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9th March 2011

Dear DECC,

CONSULTATION ON ELECTRICITY MARKET REFORM

I am responding on behalf of the British Hydrowater Association (BHA) to the consultation on Electricity Market Reform.

The BHA is the trade association for the UK hydropower industry. With around 160 members, the Association represents a wide range of interests: consulting engineering, design, manufacture, investment and operation, and specialist service providers. The BHA represents generators from small owner-operators to large UK and international companies.

We believe that carbon capture and nuclear power have a role to play but as a single technology association in the renewable area, the focus of BHA interest is on the issues relating to renewable energy. We are concerned that there may be unintended consequences in these radical proposals. They will, inevitably, introduce uncertainty at a time when financial markets remain fragile and projects in the pipeline may be delayed or cancelled. Projects developed under existing arrangements and projects already in the pipeline need to be protected.

The responses of the BHA to the consultation questions are attached.

Yours sincerely,

[Redacted signature]

RESPONSES TO THE CONSULTATION QUESTIONS

Current Market Arrangements

1. Do you agree with the Government's assessment of the ability of the current market to support the investment in low-carbon generation needed to meet environmental targets?

As a single technology association the BHA is not able to comment on the assessment.

2. Do you agree with the Government's assessment of the future risks to the UK's security of electricity supplies?

Yes

Options for Decarbonisation

Carbon Price Support

Feed-in Tariffs

3. Do you agree with the Government's assessment of the pros and cons of each of the models of feed-in tariff (FIT)?

4. Do you agree with the Government's preferred policy of introducing a contract for difference based feed-in tariff (FIT with CfD)?

5. What do you see as the advantages and disadvantages of transferring different risks from the generator or the supplier to the Government? In particular, what are the implications of removing the (long-term) electricity price risk from generators under the CfD model?

6. What are the efficient operational decisions that the price signal incentivises?

How important are these for the market to function properly? How would they be affected by the proposed policy?

7. Do you agree with the Government's assessment of the impact of the different models of FITs on the cost of capital for low-carbon generators?

8. What impact do you think the different models of FITs will have on the availability of finance for low-carbon electricity generation investments from both new investors and existing the investor base?

9. What impact do you think the different models of FITs will have on different types of generators (e.g. vertically integrated utilities, existing independent gas, wind or biomass generators and new entrant generators)? How would the different models impact on contract negotiations/relationships with electricity suppliers?

10. How important do you think greater liquidity in the wholesale market is to the effective operation of the FIT with CfD model? What reference price or index should be used?

11. Should the FIT be paid on availability or output?

The BHA is concerned that the wider introduction of feed-in tariffs (FiTs) is being made before experience of the introduction of FiTs for micro-generation. This is a high risk strategy that could put in jeopardy the development of low-carbon generation and security of supply. The RO, despite annual modification, has worked. It has increased renewable generating capacity and has helped grow the manufacturing and services base in the renewables sector.

Emissions Performance Standards

12. Do you agree with the Government's assessment of the impact of an emission performance standard on the decarbonisation of the electricity sector and on security of supply risk?

13. Which option do you consider most appropriate for the level of the EPS? What considerations should the Government take into account in designing derogations for projects forming part of the UK or EU demonstration programme?

14. Do you agree that the EPS should be aimed at new plant, and 'grandfathered' at the point of consent? How should the Government determine the economic life of a power station for the purposes of grandfathering?

15. Do you agree that the EPS should be extended to cover existing plant in the event they undergo significant life extensions or upgrades? How could the Government implement such an approach in practice?

16. Do you agree with the proposed review of the EPS, incorporated into the progress reports required under the Energy Act 2010?

17. How should biomass be treated for the purposes of meeting the EPS? What additional considerations should the Government take into account?

18. Do you agree the principle of exceptions to the EPS in the event of long-term or short-term energy shortfalls?

As the BHA represents a single technology, we do not feel able to comment on these questions.

Options for Market Efficiency and Security of Supply

19. Do you agree with our assessment of the pros and cons of introducing a capacity mechanism?

20. Do you agree with the Government's preferred policy of introducing a capacity mechanism in addition to the improvements to the current market?

21. What do you think the impacts of introducing a targeted capacity mechanism will be on prices in the wholesale electricity market?

22. Do you agree with Government's preference for the design of a capacity mechanism:

- a central body holding the responsibility;
- volume based, not price based; and
- a targeted mechanism, rather than market-wide.

23. What do you think the impact of introducing a capacity mechanism would be on incentives to invest in demand-side response, storage, interconnection and energy efficiency? Will the preferred package of options allow these technologies to play more of a role?

24. Which of the two models of targeted capacity mechanism would you prefer to see implemented:

- Last-resort dispatch; or
- Economic dispatch.

25. Do you think there should be a locational element to capacity pricing?

The BHA would welcome the introduction of a capacity mechanism. We believe that it would help to support the potential development of pumped storage hydro, which in the BHA's view would help to secure off-peak renewables generation, assist flexibility, and aid security of supply.

Analysis of Packages

26. Do you agree with the Government's preferred package of options (carbon price support, feed-in tariff (CfD or premium), emission performance standard, peak capacity tender)? Why?

27. What are your views on the alternative package that Government has described?

28. Will the proposed package of options have wider impacts on the electricity system that have not been identified in this document, for example on electricity networks?

29. How do you see the different elements of the preferred package interacting? Are these interactions different for other packages?

The interests of the BHA are in one sub-sector of the renewable industry. It is difficult for us to comment on the potential advantages and disadvantages of a package that covering the whole of the electricity market.

Implementation Issues

30. What do you think are the main implementation risks for the Government's preferred package? Are these risks different for the other packages being considered?

31. Do you have views on the role that auctions or tenders can play in setting the price for a feed-in tariff, compared to administratively determined support levels?

- Can auctions or tenders deliver competitive market prices that appropriately reflect the risks and uncertainties of new or emerging technologies?
- Should auctions, tenders or the administrative approach to setting levels be technology neutral or technology specific?
- How should the different costs of each technology be reflected? Should there be a single contract for difference on the electricity price for all low-carbon and a series of technology different premiums on top?
- Are there other models government should consider?
- Should prices be set for individual projects or for technologies
- Do you think there is sufficient competition amongst potential developers/sites to run effective auctions?
- Could an auction contribute to preventing the feed-in tariff policy from incentivising an unsustainable level of deployment of any one particular technology? Are there other ways to mitigate against this risk?

The BHA is concerned about the ability of auctions to set sustainable support levels for renewable technologies. We believe that the administrative process for setting support levels under the Renewables Obligation should remain.

32. What changes do you think would be necessary to the institutional arrangements in the electricity sector to support these market reforms?

We are unable to comment on this question.

33. Do you have view on how market distortion and any other unintended consequences of a FIT or a targeted capacity mechanism can be minimised?

The BHA is unsure how unintended consequences can be minimised. Uncertainty has already impacted market making the financing of new projects a problem.

34. Do you agree with the Government's assessment of the risks of delays to planned investments while the preferred package is implemented

The package does not fully take into account the risks for hydro developers who need a lead-in period for new arrangements of at least two years, preferably three years, because of the time it takes from project inception to commissioning and generation.

35. Do you agree with the principles underpinning the transition of the Renewables Obligation into the new arrangements? Are there other strategies which you think could be used to avoid delays to planned investments?

We would prefer to see the RO continue in its present form. We are concerned that the changes are too extensive and will lead to uncertainty, delays to projects and may make it difficult to meet renewable targets.

36. We propose that accreditation under the RO would remain open until 31 March 2017. The Government's ambition to introduce the new feed-in tariff for low carbon in 2013/14 (subject to Parliamentary time). Which of these options do you favour:

- All new renewable electricity capacity accrediting before 1 April 2017 accredits under the RO;
- All new renewable electricity capacity accrediting after the introduction of the low-carbon support mechanism but before 1 April 2017 should have a choice between accrediting under the RO or the new mechanism.

The BHA would prefer the RO to continue but of the options offered, the second choice would offer more flexibility.

37. Some technologies are not currently grandfathered under the RO. If the Government chooses not to grandfather some or all of these technologies, should we:

- Carry out scheduled banding reviews (either separately or as part of the tariff setting for the new scheme)? How frequently should these be carried out?
- Carry out an "early review" if evidence is provided of significant change in costs or other criteria as in legislation?
- Should we move them out of the "vintaged" RO and into the new scheme, removing the potential need for scheduled banding reviews under the RO?

The Government should continue with grandfathering. Projects were entered into in good faith and the terms under which they were initiated need to be protected.

38. Which option for calculating the Obligation post 2017 do you favour?

- Continue using both target and headroom
- Use Calculation B (Headroom) only from 2017
- Fix the price of a ROC for existing and new generation

BHA does not have a collective view on this issue.

