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Matt Wieckowski
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DECC.capacity.mechanism@decc.gsi.gov.uk

Dear Matt

Response to the Government Electricity Market Reform Annex C Consultation on possible models for a Capacity Mechanism – Issued 12th July 2011

About AEP

1. The Association of Electricity Producers (AEP) represents large, medium and small companies accounting for more than 95 per cent of the UK generating capacity, together with a number of businesses that provide equipment and services to the generating industry. Between them, the members embrace all of the generating technologies used commercially in the UK, from coal, gas and nuclear power, to a

wide range of renewable energies. Members operate in a competitive electricity market and they have a keen interest in its success, not only in delivering power at the best possible price, but also in meeting environmental requirements. Contact details for the Association are provided at the end of this paper.

Member Views remain split

2. As you have been made aware from the various meetings Department of Energy and Climate Change (DECC) has conducted since the publication of the Electricity Market Reform (EMR) White Paper in July 2011 and specifically during this consultation phase on possible models for a Capacity Mechanism, our members remain wedded to a broad spectrum of views on the subject of EMR generally and specifically, for this Consultation on Possible Models for a Capacity Mechanism. There is a broad range of views, including those who strongly support and those who strongly oppose the principle of a Capacity Mechanism with a number who are still undecided on the matter due to the need for significantly more detail to be provided by the DECC EMR Project Team. However, we would like you to note that there is a widespread view that there are significant challenges associated with the two specific options outlined in the Consultation Paper, the Strategic Reserve and the reliability contracts model. Members have undertaken to submit individual responses to the specific questions included within Annex C therefore we will not duplicate those within our response. We focus here on general issues of programme delivery on which there was agreement and trust that will add value to your deliberations.

Process

3. We congratulate the DECC EMR Project Team for its efforts to engage with a wide spectrum of industry representatives during this consultation process. The AEP membership has benefitted from ongoing discussions on a number of areas currently under development. Both our members and DECC had an extensive list of significant issues to address, in what has been an incredibly short period, in order to ensure delivery of proposals that would enable, through the reform of the electricity market, arrangements which would attract crucial long term investment in development of low carbon energy production throughout GB.
4. Whilst we recognise the effort that DECC has made in engaging with industry we would suggest that this needs to be put on a more formal footing as we move to develop the detail of the arrangements and later on implementation. We would suggest a process similar to that adopted when NETA was introduced, which had an overarching steering group with a number of working groups covering specific issues. This then becomes an open and transparent process by which all of industry can engage.
5. Government should also provide a clear indication of policy areas which it intends be retained for central amendment and issues which may be devolved to industry

for enhancement and further development. a belief in market principles as the most effective way to organise the electricity system and therefore a desire for DECC to commit to market principles to the maximum extent possible; with targeted policies specifically aimed at identified market failures but no 'policy scope creep'.

6. Whilst acknowledging that views differ regarding whether the introduction of a capacity mechanism should be introduced, members would prefer a scheme which is sufficiently stable and predictable to incentivise long term investment, maintains a competitive approach to energy production and the procurement of capacity, that it should be insulated from political intervention, and that it should focus on ensuring there is sufficient capacity to meet demand and not on other extraneous goals such as environmental objectives
7. It is essential that there is an opportunity to subject the eventual overall design to an impact assessment of known European Commission requirements as we believe that we have only a very narrow window of opportunity through which we can get right the design, backed up by clear deliverables. It would be unfortunate if there was any need to undo aspects which form the heart of this significant body of work and potentially affect adversely the balance of the overall intended design.
8. It is important that our members fully understand the proposals in order that they can fully assess the risks and rewards, articulate, and perhaps even enthuse about, the eventual new electricity market initiatives.

Minimum Project Deliverables

9. It is important to acknowledge the full extent of the challenge set by the overall objectives that reform of the electricity market is actually seeking to achieve. We need to deliver decarbonisation whilst ensuring secure electricity supplies and maintaining cost-effective delivery.
10. Our members would be supportive of an emerging clear direction from Government by the time of the Technical Update document to be produced at the year-end allowing for the introduction of legislation at the start of the second Parliamentary session in May next year. During the development of the New Electricity Trading Arrangements, which took around four years of development, industry was given a clear steer from Ministers about the direction of travel. We believe there would be benefit in adopting a similar approach for EMR. If industry and therefore investors are able to see an overview of the final objectives, then we can all begin designing appropriate vehicles to ensure delivery. It is imperative that timely progress is made on more detailed design work so that primary legislation might be brought forward with a clear indication regarding expectations around delivery.
11. In support of such an approach we would request that the EMR proposals are accompanied by a thorough set of worked up examples in order that industry is able to undertake an initial 'sense check' to be comfortable that the overall design

delivers exactly what it is expected to. If there is an opportunity to 'scrutinise and understand' then we believe that there will be significant benefit in that:

- a) There should be a clear understanding regarding the direction of Government Policy which will ensure that those who wish to attract investment have been able to fully assess the risks and rewards against a known set of criteria associated with the overall market design;
- b) There should be clear evidence that the proposals would work for both the supply and demand side of the industry. It follows that this should therefore encourage significant and necessary development of capability within the demand side;
- c) There should be an opportunity to provide a clear explanation of expected costs of the total package in order that consumers are able to understand the potential impact on their energy bills;
- d) Industry will be working within an agreed timetable for review of the scheme in order that any design enhancements may be undertaken if necessary, and
- e) It should be clear that there is a commitment to maintaining an effective investment framework during the transition.

Options that could promote Investor confidence in the chosen GB Model

- 12. Members believe that it is vital that industry has access to an overview of how all ongoing initiatives, for example the raft of current and planned Ofgem initiatives comprising the future structure of charging to be delivered by Project Transmit, the impact and integration of amended outturn electricity prices potentially resulting from an Ofgem significant code review of electricity cashout or actual delivered levels of offered energy resulting from the Ofgem liquidity initiatives, fit together with any and all of the EMR proposals. In addition it is vital that the impact of gas developments is not ignored as changes to the gas regime will have a significant impact on the Government's overall energy policy aspirations.
- 13. Members are concerned that there should be no surprises, because we acknowledge that we do not have time to get this important initiative wrong. In the very near future, the UK MUST succeed in attracting significant investment in generation, infrastructure, storage and a raft of new technologies, including Carbon Capture and Storage, in order to deliver both the Government's on shore and off shore low carbon aspirations.
- 14. It is essential that there is an overarching blue print detailing all centrally planned Government initiatives made available for further development with industry. This would offer an opportunity for stakeholders to be able to assure themselves that the numerous individual initiatives that form part of the total overall energy market

design do not promote unintended consequences which might devalue the projected deliverables that are to form part of the overall workable market design.

15. We believe that such a clear outline of the overall policy framework, with a clear prioritisation of objectives would strengthen any investor message in that it would create a **long term view** of what the end goals and design are intended to deliver. Once the market has satisfied itself that the design is fit for purpose, as we did with the New Electricity Trading Arrangements, we will work together to ensure a timely and appropriate delivery and implementation plan.
16. Government must ensure that a clear overview of expected outputs, monitoring procedures and reporting is developed with industry in order that it is able to assess the success of delivery of the overall design.

Conclusion

17. AEP members acknowledge the need to attract future investment and are committed to provide all necessary resource to ensure development and eventual delivery of a model for electricity market reforms which enable Government targets to be met at an appropriate cost to both the industry and consumers.
18. If you require any further information please contact [REDACTED] Head of Electricity Trading on [REDACTED] or the email [REDACTED].

Yours sincerely

[REDACTED]

Chief Executive

(By email)

