E.DSO advocacy paper

DSO Recognition: A call to reassess EU Funding priorities

Connecting the missing pieces in the EU´s funding puzzle

The European Union (EU) plays a pivotal role in facilitating financial assistance to its Member States (MS) and businesses through various grant programs. Two notable examples are:

1. Horizon, which successfully promotes Research, Development, and Innovation (R&D&I), and
2. Connecting Europe Facility (CEF), established in 2013 based on the TEN-E Regulation, as a key funding for energy projects.

These programs represent direct sources of EU funding. However, the EU also indirectly manages significant financial redistributions through mechanisms like the Common Provisions Regulation (CPR), the Recovery and Resilience Facility (RRF), and REPowerEU.

In our extensive engagement with CEF, RRF, and REPowerEU, and drawing from our extensive experience with E.DSO members across Europe, we have identified a clear funding gap. Despite the 2022 revision of the TEN-E Regulation, which aimed to enhance the role of decentralised projects, the initial list of Projects of Common Interest (PCI) under the new TEN-E Regulation has raised concerns. None of the five new projects proposed for decentralised energy infrastructure, particularly Smart Electricity Grids and Smart Gas Grids, received a PCI status recommendation from the European Commission.

Furthermore, when MS had the possibility to revise their recovery plans and include a dedicated REPowerEU section for energy, very few recognised the importance of decentralised energy infrastructure.

To address these issues, we propose the following measures:

Launching a "**The Decentralised Grid Facility**" This program should be purpose-built to bolster decentralised energy infrastructure, with a specific emphasis on enhancing electricity grids. By creating this specialised initiative, we can ensure that the unique needs of decentralised energy projects are adequately addressed.

Increase Clarity in Funding Prospects: We advise the Commission to provide more explicit guidelines to Member States when unveiling new funding opportunities, such as REPowerEU. It is imperative that these guidelines encompass the entire energy value chain, with a particular focus on electricity grids. Furthermore, in anticipation of the upcoming revision of the Common Provisions Regulation (CPR), we strongly advocate that this revision specifically considers the needs of electricity grids to ensure alignment with the objectives of the next Multiannual Financial Framework (MFF).

Grant Accessibility for Regulated Businesses: A fundamental pillar of our advocacy focus on achieving a fair and treatment for regulated businesses (DSOs) to access grants. Currently, the scenario in some Member States results in financial losses for companies seeking grant acquisitions. To rectify this, we propose that the European Commission issue clearer provisions and guidelines. These measures should guarantee that regulated businesses can genuinely benefit from grant opportunities, eliminating any disparities.

Through the above strategic actions, we aim to provide a solid foundation for the development and promotion of decentralized energy infrastructure, ensuring that electricity grids play a key role in the future. Our commitment is steady, and we are available to work closely with all stakeholders to make these essential changes a reality.

I. Justification point 1- The Decentralised Grid Facility (DGF)

1.1. The Current Funding Landscape

Horizon's strength and limitations

The Horizon programme is for its support of R&D&I projects at the EU level. However, its focus on OPEX often overlooks the crucial financing of hardware that forms the backbone of the DSO industry. A major concern is that, once projects financed by the Horizon ends, they often struggle to keep momentum, leaving DSOs without key partners heavily depending on continuous funding. This gap needs to.

The Connecting Europe Facility's Limitations

With a budget of €5.8 billion allocated for energy projects until 2027, the Connecting Europe Facility (CEF) has limitations in what it can achieve. The ongoing conflict in Europe has underscored the European Union's imperative to prioritise security. Given the present geopolitical situation and an initial review of the 1st PCI list under the TEN-E 2022 framework, it is very likely that several projects will receive more attention. Historically, DSO initiatives have received a relatively small portion of the CEF. These circumstances emphasise the critical need to establish the DGF (Distribution Grid Fund).

*The missed oppor*tunity with TEN-E

In 2022, the TEN-E Regulation was revised, partly to promote the decentralised part of the energy system. Still, in the assessment of the first PCI list under the new TEN-E Regulation, no new decentralised energy infrastructure proposals made the cut for PCI status recommendation.

Limitations of other funds

Both the Innovation and Modernisation Funds, backed by the EU ETS, come with specific constraints. The Innovation Fund often bypasses DSO-related projects, while the Modernisation Fund is reserved for Member States with a GDP per capita below 90% of the EU average. This structure leaves out many DSOs.

1.2 Our proposal, The Decentralised Grid Facility

While many existing funds prioritise regions based on macroeconomic criteria and basic modernisation needs, it's essential to consider the broader European landscape. Our proposal is that the European Commission establishes a fund that supports innovative decentralised projects throughout the EU. With a programme focusing on technology development adaptation and dissemination, DSOs will drive progress beyond just regional and economic differences.

The Missing Part of the EU´s Funding Puzzle: The Decentralized Grid Facility (DGF)

We propose that the Commission introduces the DGF with these recommendations in mind:

- **Ensure the DGF operates independently**, with a clear focus on fostering the transition in the distribution grid. A dedicated budget is crucial.
- **Consider budgetary options:** Either integrate the DGF within the CEF framework with an increased budget or let it function as a standalone programme. Given the recent revision of the TEN-E Regulation, the latter might be more feasible.
- **Gradual rollout:** Start with a pilot programme for the DGF from 2025-2027. This will provide valuable insights, ensuring a seamless transition when it scales up from 2028.

II. Justification point 2- Regulatory Clarity for Member States

2.1. The importance of considering the entire energy value chain

The European Union's mandate includes a vital role in redistributing financial resources across the EU ´s Member States. These funds are crucial in driving sustainable projects, many of which are relevant to the energy sector. However, we would like to stress the importance of adopting a holistic view, addressing all parts of the energy value chain, including electricity grids.

2.2. Challenges with monitoring a vast number of projects

In a recent documentary by Deutsche Welle (DW), Stefan de Keersmaecker – EC´s Spokesperson for Regional Policy, highlighted that the number of projects funded under Cohesion Policy are around 1,5 Million. Given the vast number of projects, it is an impossible task for the Commission to monitor each project's alignment with intended objectives. This vastness implies a risk of certain essential components of the energy value chain, like the electricity grids, being overlooked.

2.3. Decentralised Grids - An overlooked pillar of the Energy Transition

The European Commission's acknowledgment of the role of electricity grids in the energy transition is highly appreciated. However, experiences from national programmes and initiatives like REPowerEU suggest that while energy generation often receives considerable attention, electricity grids, especially at the local and decentralised level, sometimes remain underfunded. While there are EU funding mechanisms targeting cross-border energy infrastructure, the emphasis on decentralised grids has in comparison been limited. Addressing this imbalance is essential to ensuring a robust energy infrastructure that supports not only the centralised, but also decentralised generation.

2.4. Recommendations, Clarity for Member States

Balancing generation with grid support in new funding opportunities.
When the Commission introduces new funding mechanisms, such as REPowerEU, it is essential to include provisions ensuring that support for additional electricity generation is balanced with a proportional amount of support for electricity grids. This approach ensures that as the EU scales up its generation capacities and distribution infrastructure simultaneously to handle the increased load.

Revision of the CPR for the upcoming MFF.
In anticipation of the next Multi-Annual Financial Framework (MFF), and revision of the Common Provisions Regulation (CPR) and regulations under its umbrella, it is recommended to incorporate similar provisions as stated in the point above into relevant programmes. The European Regional Development Fund (ERDF) and the Cohesion Fund stands out as especially relevant with their potential of supporting decentralised grids.

Deciding grid investment ratios with Distributed Network Development Plans.
The "Distributed Network Development Plans," expected to be in place by the time of the next MFF and revised CPR, can serve as key tools to establish the desired balance between generation and grid infrastructure. As the ratio between generation and electricity infrastructure varies between Member States, these plans can help in deciding the level of dedicated support grids should receive in line with the points above.

Alternative actions.

Should the revision of the CPR not meet expectations in connection to the next MFF, we recommend the Commission to utilise its powers to issue a delegated act. This act would address the imbalance, ensuring that incentives for electricity generation are matched with support mechanisms for the development of electricity grids.

III. Justification point 3 - Ensure Grants Benefit Regulated Businesses

3.1. Differences in EU incentive models:

Across the EU, incentive models differ significantly. Some Member States offer additional WACC incentives for EU projects, while others provide regulatory depreciation for assets financed by grants. These methods effectively encourage DSOs to pursue PCI projects and CEF funding. However, this is not the case everywhere. In many Member States, assets financed by grants cannot be basis for tariffs. This, coupled with increased OPEX from such assets leads to negative results.

Despite the improvements in the revised TEN-E Regulation, no new PCI Smart Electricity Grid projects have been recommended for PCI status. According to a recent member survey (which also was extended to the DSO Entity), we have learnt that one of the major reasons for the few Smart Electricity Grid projects on the PCI list is connected to these financial disincentives.

3.2. The importance of regulatory depreciation for DSOs

Eventually, assets financed by grants need replacement. Without depreciation recognition, reinvestment capital is lacking. The revised TEN-E Regulation highlights the Smart Electricity Grid category's eligibility for regulatory incentives, such as being able to benefit from regulatory depreciation.

3.3. Expanding the scope of financial incentives

Financial incentives shouldn't be limited to grants. PCIs could receive a "smartness bonus", leveraging the robust PCI selection process to access other mechanisms or grants beyond the limited CEF Energy budget. A potential link to programmes like Horizon Europe could promote innovative energy transition solutions, ensuring projects like flexibility platforms extend beyond their initial life cycle and are supported for commercialisation.

3.4. Understanding regulatory depreciation through connection fee and tariff mechanisms

The logic when a DSO connect a customer to the electricity grid offers insight into this logic. A one-time connection fee, reflecting the actual cost of connecting the customer is charged. Following the connection, tariffs, including the depreciation cost, are being charged to ensure necessary modernisation and replacement of grid assets. This system ensures continuity since the connection fee is a one-time cost.

Recommendations, Regulatory Incentives & Grant Recognition

Adaptation to the TEN-E Revision.
Following the revision of the TEN-E regulation, Smart Electricity Grid projects are now qualified for regulatory incentives, i.e., regulatory depreciation. Member States need to adapt to this change promptly to ensure a harmonised approach.

Guidance from the European Commission.
Given the unequal treatment of DSO funding across various forms of public funding, the European Commission should issue guidelines to support Member States.

Operational Expenditure (OPEX) and disincentives.
Measures should be in place to prevent DSOs from encountering disincentives, such as increased operational costs associated with grant-funded projects.

Regulatory depreciation for Capital Expenditure (CAPEX).
Allow DSOs to benefit from regulatory depreciation for capital expenditures related to the maintenance, repair, or replacement of project assets.

Amending the Common Provisions Regulation (CPR) for Grant-Funded Assets.
In addition to issuing guidelines on the treatment of funded assets, the Commission should, in the longer term, consider amending the CPR to:

Provide clarity on how assets financed by grants should be recognised in national regulations.

Establish a standardised framework for the treatment of such funded assets with an emphasise the importance of regulatory depreciation for assets financed by grants, as it relates to recovering costs over time.

IV. Potential Inclusions for the Grid Action Plan (2023) with regards to funding.

4.1. The Decentralised Grid Facility (DGF)

- The European Commission can recognise the pivotal role of decentralised electricity grid projects and declare their intent to establish the DGF.
- In preparation for the DGF, the Commission could initiate a public consultation to address the specific needs and challenges encountered by DSOs.
- Announce a preparatory phase, with the aim to launch a pilot programme by 2025.

4.2. Regulatory Clarity for Member States

- Address an oversight of electricity grid funding within the vast scope of projects under the CPR.
- Declare that the Commission is looking for a balance between energy generation and decentralised electricity infrastructure.
- The Distributed Network Development Plans can be used to support Member States in investment strategies to reach EU targets.

4.3. Ensure Grants Benefit Regulated Businesses

- **Regulatory Incentives**: Emphasize the critical role of well-structured incentives and regulatory mechanisms for assets financed through grants.

- **Guidelines:** Develop guidelines for DSO incentive structures in cooperation with relevant stakeholders.
- **Feedback & Dialogue**: Follow-ups of regulatory treatment of assets financed by grants and foster dialogue between DSOs, Member States, and the Commission for improvements.