

Response of INEOS Chlor Limited to the specific questions posed by DECC in the Electricity Market Reform consultation. This should be read in conjunction with the main part of our 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 believe the current market may well fail to deliver the Government's desired investment in low carbon generation. Alongside the proposals for a Feed in Tariff, we believe there may be opportunities for Government, Energy Intensive Industry and low carbon generators to work together to deliver *both* investment in low carbon generation and a secure future for Energy Intensive Industry in the UK.

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

We would be concerned at security of fuel supply should the UK invest solely in CCGT to replace coal generation retiring in the coming years. Our concerns regarding the adequacy of the UK's gas storage are a matter of record and our view has not changed.

We are not convinced of the need to introduce capacity mechanisms to address this.

## **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 agree with the assessment.

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

We believe FIT with CfD represents the best policy option.

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?

We recognise that the Government fully intends to pass risks onto energy consumers, and that the ultimate transfer is from generator to customer, with the Government "brokering" the arrangement. More broadly however we believe that moving price risk from the generator, whilst leaving operating risk, is likely to provide the best overall value.

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?

No comment

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?

No comment

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?

No comment

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?

No comment

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?

We believe a successful reference price is vital to the proper functioning of an electricity market. It is almost inconceivable that a CfD could operate successfully without one.

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

Output

## **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?

We believe an EPS will increase supply risk with little or no benefit for decarbonisation of the electricity sector.

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?

We do not believe EPS is appropriate at any level.

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?

We do not believe EPS is appropriate at any level. If introduced it must not apply to existing generation.

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?

We do not believe EPS is appropriate at any level. It should not be introduced, and if it is, should not be extended to cover existing plant.

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

We do not believe EPS is appropriate at any level.

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

No further comment

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

We do not believe EPS is appropriate at any level.

## **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?

No. We do not believe a capacity mechanism is currently required. Existing mechanisms may well be sufficient, and there is no pressing need to introduce legislation now. The government should consult further on this.

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

No. We would like to see significantly more work on this.

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

We are concerned that it would be unnecessary and add extra costs.

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

- a central body holding the responsibility;

- volume based, not price based; and
- a targeted mechanism, rather than market-wide.

No. We would like to see significantly more work on this.

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?

As a very significant demand side provider of response services, we believe simplicity is the key. As ICI Chlor-Chemicals we responded in 1999 to the Government's Review of Electricity Trading Arrangements noting, "OFGEM's over reliance and optimistic expectation that the demand-side will participate extensively in the new market". Our key point was that the markets were too complex, too risky and too opaque to allow significant demand side response. We remain convinced of these points.

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

- Last-resort dispatch; or
- Economic dispatch

We do not believe the case is yet made for a capacity mechanism

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

We believe there is a case for more work on these issues to allow a better informed debate.

## **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?

We have set out our position on these issues independently. We do not believe carbon price support adds in any way to the package of measures (particularly FIT).

27. What are your views on the alternative package that Government has described? See 26 above

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?

No comment

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?

We would like to see more debate on these issues. We would simply note that previous regulatory attempts to create "competition" in utility supply through auctioning has not in our view been in any way successful.

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

No comment

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?

We would like to see more debate on these issues.

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

No comment

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?

No comment

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

No comment

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?

No comment

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

No comment

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## **Electricity Market Reform – DECC Consultation Response from INEOS Chlor Limited**

INEOS Chlor welcomes the chance to respond to the consultation on Electricity Market Reform. INEOS Chlor is a manufacturer of chlorine and caustic soda with operations in the UK, Norway, Germany and Sweden. The electrolytic processes we operate are very energy intensive, and electricity is a key raw material representing approximately 60% of our manufacturing costs.

### **Feed-in Tariff and support for low carbon generation**

We are supportive of plans to make the transition to a low carbon economy and welcome the recognition of the need to renew the UK's generation capacity. We have publicly stated our support for new nuclear generation in the UK and recognise the difficulties in investing in high capital long term projects within an uncertain market. We are however extremely concerned that this support adds to energy costs in the UK and creates an equal but opposite certainty of undermining investment in energy intensive industry. The cumulative burden of energy taxes is creating a bleak outlook for our industry in the UK.

The Government now proposes two independent measures to provide support for low carbon investment in the UK. It is difficult to understand why both measures are required. If the Feed in Tariff is set at an appropriate level to support new investment, what purpose does Carbon Price Support serve other than as a taxation stream for Government? For this reason, our support for the proposed Feed in Tariff must be qualified.

We believe a flourishing energy intensive sector is vital to the successful decarbonisation of the UK and European economies. Decarbonisation and the reduction of man-made carbon emissions will be best achieved if:

- the UK becomes a low carbon economy, in particular with respect to energy (electricity) production, and
- the UK manufactures the energy intensive goods it requires within this low carbon economy.

We see clear evidence of a considered plan to achieving the first of these aspirations - unfortunately there is no evidence that due regard has been given to the latter. We urge the Government to consider how the support being provided to low carbon generation can be managed whilst ensuring that Energy Intensive Industry survives the transition from a fossil fuel economy to a low carbon one.

The recognition of the need for new nuclear investment, and the desire of UK Government to provide the framework to enable this investment represent a unique opportunity to bring together energy, climate and manufacturing policy. Nuclear power is ideally matched to the requirements of Energy Intensive Users. We note that the French government has recently assisted Energy Intensive Industry through brokering a long term supply agreement between the Exeltium consortium and the French nuclear generator. Through the deal industry receives competitive energy, and the nuclear generator receives financing for the next generation of nuclear power stations. If the Government can secure commitments to deliver a similar scheme

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from UK nuclear generators, in return for (and as part of) the suite of measures targeted at providing support for new nuclear, these critical policy issues could be delivered together.

**We urge the government to seek commitments from nuclear generators to provide an “Exeltium” like arrangement in the UK in return for the supportive legislation currently proposed.**

## **Capacity Payments**

We remain to be convinced of the need for a capacity payment. We recognise the challenge of providing back-up generation to intermittent wind, but believe that existing market mechanisms, for example Short Term Operating Reserve, may be more than adequate to provide such a service. In any case it is clear that there is no requirement for a capacity payment now, and no need to introduce legislation to provide for one at this stage.

We would urge the Government to consult more widely on this aspect.

## **Emissions Performance Standards**

We do not believe that an Emission Performance Standard is an appropriate mechanism for managing CO<sub>2</sub> emissions. We believe that the current CO<sub>2</sub> market provides the appropriate distinction between high and low carbon technologies, and that an artificial “ceiling” could be hugely counterproductive. Market participants, who are best placed to invest in the market, should have the ability to decarbonise in the way they choose.

We run the risk of creating a high priced electricity market that attracts high carbon electricity from abroad through interconnection, at the expense of UK generators and jobs.

## **Reforms to the electricity market –**

In addition to the comments above, we make a number of observations as “independent operators” in the UK electricity market with experience of the German EEX and Scandinavian NordPool markets.

We find the current UK market significantly more difficult to trade than its European counterparts. The lack of a suitable “reference price” 10 years after the market’s introduction is little short of damning. Liquidity is poor, innovation and competition from suppliers is almost non-existent.

We believe there are a number of structural problems within the UK electricity market.

- vertical integration among electricity suppliers significantly inhibits liquidity and competition;
- the UK market is the most complex in Europe – it cannot be the case that the UK is inherently more complex than Germany, Norway, Belgium etc.



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We have designed complexity into our market, and frequently seek to add more. We believe the codes of governance are flawed. Too often change is driven by economic theory to “allocate costs where they arise”, with little regard to the complexity this creates. The key to an active market, open to all not just the few, is simplicity. We believe all market changes must be judged in part by the effect they have on complexity, and that market governance should have simplicity as an objective;

- alongside this, we have created perhaps the most risky market in Europe. The dual cash out, and the “sharpening up of price signals” can only seek to re-inforce the “big is beautiful” model of electricity supply and generation in the UK. NordPool and EEX survive and flourish on far less punitive cash-out arrangements. It is not co-incidence that smaller independent suppliers have failed to survive in the UK;
- the lack of a reference price must be addressed now to allow risk-free financial trading. As a company we can access reference prices for Germany back to the market opening in mid 2000 and similarly a wealth of reference price data on NordPool, and in the UK on NBP gas. There is no such definitive price list for UK power.

We would urge the UK Government to look closely at the successful power markets across Europe, and to base reform on the key elements of these markets.

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