



16 August 2012

Matt Coyne
Department of Energy and Climate Change
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Dear Mr Coyne,

Airvolution Energy Limited (AEL) is an independent onshore wind farm developer established to develop, construct and operate small wind energy projects (2-15MW). We ideally look for sites on or near developed/brownfield land and often look to sell our electricity direct to a local high energy user. We are backed by a private equity firm called ESB Novusmodus and rely on the banking sector to build out our projects. As a result of this, we feel very tuned in to the needs and demands of the investment sector for independents.

In responding to this consultation, I am referring to the efforts of AEL in the PPA market for the past 6-12 months for the implementation of four of our consented projects, amounting to 16MW. However to provide a more in-depth response, I will also draw on my experience from my previous role up to October 2011 as Managing Director of Your Energy Ltd (YEL, now AES Wind Generation), an independent generator in the UK market. From 2005 to 2012, YEL successfully financed eight onshore wind projects totalling around 140MW).

I will respond using the appropriate guideline questions on page 15 of the call to evidence set out on the next page.

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Identifying the problem

1. Please could you provide a summary of your experiences with the PPA market over the past three years?

As mentioned in the introduction, I have been involved with the implementation of twelve consented onshore wind farm sites amounting to around 160MW both with YEL up to October 2011 and AEL since then. Between 2005 and 2009, YEL contracted PPAs with two of the "big six" utilities for five of our projects amounting to around 70MW but in the past three years we have noticed an almost complete withdrawal of the large utilities from the PPA market. There remains only a handful of small to medium sized players (aggregators) left to contract with and one or two foreign utility new entrants. During the period from 2009 to 2012, the next three projects in YEL's consented pipeline were contracted with a foreign new entrant, whose book quickly became swollen and is now harder to engage with as a result.

AEL are now seeking contracting parties to buy electricity from our four projects (and any more that might be consented in the future) and with the absence of the "big six" utilities and the huge demand on the foreign new entrants we are now faced with dealing with a very small number of independents, most of whom are not creditworthy for project finance lenders. Project finance lenders – who in themselves are also in short supply for small independent projects – require a PPA of between 7.5 and 10 years in length for security and a credit worthy entity backing up the purchase contract. This market is very thin indeed and we would support any initiatives to make it easier for onshore wind farm generators to have a "route to market".

2. Have you seen significant changes to the PPA market over the past three years, and if so, what do you think has driven this? If you have asked PPA providers for explanations of why changes have occurred, what reasons have been provided?

Yes, the big six utilities have pretty much exited the PPA market for small independent generators and there is a gross oversupply of renewable projects seeking power offtakers. As a result the commercial terms are deteriorating under the classic supply-demand dynamic. A few foreign utilities have entered the market and their contracts have been snapped up very quickly leaving a handful of small to medium sized power purchasers, often without a good credit rating. The reasons for this are not entirely clear and it would be best to ask the large utilities as to why they are more reluctant to write PPAs but surely a couple of obvious reasons must be (a) the uncertainties facing the electricity market and renewables in general; (b) oversupply of ROCs in certain cases and (c) pressures on the large utilities to invest in other power infrastructure projects.

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3. **How does the GB market for PPAs compare to other international markets? If you operate in other markets, how do PPA structures and terms differ? If terms differ what are the drivers behind the differences?**

We are a UK generator and do not have any experiences of international markets.

4. **What are the factors preventing or encouraging participation in the GB market? How (and why) do you expect these to change over time?**

Uncertain regulation is the overriding negative factor facing new investors in the GB market. The recent announcement on the ROC banding only provided pricing certainty for one year and this is clearly untenable when the development timeline for an onshore wind project from site identification to commercial operations is typically more than five years. The uncertainty will only increase as we approach 2017 and the introduction of the EMR system unless it is carefully managed.

5. **Do you expect the EMR package to change the PPA terms that you might offer/receive and if so how do you believe they will change? What do you think is the primary driver for these changes?**

We expect that the uncertainty created by EMR is likely to discourage the provision of PPAs and thereby make the terms offered increasingly uncompetitive and PPAs harder to obtain. We expect this to be the case over several years until any changes have had several years to "bed in" and institutional education and experience has risen. It would be a good idea to have some overlap / transitional period where both systems could work in parallel.

6. **What has been the determining factor in selecting a preferred PPA and PPA provider?**

That it had to be a bankable PPA provider, implying a highly rated parent company and at least a 7.5 year term.

7. **Have you seen a change in investment returns as a result of the changing nature of PPA terms and can you provide an example, including how this has been calculated? Do you expect the EMR package to change investment returns, and if so what is the driver for this?**

Yes, as outlined above due to supply-demand issues the returns coming from the current PPAs have deteriorated. Power purchasers are applying higher discounts to forward power prices to account for the increased volatility and uncertainty. For example, we are typically seeing power prices offered now for 2015 at a 30% discount to the Poyry Central forecasts. Smaller power purchasers also find it harder to account for the balancing risks in the electricity market and price that into their offering.

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Options to achieve the Government's objective

8. What are your views (costs, benefits and risks) on the potential options discussed in this call for evidence that may be necessary to achieve the Government's objectives?

The current state of the PPA market is extremely poor, and the main risk is that independent generators are entirely discouraged from proceeding with projects. The main objective should be to increase competition in the PPA market. It is unlikely that market-led initiatives will be sufficiently strong to encourage this, and we would encourage stronger measures such as competition measures and regulatory measures. We would like particularly to see measures to support independent aggregators, an offtaker of last resort and an obligation on large suppliers to offer a PPA on a commercial and timely basis. The process needs to be simplified considerably. A structure whereby renewable generators can get a guaranteed minimum payment (either from the ROC or FiT) and then choose to opt in or opt out of the power market is the easiest. Perhaps under EMR, the threshold for FiT projects should be increased to 20MW and suppliers are obliged to write PPAs for projects below this level, providing, of course, the current unworkable situation with respect accelerated depreciation is revised accordingly.

9. What are your views of the potential for market distortions and possible impact on the wider market?

We aware that RenewableUK and Scottish Renewables have made submissions highlighting the importance of the small scale renewable sector. The average size of an onshore wind farm in England currently is 12MW and the UK as a whole is around 20MW. This is an important sector and it should not face regulations that are distorted in favour of larger generators, such as offshore wind and nuclear power. This needs to be carefully managed.

10. Can you identify and explain any other viable options (voluntary, competition based, regulatory or otherwise) that should be considered?

All the points have been made in the previous questions – nothing more to add.

Please do not hesitate to get in touch should you require any more information and thank you for giving us the opportunity to comment on this important issue.

Yours sincerely,

Chief Executive

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