

## Electricity Market Reform Consultation 2011 – Response from Wessex Water Services Limited (WWSL)

- WWSL acknowledges and supports the needs for the UK economy to decarbonise.
- However the current suite of instruments relating to this aim (including CCA, EUETS, CRC as well as RO and now FiTs) are potentially confusing and there is a risk that carbon support pricing, further changes in FiTs and EPS will add to this confusion.
- These reforms present an opportunity to simplify some measures in this diverse mix of initiatives. A simplification of the CRCEES would be to treat renewable generated electricity as zero carbon regardless of any other subsidies. We feel this would not impact on the efficiency of energy use but would send a stronger signal for the development of renewable electricity projects.
- WWSL welcomes changes that help provide:
  - i) a fair reward for investment in renewables
  - ii) predictability of that reward as both a consumer and a renewable energy generator
  - iii) a stable and liquid power market with extended price visibility
- WWSL would also like to see revenues from revenue raising mechanisms put back into both UK renewable generation and used to protect vulnerable customers.

Ref:	Queries and Responses
Q1	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?
A1	Yes. Investment in generation is required and the move from primarily fossil fuelled generation to a greater share of renewable and low carbon sources is essential. The mix of carbon price support with renewable incentivisation sends the right messages. However there is a view that a pure carbon tax would send a clear message to the market and allow it to respond with optimal solutions. This would also simplify implementation and limit the additional mechanisms added to a market already faced with a myriad of different schemes all intended to promote decarbonisation. Also the UK is competing for global capital and resources in the area of power generation so must make the UK attractive to investment from the global capital markets.
Q2	Do you agree with the Government's assessment of the future risks to the UK's security of electricity supplies?
A2	Yes – Retirement of ageing plant combined with the UK's environmental commitments make it vital to stimulate timely investment. However demand growth may be overstated and depends on the degree to which renewable electricity is used to support wider decarbonisation. There is an argument that such a "predict and provide policy is not optimal for the electricity market. Arguably optimum solutions should arise from operation of the market ("market forces") itself rather than from Govt. Never the less, security of electricity supply is paramount to the water industry whose reliable function is essential to ensure public health and so the industry welcomes the importance placed on security of supply by Govt..
Q3	Do you agree with the Government's assessment of the pros and cons of each of the models of feed-in tariff (FIT)?
A3	Yes. In particular CfD FiTs provide a high level of price certainty while still requiring skilful market trading to ensure the revenue stream

	expected and so helping minimise cost to the consumer while contributing to market liquidity.
Q4	Do you agree with the Government's preferred policy of introducing a contract for difference based feed-in tariff (FIT with CfD)?
A4	Yes
Q5	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.
A5	Much more price certainty and hence cheaper and easier finance. However the price setting mechanism is very important as it will set longer term market expectations which could on the one hand be insufficient to stimulate the desired investment while on the other hand could potentially result in over rewarding low carbon generators to the detriment of customers.
Q6	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?
A6	Efficient operation, despatch and utilisation contribute to and are incentivised by a liquid and so competitive market.
Q7	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?
A7	Yes –subject to modelling reliability and assumptions
Q8	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?
A8	Fixed and CfD FiTs seem both likely to increase investment significantly more than premium FiTs. However CfD FiTs also incentivise competitive market participation.
Q9	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?
A9	VIUs would invest and source more from low carbon generation. Existing gas generation would still have a key role due to its flexibility and also lower emissions than coal so impacted by a lower carbon price support burden. Renewable generation should increase due to improved price certainty and returns stimulating greater levels of investment. New entrants should also be attracted by these improved returns and easier availability of finance. New investment from Europe may become available as the FiTs mechanism is commonly used and well understood in Europe.
Q10	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?
A10	Very important as the generator will need to trade effectively to ensure getting full return on its output and a liquid market is necessary to

	promote value certainty. Reference price is clearly important and should be set commercially.
Q11	Should the FIT be paid on availability or output?
A11	Output as the point of renewable generation is its low carbon output as generally it is not readily despatchable. Availability is a more appropriate way of rewarding plant capable of despatch but that may not be called to run or to run so as to maximise output.
Q12	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?
A12	Yes but could this not be better achieved by setting carbon price support at a level that drives operators to reduce carbon emissions while doing so via their commercial decisions.
Q13	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?
A13	450g/kWh would send a strong signal of the Govt's commitment to decarbonisation. This tighter limit may require derogations to enable some processes to be trialled and so such derogations should be granted for demonstration projects.
Q14	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?
A14	Yes. Retrospective application would only hasten or precipitate the closure of older coal plant risking security of supply.
Q15	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?
A15	Yes
Q16	Do you agree with the proposed review of the EPS, incorporated into the progress reports required under the Energy Act 2010?
A16	Definitely yes
Q17	How should biomass be treated for the purposes of meeting the EPS? What additional considerations should the Government take into account?
A17	
Q18	Do you agree the principle of exceptions to the EPS in the event of long-term or short-term energy shortfalls?
A18	Yes. To ensure security of supply, particularly as the UK is moving toward a market containing more inflexible and intermittent generation.
Q19	Do you agree with our assessment of the pros and cons of introducing a capacity mechanism?
A19	It lacks detail regarding interactions with other proposed changes e.g. carbon price support which may hasten some plant closures so increasing the need for additional capacity or peaking plant to compensate.

Q20	Do you agree with the Government's preferred policy of introducing a capacity mechanism in addition to the improvements to the current market?
A20	Yes. Needed for peaking plant
Q21	What do you think the impacts of introducing a targeted capacity mechanism will be on prices in the wholesale electricity market?
A21	It will increase price as greater levels of backup availability requires but still a relatively small impact – at least in earlier years.
Q22	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.
A22	Yes – NGT preferred as central body? Yes. Yes
Q23	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?
A23	If properly designed this is likely to improve/stimulate investment in demand response plant and innovative load shedding strategies
Q24	Which of the two models of targeted capacity mechanism would you prefer to see implemented: Last-resort dispatch; or Economic dispatch.
A24	Economic despatch
Q25	Do you think there should be a locational element to capacity pricing?
A25	Yes – as this would send the correct price signals to incentivise generation build in areas where it is most needed while helping reduce transmission and distribution losses.
Q26	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?
A26	Yes. However the volume of initiatives could create confusion and uncertainty.
Q27	What are your views on the alternative package that Government has described?
A27	Thought unlikely to stimulate as much new generation and unlikely to attract as much investment as CfD FiTs.
Q28	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?
A28	Almost certainly. The enabling legislation will need careful consideration and drafting so that unexpected outcomes can be properly managed or accommodated
Q29	How do you see the different elements of the preferred package interacting? Are these interactions different for other packages?
A29	There are now a lot of initiatives being rapidly deployed by the Govt and there is a real concern that this could lead to confusion and uncertainty neither of which are good for investment. It could also



	result in scope for gaming and will almost certainly involve high levels of bureaucracy. All of the above could significantly reduce the desired effect and lead to sub-optimal outcomes.
Q30	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?
A30	
Q31	<p>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?</p> <p>Can auctions or tenders deliver competitive market prices that appropriately reflect the risks and uncertainties of new or emerging technologies?</p> <p>Should auctions, tenders or the administrative approach to setting levels be technology neutral or technology specific?</p> <p>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?</p> <p>Are there other models government should consider?</p> <p>Should prices be set for individual projects or for technologies</p> <p>Do you think there is sufficient competition amongst potential developers /sites to run effective auctions?</p> <p>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?</p>
A31	Such mechanisms could prove a barrier to smaller players
Q32	What changes do you think would be necessary to the institutional arrangements in the electricity sector to support these market reforms?
A32	
Q33	Do you have view on how market distortion and any other unintended consequences of a FIT or a targeted capacity mechanism can be minimised?
A33	Careful consideration and drafting of the enabling legislation
Q34	Do you agree with the Government's assessment of the risks of delays to planned investments while the preferred package is implemented?
A34	
Q35	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?
A35	
Q36	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:

	<p>All new renewable electricity capacity accrediting before 1 April 2017 accredits under the RO;</p> <p>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.</p>
A36	Choice of the subsidy mechanism is favoured
Q37	<p>Some technologies are not currently grandfathered under the RO. If the Government chooses not to grandfather some or all of these technologies, should we:</p> <p>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?</p> <p>Carry out an "early review" if evidence is provided of significant change in costs or other criteria as in legislation?</p> <p>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?</p>
A37	
Q38	<p>Which option for calculating the Obligation post 2017 do you favour?</p> <p>Continue using both target and headroom</p> <p>Use Calculation B (Headroom) only from 2017</p> <p>Fix the price of a ROC for existing and new generation</p>
A38	