this decline may be the introduction of tenders in 2018 and increasing problems with the acceptance of wind energy projects. Whether the goals of the energy transition in Germany can be achieved will depend to a large extent on how the dynamics of the expansion of wind energy continue to develop.[3]

Developments in government policy/strategy/approach

In the coalition agreement of the current 19th legislative period of the German federal parliament,[4] which was concluded on 7 February 2018 between the governing parties CDU, CSU and SPD, the government set itself the goal of continuing the expansion of renewable energies and achieving a 65% share of renewable energies in the energy mix by 2030. This is intended, in particular, to cover the additional electricity required to achieve the climate targets for transport, buildings and industry.

The coalition agreement sees the greatest challenge in the expansion of renewable energies in the capacity of the grids. Therefore, while on the one hand, the expansion of the grid must be accelerated, on the other, the existing electricity grids need to be optimised and better utilised through closer cooperation between the grid operators and new technologies. The Federal Ministry of Economics and Energy has accordingly presented an "Electricity Grid Action Plan", which provides for several measures to meet the objectives of the coalition's revenue. An important part of the action plan is the amendment to the "Network Expansion Acceleration Act for the Transmission Grid" ("*Netzausbaubeschleunigungsgesetz Übertragungsnetz*" – **NABEG**).[5] This amendment essentially simplified and accelerated the approval procedure for the expansion, reinforcement and optimisation of power lines. The amendment came into force on 17 May 2019.

In addition, the coalition agreement provides for a federal energy efficiency strategy to be developed with the aim of reducing energy consumption by 50 % by 2050. Accordingly, a draft law for a new "Building Energy Act"[6] is currently available, which is intended to bring together the existing energy regulations for the building sector. In line with the requirements of the coalition agreement, the draft law does not provide for a tightening of the current building standards. The law is scheduled to come into force at the end of 2019.

The coalition agreement also addresses the topic of sector coupling: it is intended to promote linking the heat, mobility and electricity sectors in connection with storage technologies. For this purpose, the framework conditions are to be adapted; however, the coalition agreement does not mention any concrete measures, nor have any such measures yet been implemented.

The governing parties also stipulate in the coalition agreement that the commission "Growth, Structural Change and Employment", involving various actors will be set up to work out a plan for the gradual reduction and discontinuation of coal-fired power generation, including the necessary legal, economic, social and structural measures. The appointment of the Commission was accordingly decided by the Federal Government on 6 June 2018. On 26 January 2019, the Commission presented its final report, which foresees a path towards the gradual phasing-out of coal-fired power generation by 2038, if possible by 2035 (see below). This makes Germany the only industrialised country to opt out of both nuclear and coal energy.

Developments in legislation or regulation

Energy Collective Act

Probably the most substantial changes in the legal framework of the energy market in the past year result from the Energy Collective Act. The Act came into force on 21 December 2018, amending the EEG, the Combined Heat and Power Act ("*Kraft-Wärme-Kopplungsgesetz*" – **KWKG**), the Energy Industry Act ("*Energiewirtschaftsgesetz*" – **EnWG**) and other energy regulations.[7] These changes were originally planned for the "100-

day law", which, however, was not passed in time due to differing views within the coalition, and finally was renamed the Energy Collective Act ("*Energiesammelgesetz*"). The Energy Collective Act implemented various urgent legislative requirements in the energy sector in order to further ensure the purposeful and efficient expansion of renewable energies.

A major part of the amendments of the Energy Collective Act affects the EEG 2017, in particular, the regulations regarding certain tenders, and the remuneration. One of these changes introduced into the EEG 2017 is the legal anchoring of the special invitations to tender for solar and onshore wind power plants. In total, an additional 4,000 MW each are to be put out to tender by 2021. For the regular tenders, the volumes for onshore wind energy and solar energy were slightly reduced.

In order to counter the expected lower realisation of onshore wind energy projects, the legislator has also shortened the realisation period for onshore wind turbines, which benefit from an award in the first three bid dates in 2019, from 30 to 24 months. If an onshore project is not realised within this period, the award expires.

The Energy Collection Act also resulted in slight changes for the tenders for biomass plants: the tender frequency was changed from one bid date per year to two bid dates per year, while the tender volume remains the same. This amendment aims to strengthen competition and avoid delays.

In addition, the Energy Collective Act was accompanied by successive cuts in financial support for solar plants on buildings with an output of between 40 and 750 kW. The tenant electricity surcharge for solar power generation was also reduced. It remains to be seen whether tenant electricity models can still be implemented profitably in the future.

Moreover, the Act also adapts the regulations for the partial exemption of new combined heat and power (CHP) plants from the EEG levy. This adjustment was necessary in order to comply with the EU Commission's state aid rules.

As a further result of the amendments, the EEG 2017 now contains an obligation for wind turbine operators to provide night-time identification in line with demand. These are devices that only flash red at night when an aircraft is nearby. The equipment obligation, which aims, in particular, to strengthen the acceptance of wind energy by residents, applies both to new plants and (after a transitional period) to existing plants.

The KWKG has also been amended by the Energy Collection Act, especially regarding the granting of the CHP surcharge for existing and modernised CHP plants. In particular, the CHP surcharge for existing plants was reduced, as an evaluation of the support rates showed that there was excessive support for CHP plants, due to significantly lower gas prices. The changes implemented in the EnWG relate, in particular, to the formation of the capacity reserve and the grid connection conditions according to the provisions of European law.

Modernisation of the Grid Fee Structure

The Act to Modernise the Grid Fee Structure ("*Gesetz zur Modernisierung der Netzentgeltstruktur*" – NEMoG),[8] which has been in force since July 2017, contains two important regulations: firstly, the gradual standardisation of transmission grid fees; and secondly, the reduction of the privilege of avoided network charges.

The transmission grid fees will be gradually adjusted nationwide by the NEMoG and a corresponding ordinance of the federal government. Since 1 January 2019, transmission grid fees are being standardised in five stages. In the 2019 calendar year, the transmission grid charges, for 20% of the revenue caps relevant for the formation of charges, will be determined on a nationwide basis. In subsequent years, this share of revenue caps will

increase by 20%. Starting in calendar year 2023, the transmission grid fees will then be fully calculated nationwide. The aim of these regulations is to reduce regional cost differences and thus ultimately to achieve a more equitable distribution of electricity costs. At present, grid fees account for about 25% of the total costs of electricity grids.[9]

In addition, the NEMoG amended the regulations for avoided network charges. For volatile new plants, these fees were completely suspended from 2018; for existing plants, the avoided grid fees have been successively suspended in three steps since 2018 until 2020. From 2023 onwards, new, decentralised generation plants will also no longer receive payments from avoided grid fees. These adjustments are based, in particular, on the fact that the earlier assumption, that locally generated and consumed electricity would save costs for the higher-level grid, does not correspond to the actual circumstances. In order to ensure that the costs of the energy shift in the grid fees continue to be distributed fairly and transparently, it was necessary to adjust the avoided grid fees.[10]

Capacity Reserve Regulation

The conversion of the energy supply to renewable energies naturally brings challenges for the security of supply: renewable energies such as wind and solar energy are subject to natural fluctuations. In addition, the generation of electricity from wind and sun often takes place at a great distance from the central consumption points. In the future, electricity grids will therefore have to be able to transport large generation capacities flexibly. On the other hand, the electricity market must be prepared for unforeseeable extreme situations in which additional capacities are required somewhere.[11]

For this reason, the formation of a capacity reserve was already legally anchored in Section 13e EnWG in 2016. A capacity reserve shall be used if, despite free price formation, there is insufficient supply on the electricity exchange to enable a balance between supply and demand. Originally, such a reserve was planned to be established gradually from the winter half-year 2017/2018 onwards. However, the formation of the reserve was postponed several times, most recently by the Energy Collection Act until the winter half-year 2020/2021. The Capacity Reserve Regulation,[12] which came into force in February 2019, now regulates the procedure for the procurement, use and settlement of the capacity reserve.

The capacity reserve will consist of generation plants, loads and storage facilities, which are selected for a period of two years by the transmission grid operators. Plants in the capacity reserve are located outside the market, i.e. these plants are only used when required at the request of the transmission grid operators and otherwise do not participate in the electricity market. By this means, competition distortions will be avoided. The operators of the plants in the capacity reserve receive an annual remuneration for their participation. The capacity reserve will initially be formed in the amount of 2 GW; the required amount is then regularly reviewed by the Federal Ministry of economics and energy. The invitation to tender for the formation of the capacity reserve for the first supply period from 1 October 2020 to 30 September 2022 will be carried out by the transmission system operators on 1 December 2019. It remains to be seen for which type of plants the participation in the capacity reserve will be of interest, and whether the reserve will be formed to the extent envisaged.

Judicial decisions, court judgments, results of public enquiries

ECJ: EEG 2012 is not state aid

On 28 March 2019, the Court of Justice of the European Union (**ECJ**) ruled in the final instance that the promotion of renewable energies and the special compensation scheme for

electricity cost-intensive companies under the EEG 2012 did not constitute state aid (Case C-405/16 P).[13] In November 2014, the European Commission classified both the renewable energy support and the special compensation scheme as aid (decision of 25 November 2014 on the aid scheme SA.33995 (2013/C) (ex 2013/NN)).[14] The European Court dismissed the action brought by Germany against the ruling at first instance.[15] However, the ECJ has now upheld the action, set aside the ruling of the European Court and annulled the commission's decision of November 2014.

The ECJ thus follows Germany's view that the EEG 2012 does not constitute aid within the meaning of Art. 107 (1) TFEU. The promotion of EEG plant operators is not financed from state resources, but via a private-sector levy system financed by end consumers. The measure is not attributable to the state since the state has no executive function in the course of the implementation of the EEG levy.

The ruling of the ECJ is of great relevance especially for electricity cost-intensive companies: due to the original decision of the European Commission, limitation decisions were partially revoked in 2013 and 2014. As a result, any amounts paid in excess will now be refunded to the companies concerned.

The decision also has a significant impact on the future energy policy. Due to the fact that state aid control is no longer necessary, the legislator has further options to promote renewable energies. In addition, far-reaching consequences could result from the judgment for other ranges of the energy industry, for instance, in connection with grid fees. In May 2018, the EU Commission decided that grid fee exemptions for certain electricity cost-intensive companies in 2012 and 2013 violated EU state aid law.[16] A number of affected companies filed actions for annulment before the European Court. Following the ruling of the ECJ, the prospects of success of these actions have now increased significantly, as against this background the argument that network fee exemptions were not granted "from state funds" also seems reasonable.

Federal Court of Justice: Equity interest rate for gas and electricity networks

On 9 July 2019, the German Federal Court of Justice made a surprising decision of great commercial significance for both electricity and gas network operators and electricity and gas customers:[17] the Court ruled that the Federal Network Agency determined the rates of return on equity for the third regulatory period correctly. The Federal Court of Justice thus set aside a ruling of the Higher Regional Court Düsseldorf from March 2019,[18] which classified the fixed equity interest rates as too low and accused the Federal Network Agency of making an incorrect calculation. After the clear decision of the Higher Regional Court, the decision of the Federal Court came as a surprise to the network operators.

The return on equity indicates the return that network operators can achieve from their investments. The low setting of the equity interest rates for the third regulatory period leads to an approximately 1/4 lower return for network operators compared to the last regulatory period. They must therefore reckon with lower network charges. For electricity and gas customers, on the other hand, the surprising decision of the Federal Court of Justice is good news, as the burden of the network charges is at least limited.

Higher Regional Court Düsseldorf: German balancing energy market

On 22 July 2019, the Higher Regional Court Düsseldorf declared the controversial mixed-price procedure on the German balancing energy market to be against the law.[19]

Since October 2018, the mixed-price procedure has determined pricing on the balancing energy markets. The award of the contract for balancing energy quantities thereafter takes

place on the basis of a mixed price, consisting of the performance price and a weighted commodity price. The purpose of this procedure was to prevent the possibility of abuse that the previously applicable pricing procedure had revealed. However, the mixed-price procedure introduced at that time was often subject to criticism. In particular, it was criticised that the procedure structurally discriminated against renewable energies, as conventional power plants with high performance and low operating prices were systematically preferred. In addition, the total costs of balancing energy had been driven up by the mixed-price method.

In its decision, the Higher Regional Court Düsseldorf judged the mixed-price procedure to be excessive intervention for market participants, and therefore declared it to be unlawful. As a result, the previously valid tender procedure on the basis of performance prices will be revived. In the medium term, the balancing energy market is then to be fundamentally reorganised by the introduction of balancing labour markets, as prescribed by European law.

Major events or developments

Stagnating expansion of wind energy

Wind energy in Germany is an important driver for the transition of energy systems. However, the expansion of onshore wind energy is currently stagnating. The tenders introduced in 2017 to determine the amount of funding under the EEG 2017 were clearly undersigned on all bid dates in 2019.[20] In the last bid date on 1 September 2019, only 176 MW of the 500 MW put out to tender were awarded.[21] The tendered bidders benefited from the low level of participation, so that the average volume-weighted surcharge value of 6.20 ct/kWh corresponded to the fixed maximum value. In particular, long approval procedures, missing land for wind energy, and a large number of objections are held responsible for the stagnating expansion of onshore wind energy.

In view of these developments, a "wind summit" took place in September 2019 at the Federal Ministry of Economics and Energy to which representatives of the industry, the federal states and environmental associations were invited. In the run-up to the summit, various associations presented a 10-point programme for the expansion of wind energy, which contained proposals for ensuring the availability of land, the manageability of nature conservation requirements and for strengthening local capacity.[22] The conclusion of the summit was that in the following weeks, the Federal Ministry of Economics and Energy will develop a plan for concrete measures to accelerate approval procedures and make more land available for wind energy.[23] It remains to be seen how these proposals will be implemented in detail.

Shortfall in the German electricity system

In June 2019, the German electricity grid was significantly undersupplied for three days. The shortfall was so significant that the four transmission grid operators in Germany had to call up reserves of balancing energy throughout Europe because twice as much balancing energy as had been booked in advance was unexpectedly required. Following these bottlenecks, electricity prices on the energy exchange increased significantly for a short time.

How this imbalance in the German electricity market could have occurred has not yet been conclusively clarified. It is assumed that mis-speculation by electricity traders was the cause. (In general, electricity traders must ensure that generation and electricity consumption in their area of responsibility are always balanced.) In order to avoid the purchase of expensive energy on the spot market, some electricity traders may have speculated that there would be enough balancing energy available in the event of an undersupply of the grid.

In the wake of these events, the Federal Network Agency submitted a package of measures to strengthen balancing group loyalty for consultation in July 2019.[24] It is intended to adjust the calculation method for the formation of the balancing energy price by, among other things, tightening existing penalties. In addition, reform proposals for calculating the balancing energy price are to be submitted to the Federal Network Agency for approval. By linking this price to a suitable stock market price index, it is intended to eliminate incentives to exploit price differences. Market participants are also to be obliged to settle their balancing groups at an earlier date in order to prevent systematic short-selling immediately before physical fulfilment.

Furthermore, in view of the incidents, the Federal Network Agency once again urged all market players to comply with their legal obligations. In addition, the regulatory authority reserved the right to initiate supervisory measures in case of suspicion of deliberate manipulation of energy forecasts or unlawful arbitrage transactions on the balancing energy price.

Power Purchase Agreements

Long-term Power Purchase Agreements (**PPAs**) in the renewable energy sector are gaining ground in Germany.[25] This is not least due to the fact that, from 2021 onwards, the 20-year subsidy under the Renewable Energy Sources Act will end for many existing plants, so that plant operators will have to evaluate new ways of marketing. Although some new plants are already being operated today without EEG support, the majority of renewable energy plants are still being supported under the EEG.

Nevertheless, the players on the German market are also increasingly concerned about alternative marketing models. PPAs are currently discussed in this respect. PPAs are contracts between plant operators and large electricity suppliers, which can have different structures. While PPAs themselves are not a new way of marketing, their application in renewable energy projects is new. It therefore remains to be seen which standards will develop for such contracts.

There are already larger-example cases in Germany. EnBW AG and Energiekontor AG recently concluded a 15-year PPA for subsidy-free solar parks in Germany. It is likely to be the first electricity purchase agreement for a photovoltaic project of this size. "The agreement stipulates that EnBW will purchase 100% of the electricity at a fixed price. Within the framework of the agreed contract term of 15 years, the two companies assume that the total amount of electricity produced will be around 1.3 terawatt hours," the companies stated.[26] According to press releases, Deutsche Bahn AG recently also concluded a PPA for 25 MW of capacity from an offshore wind farm, which is the first offshore PPA in Germany.[27]

E.ON/RWE Merger

In May 2018, the major German energy suppliers E.ON and RWE announced their intention to merge: RWE is to transfer 76.8% of its shares in innogy SE to E.ON after the renewable business has been removed from innogy and transferred to RWE. In return, RWE will receive E.ON's renewable business, a payment of €1.5 billion and shares in E.ON with a nominal value of 16.67%. This transaction aims to result in two strengthened European energy companies.

Before this transaction can be carried out, however, it must pass the European and German merger control.[28] In January 2019, RWE announced the acquisition of the renewables business of E.ON and innogy to the European Commission for review. This part of the planned transaction was approved by the EU Commission on 26 February 2019. RWE may

thus take over E.ON's generation capacities and become the central supplier of both conventional and renewable generation capacities in Germany. On the same day, the Federal Cartel Office ("*Bundeskartellamt*" – **BKartA**) announced that it considers RWE's acquisition of the 16.67 % stake in E.ON to be unobjectionable.[29] The EU Commission's approval of E.ON's acquisition of 76.8% of the shares in innogy SE is still pending. The Commission is currently examining whether E.ON's acquisition of the networks and distribution activities of RWE subsidiary innogy is compatible with the common market. The EU Commission's preliminary deadline for the E.ON/RWE merger expires on 20 September 2019. The Commission will then decide whether, and under what conditions, it will approve the final part of the planned merger.

This decision has enormous implications for the energy industry. It is feared that the planned exchange of parts of the company with E.ON could create a new electricity giant which could dominate large parts of the market and prices.

Proposals for changes in laws or regulations

Coal Commission

As agreed in the coalition agreement, the German Federal Government decided on 6 June 2018 to set up the "Growth, Structural Change and Employment" Commission (unofficially the "Coal Commission") in order to draw up a plan for a climate- and socially compatible exit from coal as well as concrete proposals for growth and employment in the affected regions. The members of the Commission represent a broad cross-section of social, political and economic actors. In drawing up the recommendations, the Commission has therefore consulted numerous scientists and interest groups, discussed the state of knowledge and the facts in detail, and weighed the various positions against each other.

The Commission presented its final report on 26 January 2019.[30] In this report, the Commission recommends the end of coal-fired power generation in Germany by 2038 at the latest. As intermediate steps, reductions in coal capacities to 30 GW in 2022 and 17 GW in 2030 are planned. In 2032, a review will be carried out to determine whether it will be possible to stop coal-fired power generation in Germany as early as 2035. For lignite-fired power plants that have already been built but are not yet in operation, a negotiated solution is to be sought so that these power plants are not put into operation. Should this not succeed, regulatory solutions and compensation should be considered between 2023 and 2030. For coal-fired power plants, voluntary decommissioning premiums are to be paid, which will gradually decrease by 2030.

In addition, the report shows how economic structural change can succeed in the regions concerned. In order to support these regions in their structural change, the report proposes funds of over €40 billion. In order to implement the Commission's structural policy recommendations, a draft law on structural strengthening was prepared and adopted by the Federal Cabinet at the end of August.[31]

The legislative implementation of the Commission's energy policy proposals is currently being prepared. A corresponding law is to be presented in autumn 2019 so that the legislative process can be completed by 2019.

Planned changes of EEG and KWKG

The law amending the law on energy services and other energy efficiency measures ("*Energiedienstleistungsgesetz*" – **EDL-G**[32]), which was passed in the German parliament on 27 June 2019, not only further develops and simplifies the regulations on mandatory

energy audits. The law also contains further amendments, in particular to take account of the ruling of the European Court of Justice on the state aid character of the EEG 2012 (see above).[33]

Since, from a German perspective, the ruling can also be applied to the KWKG, the German legislator has decided to remove the European Commission's approval reservations under state aid law in the KWKG. Due to the previous reservation of approval, support for existing CHP plants was suspended for the year 2019. This led to a noticeable deterioration in the economic situation of plant operators. With the abolition of the approval reservation, the subsidy for existing plants can now be granted.

In addition, the legislator set the EEG levy for self-supply from CHP plants back to 40%, with retroactive effect to 1 January 2019. Furthermore, the EEG 2017 also lifts various approval reservations under state aid law.

The EDL-G still requires the approval of the Federal Council, which is expected to decide on it at its next plenary session on 20 September 2019.

Regulatory framework for energy storages

Due to the fact that the generation of electricity from wind and solar power plants depends on the weather and not on the demand for electricity, energy storage facilities will be playing an increasingly important role in the energy transition. Energy storages could ensure the security of supply and reliability of the power supply even with increased use of renewable energies. Accordingly, the regulatory framework for electricity storage facilities was gradually improved by the legislator: with the introduction of the EEG in 2017, the double burden of the EEG levy on both the fed-in and fed-out quantities of electricity was discontinued. Under certain conditions, it is also possible to exempt energy storage facilities from grid charges for a period of 15 years from commissioning.

In the future, the regulatory framework for energy storage is to be further improved: the European Union's new directive 2019/944 on common rules for the internal market for electricity and amending Directive 2012/27/EU,[34] which came into force on 4 July 2019, stipulates that storage facilities providing grid services such as balancing energy will in future be treated equally with other power plant technologies. This means, for example, that storage facilities will be given their own grid connection entitlement. In addition, the double burden of taxes and levies on energy storage facilities is to be eliminated if the storage facilities provide network services. This would mean that energy storage facilities in Germany would no longer be burdened twice with statutory levies and concession fees.

As part of an EU Directive, these regulations do not apply directly, but must be implemented by the Member States. The Member States have until 31 December 2020 to implement the Directive.[35]

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