

CONSULTATION QUESTIONS

The Government's objective for the consultation process is to develop the evidence base on the options for reforming the electricity market. Therefore, respondents to this consultation are asked to provide evidence and supporting information to backup any opinions expressed in their response.

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?

We do not support removing an obligation on suppliers to source renewable generation. If there is a concern that the investment will not be forth-coming then the obstacles such as grid, planning, project funding should be tackled and the obligation not changed. It would appear from the consultation that is being changed for the sake of change.

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

Security of electricity supplies is a risk due to the lack of investment in infrastructure, energy storage and energy efficient programmes. Nuclear plant is not flexible, it is base-load. How can this base-load capability be matched with a variable wind generation plant. Flexible plant or significant storage needs to be included in the generation mix that is built in the UK.

Options for Decarbonisation

Carbon Price Support

This is the subject of a separate HM Treasury / HMRC consultation. Readers of this consultation with specific comments on the carbon price support mechanism should cover these in a separate submission to the HM Treasury / HMRC consultation, which can be found at http://www.hm-treasury.gov.uk/consult_index.htm

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)?

We do not accept that FIT with CFD will help enable smaller generators to enter the market. It would appear that the mechanism would be complicated and difficult to administer, hence turn investors to other markets. FIT with CFD appears not to be better than the current ROC

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system. A premium FiT is the preferred option.

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

No – As an independent developer, we believe that it will be impossible to project finance a project under this package. While it might ultimately be accepted by funders as low risk a significant time delay will occur until the risk profile is understood. This time delay is something that the UK Government cannot afford if the renewables targets are to be met.

The proposal to implement a feed in tariff over a low carbon obligation is intended to reduce or remove exposure to the volatility inherent in wholesale electricity prices. There is an assumption that removing or reducing this exposure, the financing costs generators face are reduced accordingly, and in turn so are the costs transferred to the consumer. We are fearful that the Contract for Difference mechanism will actually increase financing costs.

The Contract for Difference system will require liabilities to sit on a generator's balance sheet for an as yet unidentified period of time. These liabilities will be difficult to forecast, as do not have a trading function. The bankability of such a proposition is questionable, and is likely to further enhance the risk generators are exposed to. This could then increase the financing costs they are expected to bear. Not only will this affect the feasibility of investment in renewable resources, but could affect those marginal projects that may have gone ahead under current market arrangements

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?

Cheaper financing – would be the theory however we suspect in practice that funders would extract the saving elsewhere in the credit agreement and the economics on individual projects would take a further reduction. A must take the power scenario without utilities taking of 15% of the £mwhr rate to manage so called risks would be very attractive.

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?

Good wind farm operational management drive us to undertake maintenance and repair work when it is not windy. Forecasting tools are already in place to maximise the availability of the turbines. The proposed policy would have no impact on the way that wind farms projects are currently operated. If the proposed policy were to reduce the £MWhr revenue value below the current and/or expected levels then we would reconsider our investment in new wind projects in the UK.

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?

The case for change does not seem particularly well developed or presented. When replacing the Renewables Obligation with a Feed in Tariff, the Redpoint analysis details reductions in hurdle rates for both renewables and nuclear technologies.

Firstly, we do not see that the rates detailed in the Redpoint analysis are representative of the Returns on Investment for both utilities and independents. Secondly, these intended reductions are relatively slight and there exist significant complexities and fundamental uncertainties yet to be resolved relating to revenue support mechanisms (and namely a Contract for Difference) and across the wider policy and regulatory landscape.

Such enormous amounts of complexity and uncertainty create further barriers to market entry, and will negate such slight reductions in hurdle rates. There exists the potential for reversal of these intended reductions, and the possibility of an actual increase in hurdle rates for renewables technologies, which would be unwelcome considering the requirement for accelerating renewables investment.

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?

The premium FIT mechanism is really the only proposal that is likely keep the existing investor base. New investors are unlikely to enter the market until the FIT mechanism has operated for a year plus.

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?

Removing the current obligation from suppliers to source renewable removes an important incentive for suppliers to provide a pathway for low carbon generation to reach consumers and will adversely impact smaller market participants such as ourselves.

Currently, electricity suppliers are obliged to source a specific and increasing proportion of their electricity from renewable sources. If this obligation is not met via purchasing renewable power, suppliers face paying a financial penalty that outweighs the cost of purchasing renewable power in the first instance.

If suppliers are no longer obligated to purchase renewable power, generators could then be exposed to a significant degree of offtake risk. In these circumstances, higher discounts could be applied to the terms of a Power Purchase Agreement. Consequently, the revenues a generator would expect to receive under this contract would decrease.

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When securing financing, banks prefer the certainty of long term power contracts. If these are more difficult to secure because an obligation to provide them has been removed, the transfer of risk to the financial institution will be complemented with an increased cost of capital for the generator.

This potential squeeze on revenues and costs will make us review our renewable energy investment in the UK market and most likely transfer our investment to other more favourable markets.

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?

The Ofgem liquidity review has a crucial interdependency with the reform proposals and we see it as important that the liquidity review is considered as part of this exercise and not a separate exercise.

Liquidity is particularly important for the effectiveness of Contract for Difference as the mechanism is reliant on an effective reference price and the assurance that generators will find a route to market in the absence of a supplier obligation.

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

Output is the established mechanism. It is not clear how the FIT would be paid on availability.

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?

No comment

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?

No comment

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?

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No comment

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?

No comment

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

No comment

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

No comment

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

No comment

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?

For renewables to achieve maximum penetration onto the grid network, a flexible system and generation plant mix is required.

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

The introduction of a capacity mechanism is excepted provided the improvements to the current market provided that renewables remains at least as attractive as at present in order to meet the mandated targets.

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

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We would hope that the use of such a mechanism would not significantly impact on the wholesale electricity price however it will depend on how the different types of resources are procured.

22. Do you agree with Government's preference for a 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.

Targeted mechanism preferred

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?

Technologies could play a role if a targeted mechanism is used

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

- Last-resort dispatch; or
- Economic dispatch.

It is difficult to form a view on the proposals without more detailed information

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

Yes.

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?

No – premium FiT is our preferred options as it is the simplest of the packages proposed and other than maintaining the ROC gives the best probability of achieving the mandatory targets.

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

There has been very little communicated as to how an auction process applicable to the UK could be designed, especially given the need for the UK to accelerate investment in renewables.

The uncertainty and increased risk that investors would be expected to bear under an auction process is not an attractive proposition for the industry. As such, it is difficult to see how this proposition would be attractive to that broader pool of capital needed to accelerate investment levels.

We oppose the introduction of auctions as a means of setting support levels, and support the retention of an administrative process for setting support levels.

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?

No comment

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

No comment

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?

Banks and funders will not be comfortable with the Contract for Difference mechanism risk and the fact that revenues receipted may have to be paid. It is unclear who will contract

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with who for the CfD which is another risk that funders will need time to get comfortable with. A system that is too complicated will drive investors away from the UK market which is an unthinkable consequence and will mean that the renewables targets are not achieved.

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?

How the auction system would work has not been explained particularly well in the document. Without the basic fundamentals of how such a system would work and how it would impact on renewables projects and technologies it is difficult to give any view. As an organisation we are against the introduction of auctions as it makes project financing almost impossible. It is a further development risk that we are not prepared to fund.

- Should auctions, tenders or the administrative approach to setting levels be technology neutral or technology specific?

No other comments than noted above

- 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?

This would seem a reasonable approach however we do not support a contract for difference mechanism.

- Are there other models government should consider?

The existing ROC model as it works and is understood by industry, funders, investors and Government. It is a false strategy to think that the price of electricity can be reduced with level of investment required in infrastructure, renewables, convention generating technology, etc.

- Should prices be set for individual projects or for technologies

Technologies would appear to be the simplest approach.

- Do you think there is sufficient competition amongst potential developers / sites to run effective auctions?

Against auctions. Auctions for sites in the past effectively stopped development of onshore wind. Developers have well tried and tested tools for selecting sites. Running

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an auction process will reduce bidders to the major utilities which would make the market even more closed than it is today.

- 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?

A significant reduction in the overall all £MWhr will stop development of most wind sites in the UK

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

In Scotland the grid network needs to be split away from the generation and supply businesses.

Ofgem and DECC need to be given more teeth and be organised to make sure that the arrangements are managed efficiently and have the ability to change quickly if it is not working.

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 broad principles of the proposals must include:-

- Viable levels of income for typical projects, and not just the best.
- Clear route to market at initiation of development.
- Certainty and stability for a reasonable period of time.
- Protection of existing operational projects, and of projects already in construction and of projects in the formal planning process (planning application submitted)
- Clear process map for implementing the changes.

We are deeply concerned that there exists enormous potential for unintended consequences, given both the complexity of the proposals and the significant lack of clarity within the proposed package.

34. Do you agree with the Government's assessment of the risks of delays to planned

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investments while the preferred package is implemented?

Yes – but potentially it will take 2 to 3 years to get investment moving again if the implemented mechanism does not work.

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?

Need to receive more detail on how the transition arrangements will work, however, the ROC banding review is likely to stop investment, development and construction of new projects until FiT levels are known.

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 - Preferred.

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 changes in costs or other criteria as in legislation? – Preferred.
- 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?

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 - Preferred