UPDATE PAPER TO ETI COMMITTEE ON ELECTRICITY MARKET REFORM (EMR)

Background

1. On 23 June 2011 the Committee received a briefing paper from the DETI Minister on the proposals for electricity market reform in Great Britain and possible implications for Northern Ireland. This paper set out the policies supporting Electricity Market Reform (EMR) and explained the work underway by the Department to analyse the impact on Northern Ireland.

2. This latest briefing paper is intended to inform the ETI Committee of developments since the Minister's last update and publication of the Coalition Government's White Paper. It also includes the latest position on the proposed Carbon Price Floor.

EMR White Paper

3. The Coalition Government published its White Paper entitled 'Planning our electric future: a White Paper for secure affordable and low-carbon electricity'[1] on 12 July 2011. Although set at a relatively high level, the White Paper confirms:

    - a move to a Feed-In Tariff with Contracts for Difference (FIT CfD) for large scale renewables (i.e. above 5MW) in 2014/15;
    - the closure of the Renewables Obligation for England and Wales to new generation from 1 April 2017;
    - The introduction of an Emissions Performance Standard and a Capacity Mechanism; and
    - A new institutional framework to administer the FIT CfD and Capacity Mechanism.

4. Importantly, the White Paper includes a commitment by the Coalition Government to work with the Devolved Administrations 'to design and deliver relevant elements of the policy package and ensure that reform is consistent with the devolution settlements and takes account of existing market arrangements'.

Feed-In Tariff with Contracts for Difference

5. The White Paper confirms that a Feed-In Tariff with Contracts for Difference (FIT CfD) for low carbon technologies will be introduced in Great Britain in 2014/15. This will be for large scale renewables (i.e. above 5 MW), nuclear and carbon capture and storage (CCS). The FIT CfD will be tailored to accommodate the different characteristics of these technologies. For example, intermittent generation such as wind operates differently to baseload plant such

[1] http://www.decc.gov.uk/en/content/cms/legislation/white_papers/emr_wp_2011/emr_wp_2011.aspx

as a biomass station or nuclear so how the strike price is set for intermittent and baseload generation will differ.

6. A recent study undertaken on behalf of DETI and the Utility Regulator examining the implications and options arising from the EMR proposals, suggests that the type of large scale FIT CfD proposed for the GB energy market could work in Northern Ireland under the Single Electricity Market, albeit with some differences. We are in the process of finalising this study and the Committee will receive a copy in due course.

7. DETI is working with DECC and the Utility Regulator to examine how the costs associated with introducing and administering a FIT CfD in NI could continue to be spread across all UK consumers as currently happens with the NIRO. This work is also looking at how a UK-wide institution to administer the FIT CfD could work within the context of devolution and continue to allow devolved Ministers to exercise authority over issues affecting renewables incentivisation.

8. DECC will be publishing a technical update paper before the end of December which will provide more detail on the preferred solution for the managing institution. A later paper will focus on the FIT CfD. As DETI is currently consulting on a number of EMR-related issues as part of the NIRO consultation, the technical update will not confirm any arrangements pertinent to Northern Ireland. However the Minister would intend to confirm the Northern Ireland position by the end of March 2012.

Closure of the Renewables Obligation in 2017

9. The Renewables Obligation for England and Wales will close to new generation from 1 April 2017. Whilst a final decision has still to be made by the DETI Minister and the Scottish Government in relation to the NIRO and Scottish RO, there is a strong consensus that we will have to follow suit - as, keeping the the NIRO and Scottish RO open to new generation would not be financially viable. The report produced for DETI and NIAUR shares this assessment.

10. You will be aware from the NIRO consultation that DETI is proposing to extend the end date of the NIRO from 2033 to 2037. This will bring us into line with the other two Obligations and also give greater certainty to generators investing up to 2017.

Legislation

11. DECC is preparing an Energy Bill which will introduce the FIT CfD, the institutional arrangements and other EMR-related issues. The timescale is tight, but DECC hopes to have the Bill on the statute book by Spring 2013. As the Committee will be aware, DETI is preparing its own Energy Bill on a range of issues, although the timetable is more likely to be late 2013 for enactment.

12. DECC will be finalising policy advice on the FIT CfD sometime during November. While clauses on the Bill will be at high level, more detailed policy advice is needed to help DECC scope out the role for institutions and how it might operate in Northern Ireland. DECC is willing to widen the scope of the Bill

to include Northern Ireland for the FIT CfD and the institution and there are practical reasons as to why this should be considered; viz -

- It strengthens the rationale for socialisation of costs across all UK consumers
- There is a risk that any delay in introducing the FIT or institution powers in a DETI Bill would increase the risk of NI having to introduce a separate FIT and institution which would be extremely expensive for consumers and potentially complex to administer.

13. Extending the DECC Bill to NI will require the Northern Ireland Assembly's approval for a Legislative Consent Motion (LCM). DETI is therefore using the NIRO consultation to seek views on the introduction of Feed-In Tariff powers (for small and large scale incentivisation) and NI's participation in a UK-wide institution through Westminster legislation. Given the pressing timetable, DETI will commence preparatory work on this to ensure that Northern Ireland does not miss out on the opportunity to be included in this legislation.

Small Scale Feed-In Tariff

14. Northern Ireland did not introduce a small scale Feed-In Tariff (FIT) at the same time as the rest of the UK in 2010 because we did not have sufficient time to introduce the powers by way of a LCM and there was some concern as to the associated cost of a FIT to the consumer. A study undertaken last year on behalf of DETI and NIAUR concluded that Northern Ireland should continue to use the NIRO as the main form of incentivisation as it would help us attain the 40% target by 2020 at least cost to the consumer. The caveat to this recommendation was that the NIRO was the preferred option so long as there was no material change to its operation in the period up to 2020. This recommendation was noted and accepted by the ETI Committee in the findings of its inquiry into barriers to renewable energy production.

15. The EMR proposals mean that the NIRO is now unlikely to be available to new generation beyond 2017 and therefore renewable electricity will need to be incentivised through an alternative mechanism. Whilst this is likely to be in the form of a FIT CfD, this is not appropriate for small scale renewables given its complexity. The NIRO consultation therefore seeks views on the introduction of a small scale FIT in line with that in GB. The primary powers for a small scale FIT will be progressed through the DETI Energy Bill.

16. In the event of the introduction of a small scale FIT, it will be necessary to review the NIROC levels for small scale renewables to ensure both mechanisms are consistent.

Emissions Performance Standard

17. The White Paper proposes the introduction of a UK-wide technology-neutral Emissions Performance Standard (EPS), subject to agreement with the Devolved Administrations. Emissions is a devolved issue and DECC has been advised that Northern Ireland will make its own decision as to if and when an EPS is required, taking into account the different energy market here. An EPS

would require any future coal fired power plants in particular to include carbon capture technologies to meet more stringent emissions standards.

18. There has been correspondence between the DETI and DOE Ministers on this issue, including the possible use of the DETI Energy Bill as a vehicle for introducing an EPS. We are currently awaiting a response from the DOE Minister.

Capacity Mechanism

19. The final decision on the design of a GB Capacity Mechanism will be communicated in the technical update paper; however it has been agreed with DECC that this will not apply to NI as a capacity mechanism is already in place through the SEM. Nevertheless, DETI and NIAUR will keep abreast of developments to ensure no negative impact on NI generators.

Carbon Price Floor

20. The UK's 2011 Budget introduced a UK-wide Carbon Price Floor environmental tax from April 2013 as part of Electricity Market Reforms. The aim is greater security of supply and to help the UK meet its 2050 carbon reduction targets.

21. The tax was designed for the GB market to reduce carbon emissions and replace a significant part of its ageing generation fleet over the next decade with renewables and low carbon generation - for example, nuclear. The tax will make wholesale electricity generated in Northern Ireland more expensive and make it harder to compete with Irish based generators which do not have to pay the tax.

22. DETI and DFP are working with Treasury to resolve the problem of imposing the tax on Northern Ireland when evidence is showing that it will not deliver the same range of benefits as those identified for GB. This will be a long running process over the next year which will need to be considered as part of a larger package of measures under discussion with Treasury, including Corporation Tax.

EMR seminar for stakeholders

23. Energy stakeholders have been invited to a seminar on Wednesday 23 November in the Park Avenue Hotel, Belfast, to update them on EMR developments since our last event in February. A number of DECC officials will be presenting on the various EMR issues and it will allow DETI to communicate progress since the White Paper's publication. The event will be an opportunity for the energy industry to share any concerns it has with the EMR proposals**.** Committee members received an invitation, via the Minister, to attend.

ENERGY DIVISION
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16 January 2012

Dear Alban

ELECTRICITY MARKET REFORM – ANALYSIS OF POLICY OPTIONS FOR DETI AND NIAUR

Over the past number of months, the Committee has received several papers informing Members of the ongoing work to consider the implications for Northern Ireland arising from the Coalition Government's Electricity Market Reform (EMR).

These briefing papers have alluded to a study undertaken on behalf of DETI and the Regulator's Office to analyse the impact of EMR on renewable electricity incentivisation in Northern Ireland. Work started during the EMR consultation stage in the first half of this year when the Department became aware of the proposal to move away from the Renewables Obligation to either a Feed-In Tariff with Contracts for Difference (FIT CfD) or a Premium Feed-In Tariff (essentially, a Fixed ROC mechanism).

The purpose of the study was to assess the implications for the Northern Ireland Renewables Obligation (NIRO) and consider if the alternative incentive mechanisms proposed would work in Northern Ireland as part of the overall Single Electricity Market (SEM). This work was also to look at the impact on consumer costs and the 40% renewable electricity target.

This work has now completed and I am now making its findings public to help inform responses to the EMR-related questions contained in the ongoing consultation on changes to the NIRO.

A final draft of the report could not be finalised until after the authors, Cambridge Economic Policy Associates (CEPA), had been able to take account of the final proposals contained in the EMR White Paper published in July – which confirmed that the preferred solution is a FIT CfD. A draft copy was sent to DECC to allow its analysts an opportunity to consider the findings and challenge any assumptions made. This work has now completed and we are now in a position to release the report.

The report's findings have helped allay many of our concerns that what was being proposed for Great Britain could not work in Northern Ireland. The CEPA study has been particularly beneficial in showing DECC that an outcome that does not include Northern Ireland would put consumers in a less favourable position compared to staying with the NIRO. Throughout this process I have been stressing to Energy Ministers in DECC that any solution for Northern Ireland must not leave our consumers any worse off and I have received assurances that a UK-wide solution will be found.

The main findings from the report are:

- The Feed-In Tariff with Contracts for Difference (FIT CfD) proposed for the GB market could work in Northern Ireland within the context of the SEM.
- A FIT CfD could actually be easier to implement under the SEM that in the GB market, albeit with changes to reflect the different market arrangements.
- A standalone incentive mechanism for Northern Ireland, purely funded by Northern Ireland consumers, would be prohibitively expensive.
- The costs of establishing and administering any replacement to the NIRO should be socialised across all UK consumers (this is currently the arrangement with the NIRO).
- The NIRO should close to new generation in 2017 if both the RO and Renewables Obligation Scotland do likewise.
- The NIRO should be extended to 2037 to support any transition from 2017.
- A separate, less complex FIT should be introduced to support small scale renewable electricity along the lines of that in place in Great Britain.

I understand that my officials will brief the Committee on final EMR-related decisions once the outcome of the current consultation has completed.

Yours sincerely

Arlene Foster

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15th May 2012

Dear Alban

ELECTRICITY MARKET REFORM – NORTHERN IRELAND POSITION

My letter of 6 April 2012 provided the Committee with an update on progress to implement UK-wide aspects of Electricity Market Reform (EMR) in Northern Ireland.

In addition to setting out progress on the proposed transition from the Northern Ireland Renewables Obligation and the introduction of an Emissions Performance Standard, my letter explained that I would be submitting a paper to the Executive regarding implementation of the relevant EMR policies in Northern Ireland and the need to seek a Legislative Consent Motion from the Northern Ireland Assembly. I am pleased to say that I have the necessary approval from the Executive to proceed and have notified the Secretary of State for Energy and Climate Change of my intentions to progress a Legislative Consent Motion which will extend the Contracts for Difference, institutional delivery framework and Emissions Performance Standard to Northern Ireland.

DECC will publish its draft Energy Bill for pre-legislative scrutiny on 22 May 2012 prior to introduction in Parliament in early November. The draft Bill will not contain all elements of the agreed position in relation to Northern Ireland. This is entirely a scheduling issue to allow Parliamentary Counsel further time to scrutinise the issues specific to Northern Ireland's market conditions. I am assured that the clauses will be in place prior to introduction of the Bill in November. Alongside the draft Energy Bill, DECC will also publish an EMR policy overview document. This will include a number of technical annexes which will cover the agreed position with all three Devolved Administrations. It is my intention to make a public announcement on how EMR will be introduced in Northern Ireland to coincide with DECC's publications.

My announcement will confirm the position on the range of EMR issues which I have been keeping the Committee updated on. Specifically, I will confirm that, subject to a Legislative Consent Motion in the Northern Ireland Assembly, DECC's Energy Bill will extend to Northern Ireland for the purposes of:

- The introduction of a Feed in Tariff with Contracts for Difference (FIT CfD) for large scale renewable electricity generation (greater than 5 MW);
- Administration of the FIT CfD on a UK-wide basis to ensure socialisation of costs across all UK consumers, with a role for SONI and SEMO in the provision of data for setting Northern Ireland strike prices;

- A UK-wide Fixed Renewable Obligation Scheme from 2027 to minimise the risk of a hiatus in investment in new renewable generating stations and to maintain confidence in the stability of conditions for investment in renewable energy; and
- The introduction of a UK-wide Emissions Performance Standard for new coal fired power stations to limit the amount of carbon that they can emit.

In addition, the announcement will confirm

- The closure of the Northern Ireland Renewables Obligation to new generation and additional capacity after 31 March 2017;
- Extension of the NIRO to 2037 to ensure that stations accrediting up until 2017 receive the fill 20 years support; and
- My intention to introduce the enabling powers for a small scale Feed-In Tariff in the forthcoming DETI Energy Bill.

As you will be aware, National Grid has been chosen to administer the FIT CfD on a UK-wide basis. We have been considering the options for local administration. However it has become increasingly clear that, in order to protect the position in relation to socialisation of the costs across the UK consumer base (thereby minimising costs for Northern Ireland consumers), while also keeping the FIT CfD as simple as possible for developers, joining a UK system is the best approach to take.

The FIT CfD is only for large scale generation (i.e. above 5 MW) and we would only expect to have approximately 10-15 contracts per year in Northern Ireland. In addition, many of the larger generators will already be operating in Great Britain – so, it is sensible to streamline processes and have a single administration system. The issue of a single administration system was covered in DETI's consultation on changes to the Northern Ireland Renewables Obligation (published 27 October 2011) and there was support for this approach. A UK-wide administration system also has the support of the Utility Regulator.

I mention above socialisation of the costs in the context of protecting the Northern Ireland consumer. But, there is also the risk that any difficulty in socialising costs across all UK consumers would likely mean the model proposed for Northern Ireland would be of less interest to investors, meaning the cost of capital may be higher, as investor confidence in having two separate markets may be lower than that surrounding a single UK wide market. Finally, difficulty in socialising costs may also mean any mechanism for reconciling any discount for Northern Ireland consumers would be more complex. Based on all of this, I have concluded that a UK-wide administration system would serve Northern Ireland best and will protect both consumers and investors better than a stand alone system.

Officials will be attending the Committee meeting on 31 May 2012 and will be able to discuss the current position on EMR and the next steps.

Sincerely,

ARLENE FOSTER MLA
Minister of Enterprise, Trade & Investment