

Cost Sharing of Cross-Border Grid Projects in the EU: An Incentive-Based Negotiated Framework

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Cross-border electricity and gas interconnection projects are central to achieving the European Union's goals of energy market integration, green transition, system resilience, and a secure energy supply. However, these essential infrastructure investments frequently encounter financial roadblocks because the costs and benefits are rarely distributed evenly across different countries. Currently, the realization of these projects is hampered by a lack of transparency, known as information asymmetry. Project developers know the true value they expect to gain from a project and have incentive to understate this value to minimize their share of investments and maximise that of the EU. Furthermore, the EU's current financial support system - the Connecting Europe Facility (CEF)—often acts as an after-the-fact subsidy. This ex-post funding approach can inadvertently complicate negotiations and encourage strategic gamesmanship among stakeholders rather than fostering true cooperation.

The paper proposes a new conceptual framework that shifts the EU's funding from a passive subsidy to a proactive, strategic tool. Instead of evaluating costs and benefits as a single exercise, the new approach separates them to account for the fact that a firm's true benefits are private information. Under this new model, the EU utilizes CEF funding to cover the broader, EU-wide benefits of a project, such as market coupling and energy security, which lowers the remaining financial burden for the participating firms. Because the EU funding is conditional, the companies must negotiate with each other to cover the remaining costs. Since the project will only move forward if the companies reach an agreement, they are naturally incentivized to truthfully reveal how much they value the project. This dynamic forces a cooperative environment where firms will need to work together to secure the EU's benefits while competing fairly to minimize their individual costs.

The proposed framework offers several key benefits, primarily by structuring the funding as a negotiation requirement that forces companies to reveal their true willingness to pay to avoid the risk of the project failing completely. Consequently, the final cost allocation naturally settles into an arrangement where each firm pays a share that is directly proportional to its actual, privately valued benefits. This approach also ensures an efficient use of public funds, as the EU can calculate its financial contribution to provide just enough funding to make an otherwise stalled project viable, avoiding unnecessary over-subsidization.

Furthermore, the EU can present a "Menu of Options" with different project sizes and funding levels, allowing the negotiating firms to select the design that delivers the highest mutual value. Ultimately, this transparent, willingness-to-pay approach increases commercial confidence by signaling to financiers and national regulators that the projects are commercially viable and not reliant on inflated cost estimates.

To implement this framework and improve the efficiency of cross-border energy investments, the authors recommend specific policy shifts. First, the European Commission should use CEF co-financing strategically to unlock initial investments, rather than applying it as a static, one-size-fits-all subsidy. The specific share of this EU funding should be transparently tied to the value of system-wide EU benefits, such as security of supply or innovation. Additionally, regulators should integrate structured negotiation principles into standard cross-border cost allocation procedures to improve predictability and align national interests with broader EU goals. Finally, rather than using flat funding rates, the EU should calibrate its financial support on a project-by-project basis, prioritizing funds where small contributions yield the highest overall welfare gains.

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Publication	June 2026