

Welcome to The e-POWER Bulletin!

The e-POWER Bulletin aims to provide a unique focus, giving you - the generators - just what you need to know when selling your renewable power. No more, no less. In this issue we take a look at:

- DECC capacity market reform proposals and the potential impacts on embedded benefits;
- Implications of the 2016 budget for renewables generators;
- trends in wholesale power prices;
- Proposed changes to transmission charging by the CMA;
- an analysis of the January 2016 e-POWER auction; and

- the latest e-ROC auction results.

Additionally, e-POWER will have a stand at [All Energy Conference](#) on 4th and 5th May, and I will be speaking at the Bio-energy, Community and Local Energy sessions, both on the first day of All Energy. We hope to see you there.

Whether you're a prospective or existing e-POWER user, the aim of this newsletter is to meet your needs. So if it doesn't hit the spot or you've got ideas for future content, I would love to hear from you.

Thanks for reading,

Stuart Stephens



DECC proposes capacity market reforms

The government has unveiled a series of significant changes to its capacity market regime.

The capacity market mechanism has been put in place to ensure Britain's security of electricity supply over the medium term. It sees sources of capacity offered subsidies for ensuring their availability at times of system stress.

Generators and demand-response providers secure subsidies through a competitive auction, which sets the level of capacity payments. The level of capacity to be auctioned is determined by the Secretary of State, and is based upon National Grid's *Electricity Capacity Report*.

The capacity market is technology neutral. Most types of capacity can participate, including new and existing generation plant, storage, demand side response and interconnector capacity. Technologies are only excluded if they are in receipt of other subsidies, or have a Short-Term

Operating Reserve (STOR) contract that extends beyond the capacity market operational year.

DECC review

On 1 March [DECC announced a consultation](#) proposing major reforms to the capacity scheme, among concerns that it is failing adequately to support the government's energy objectives. In particular, the government is concerned about the lack of new gas capacity being brought forward, a key policy objective for the government.

But the proposed changes also reflect wider developments in the current market conditions and uncertainty about the future supply picture.

As a result, the wide ranging proposals could impact renewables and embedded generators not involved in the capacity market.



New proposals

DECC had already been reviewing the capacity market following the first two auctions, which were held for the delivery of capacity in 2018-19 and 2019-20. The department said it had received a clear message from industry and investors that the mechanism retained their confidence. However, feedback was also clear that the volume of procured capacity would need to rise in order to bring forward significant new capacity.

In response to this, DECC is proposing to buy more capacity and to buy it earlier. The next T-4 auction in December 2016 will purchase up to 3GW more capacity than would otherwise have been the case. The theory is that, by increasing the level of capacity and thereby raising the clearing price, new build gas is more likely to be successful in the auction. The government is confident that there is a healthy pipeline of gas projects ready to take advantage of the change; however, there is no certainty on what technologies may come forward.

Further, DECC has proposed to bring forward the first capacity market delivery year to 2017-18. It would not be possible for developers to deliver new gas plant in time for this, and so the capacity gap will likely be filled out by existing generation such as energy from waste sites. The staging of this early auction will allow the National Grid to close the requirement for its Contingency Balancing Reserve for that year.

Diesels impact on the wider market

DECC has also heard complaints that diesel engines are being given an unfair advantage within the capacity market, in light of the way they are treated in the main energy markets. But the department felt there were a number of reasons why it could be expected that diesel would play a smaller role in the future.

Firstly, Defra will consult later this year on options to set binding emission limit values on relevant air pollutants from diesel engines, with a view to having legislation in force by January 2019.

Ofgem embedded benefits review

Secondly, DECC noted that Ofgem was reviewing whether it would be in consumers' interests to change current charging arrangements for distribution-connected (embedded) generators.

Embedded generators can avoid the costs associated with using the transmission system through being distribution level connected. Ofgem believes current charging arrangements may be over-rewarding distribution connected generators, and the proportion of embedded generation is growing.

The regulator's concerns centre on cost reflectiveness, the over-rewarding of embedded benefits to diesel engines and power flows onto the distribution network. Overall, it believes embedded benefits could be distorting investment decisions and has already led to inefficient outcomes in the capacity market.

However, the focus of change will not just be on diesel engines, as any change proposed by Ofgem would be based on changes to overall charging regimes. As a result, the measures imposed to try and slow diesel deployment could impact the wider embedded generation market.

This has already caused alarm from embedded generators. The Association for Decentralised Energy said in response that the reforms needed to protect local energy users. It was concerned by the idea of "twisting the underlying principles" of the network charging regime to achieve policy objectives, and said the removal of embedded benefits risked the closure of a proportion of the more than 3GW of distribution-connected CHP.

Ofgem will set out its conclusions and proposed way forward in the summer, potentially including changes to the charging regime.

Budget stabilises policy landscape for generators

Chancellor George Osborne delivered his Budget on 16 March, setting out a number of important announcements for the energy sector.

Osborne reaffirmed the government's backing for the development of low-carbon technologies. His Budget confirmed that up to £730mn would be allocated, through to the end of the decade, to subsidy auctions as part of the contracts for difference regime (CfD) - the government's new support mechanism for large-scale low-carbon projects.

An array of renewable energy technologies, including onshore wind and solar photovoltaics, received support in the first CfD auction, in early 2015. However, the government has said that the subsidies available over the next five years are intended to support less developed technologies, including the UK's offshore wind industry. It is expecting around 10GW of offshore wind capacity to be developed in the UK by 2020, and believes that this figure could be doubled over the subsequent decade. The first CfD auction will allocate £290mn. Support for offshore wind will initially be capped at £105/MWh, which will fall to £85/MWh by 2026 in order to continue to drive down costs for end consumers.

The Budget confirmed that the current freeze on carbon price support (CPS) rates would be continued, keeping CPS at £18/ton out to 2020. For 2020-21, the CPS will be updated in line with inflation. In the Autumn Statement later this year, the government will lay out its longer-term plans for CPS.

In addition, at least £50mn will be invested over the next five years in new energy technologies, such as storage and demand-side response. A recent report by the government's National Infrastructure Commission suggested that developing these technologies could ultimately save UK consumers around £8bn/ year.

Finally, the government launched the first stage of a competition to bring small nuclear reactors (SMRs) to commercial operation. The first stage is intended to generate a list of SMR developers that could deliver on the government's objectives. The government will also publish an SMR delivery roadmap later in 2016 and will allocate at least £30mn for an SMR-enabling advanced manufacturing research and development programme to develop nuclear skills capacity.

Wholesale prices

Seasonal power prices are 3.0% higher when compared with prices on 15 January 2016, the issue date of the last e-POWER bulletin. Gains have been influenced rising oil and coal prices as well as increasing concerns over power supply margins for the coming winter. However, reductions in other commodities have restricted further growth.

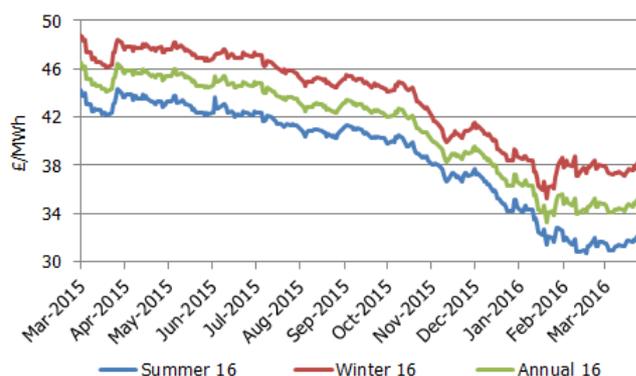
Brent crude oil is now 34.0% higher when compared to 15 January 2016, at \$39.6/bl. The price of oil rose as nations discussed the possibility of a supply freeze. Both OPEC and non-OPEC producers have attempted to negotiate freezing production at January levels. However, prices have once again started to slow as traders lose faith in the effectiveness of the production freeze. Gas markets have followed oil prices higher. Annual April 16 gas is now 1.4% above January levels.

API 2 coal prices are currently 0.5% lower when compared to 15 January, as global demand for coal continues to fall.

Overall, most seasonal power contracts have followed the slight recovery seen in oil and gas prices.

The exception was summer 16 power which fell 0.3% to £32.1/MWh. Winter 16 grew 5.3% to £37.9/MWh. Winter 16 prices have responded to the announced closure of several coal-fired power stations this summer, further tightening supply margins. Winter 17 prices also rose, climbing 2.4% to £35.9/MWh.

Seasonal price trends



CMA proposes changes to transmission charging

In a [document released on 17 March](#), the Competitions and Markets Authority (CMA) set out proposals to reform the energy market, in order to increase competition and help customers obtain a better deal for their energy supplies. As well as introducing a series of measures aimed at improving consumer engagement, the CMA also proposed changes to the contracts for difference (CfD) regime and transmission loss charges.

The CMA has recommended that DECC consults before allocating budgets for future CfD auctions so as to assess the impact of the long-run benefits and the short-run costs of supporting low-carbon generation.

The report also recommends the government makes changes to how transmission loss charges are structured. Under the current regulatory regime, the charges are allocated to both customers and generators, but with no provision made for their geographical location. The CMA recommends that 100% of the costs are allocated to generators, as opposed to the current 45%, and that the charges are priced according to location. Generators located in an area of low demand will therefore face higher charges.

Overall, pushing transmission loss charges onto transmission connected generators would mean suppliers would no longer need to source embedded generation to avoid this charge. Suppliers would then have no incentive to provide transmission loss avoidance as a benefit to embedded generators. **The result could be a loss of value in the region of £0.3/MWh to £0.5/MWh for embedded generators. The CMA will release its full recommendations in June, with proposals expected to be taken forward by Ofgem and DECC.**

Latest e-POWER auctions 141MW of commercial PPAs

The NFPA held its main e-POWER auction on 26-28 January 2016. The auction included 40 commercial projects and accounted for 141MW of capacity. Most technologies were represented, including hydro, wind, solar PV, AD, energy from waste and landfill gas ranging from 50kW to 19.5MW. Independent analysis has been conducted by Cornwall Energy on the auction results.

Average prices achieved by projects were lower when compared to previous auctions. The falls can be attributed to steep declines in wholesale power prices over the last 12 months. With seasonal wholesale prices at their lowest levels since 2007, generators took different decisions on contract lengths in the auction. Decisions were based on a view of future wholesale prices.

Contracts were sold for six months (1 April 2016 to 30 September 2016 and 1 October 2016 to 31 March 2017) 12 months (1 April 2016 to 31 March 2017) and 13 months (1 March 2016 to 31 March 2017). This is a significant change in the e-POWER auction structure, with previous auctions predominantly issuing contracts for the next six-monthly seasonal period (winter 2014-15, summer 2015, winter 2015-16).

Value retention for six-month contracts was 95.0% and value retention for 12-month contracts was 96.9%. In terms of the technology split in the auction, wind and solar PV projects accounted for 42.5% (17 projects) of the commercial sites sold and achieved average value retention of 94.3% and 95.8% respectively. Landfill gas was the second most represented technology in the auction. It achieved an average retention value of 98.2%. This figure, along with high numbers for municipal waste and AD sites, indicates the continued demand for baseload generation sites by some suppliers in the e-POWER auctions. A number of baseload sites achieved over 100% of their theoretical market value. 18 suppliers participated in the auction, consistent with numbers seen in previous seasonal auctions.

Overall, the January 2016 auction exhibited new trends for e-POWER auctions. Sharp reductions in wholesale prices have incentivised generators to choose different contract lengths in the auction, based on their view of future prices. New contract lengths indicate the flexibility demanded by generators, a trend increasing in the market with recent policy and market changes. Average value retention in the January 2016 auction was 96.4%.

[Please click here to read the full report.](#) The next e-POWER auction will be held on 27 April 2016, and already includes 33MW of solar PV sites.



Latest e-ROC auction results

The latest e-ROC auction, held 23 March 2016, saw 10 suppliers place close to 600 bids resulting in the sale of 153,664 ROCs. The average price was £41.93 per ROC, down 26p on last month.

Falls are in line with forecasts of oversupply in the market. Over 5.0mn ROCs have been added to the market in recent months through exceptionally high offshore wind load factors and generation by an additional Drax biomass unit under the RO. The impacts of this oversupply could rollover from CP14 into CP15.

The next e-ROC auction will be held on 27 April 2016.



Other industry news in brief

East Anglia ONE gets go-ahead

Scottish Power has reached a Final Investment Decision on its East Anglia ONE offshore windfarm.

Construction work on the project will begin in January 2017. Up to six onshore underground cables will be installed, each 37km in length. A converter station at Bramford will also be built.

Offshore work is scheduled to start in August 2018. 102 turbines will be installed at the 714MW site, with a total investment of £2.5bn.

The windfarm is expected to be fully operational by 2020.

French government affirms new nuclear backing

The French government confirmed on 18 March that it would provide the financial backing necessary to ensure EDF's planned new nuclear power project at Hinkley Point C

can go ahead.

Hinkley Point C would be the first new nuclear plant to be constructed in the UK for 20 years, but concerns have been raised about the costs of the project.

A Final Investment Decision is expected in May.

RO onshore wind closure behind schedule

The government will be unable to close the Renewables Obligation (RO) to new onshore wind from 31 March, as it had planned, because the *Energy Bill* is yet to complete its passage through Parliament.

The proposed legislation had its Report Stage and Third Reading in the Commons on 14 March; however, the Lords will not consider the amendments made to the Bill by MPs until 12 April.

Speaking at Report Stage in the Commons, energy minister Andrea Leadsom confirmed that the RO provisions would come into force from the date on which the Bill received Royal Assent and would not be backdated.



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