

DECC Call for Evidence on Renewable Energy Trading

EFET Taskforce Renewables Response¹ 11 May 2012

Preliminary remarks

The EU's 2020 agenda underlines the role that green innovation can play in boosting the competitiveness of the EU economy. Over the next ten years, complying with the EU's 20% target for renewable energy will require hundreds of billions of Euros in investments in renewable energy production and transmission. It is essential that this is achieved in an efficient and coordinated way.

An efficient transformation to the green economy will only be achieved if EU companies can plan ahead in a transparent, non-distorted *internal European market*, where choice of location and technology is based on comparative economic advantage. The comparison for this purpose should rest on natural, geographic, climate and hydrological considerations and technological efficiency criteria, not on arbitrary decisions about levels and locations of subsidy.

Cross border trade of renewable energy can contribute to this objective. Allowing individual Member States to meet their national targets through co-operation mechanisms will be beneficial in an EU internal market. It will promote the most cost efficient projects across the EU and consequently the lowest cost for customers. This will also help EU-based companies to develop and deploy cost effective solutions, which can be sold in global markets, thereby enhancing their competitiveness. Trade will enhance the competitiveness of energy consuming companies and increase the acceptance by society of the difficult process of transformation towards a green economy.

¹ EFET is an industry association which was set up in order to improve the conditions of energy trading in Europe, mainly in electricity and gas markets. Established in 1999, EFET represents today over 100 companies in 27 European countries. EFET works to promote and facilitate European energy trading in an open, transparent market unhindered by national borders.

National support schemes not allowing cross border trade for renewables has a number of significant and negative effects on European policy objectives:

- They increase the cost of development of renewables since (a) the deployment of technologies is driven by differing national support levels protected by trade barriers rather than economic efficiency, and (b) the incentives on developers to control costs is eroded by the prospect of guaranteed support levels.
- National renewable targets and support mechanisms have undermined the other policy instruments aimed at reducing greenhouse gas emissions, notably the EU Emissions Trading System (ETS). EU ETS has been weakened to the extent that national governments are further undermining the policy e.g. through the introduction of national CO₂ taxation measures.
- Non-harmonised arrangements for the trading and dispatch of renewables are undermining the objective of the internal electricity market. In particular, priority dispatch of renewables is artificially increasing electricity price volatility, eroding market liquidity, and having a large and negative impact on the ability of TSOs to make available transmission capacity across bidding areas. A technical and a market integration of renewables will only be possible if harmonisation efforts are successful. The goal of achieving the internal electricity market by 2014 necessitates harmonised support schemes.

It is thus, in the view of EFET members, essential that trade in renewables must be developed across the European Union. Unless this is implemented, EFET believes that the 2020 targets will not be achieved. And there will be little prospect of successful expansion of renewable and low carbon technologies post 2020. The objective of completing the internal electricity market will also be put at risk.

There are also some ongoing legal questions about the admissibility of national renewable support schemes that appear to prohibit cross border trade. One interpretation of such schemes is that they amount to a quantitative restriction on freedom of movement of goods, or an equivalent measure, and are hence incompatible with Article 28 of the Treaty. It may be the case in the future that Member States will be obliged by EU law to ensure that cross border trade in renewable energy is possible.

The best way of realising co-ordination across EU Member States is the adoption of compatible support schemes based on tradable instruments (Guarantees of Origin), such as green certificates. The development of such instruments is a clear objective of the Renewables Directive and progress to date has been disappointing. Currently there is only a limited volume of trade in such certificates on a voluntary basis i.e. where individual *companies* are looking to increase the share of renewable energy in their own consumption.

The UK government could do a lot to encourage more cross border trade through **joint support schemes**. This would mean establishing mutual recognition of certificates between Member States with similar schemes (e.g. Sweden, the Netherlands). DECC should reconsider its opposition to joint support schemes if it is really serious about tackling climate change at a European level.

Responses to individual questions

1. Should the UK make use of one or more of these mechanisms, and for what reasons?

Yes.

The use of cooperation mechanisms should be encouraged to reduce the costs of achieving EU and national targets. This will both benefit consumers and also lead to a more robust development of the renewable sector.

This is particularly important for the renewable energy technologies that are close to market maturity like biomass and on-shore wind. If support is still provided to these technologies, the most market oriented support schemes and cross border trade possibilities should apply, making use of competition as a driver for further cost reductions. Better EU cooperation would mean such facilities would be sited in the most optimal locations which would reduce costs.

For technologies that need more time to reach maturity, such as off-shore wind or solar PV, the focus should be research, development and demonstration for limited volumes to cut costs. These technologies will hopefully mature in the future and be able to deliver volumes at reasonable cost in the future. Support for non-mature technologies should be limited to keep costs as low as possible for customers.

A first step for the UK could be to open the border for trade of renewables from other countries. This could be done either by using the joint project mechanism or by agreeing with a country using renewable energy tradable certificates to take a limited quota in their system.

2. What do you consider to be the potential costs, benefits and risks to the UK of making use of each of these mechanisms to import and export renewable energy?

- **Statistical transfers**
- **Joint Projects**
- **Joint Support Schemes**

Statistical transfer as a stand-alone mechanism is hardly an option for fulfilling the 2020 target. It will most likely be difficult to find a country that would like to offer a firm contract ensuring the transfer of statistics in 2020 due to domestic uncertainties to reach national targets. Another problem would be to establish a “price” for such a statistical transfer.

Joint projects are more likely to materialise but they involve a heavy administrative burden. To identify a project, a non-discriminatory process would be needed in the selling country, in addition to contractual processes between three parties etc. Some projects will probably see the light, but the volumes will likely be limited.

Joint support schemes are most likely the most efficient solution. However, the process to implement them will take some time. A first step would be to agree with another country on a system with a limited quota. The government could negotiate to take a limited quota in an existing certificate scheme.

3. What do you consider to be the potential across Europe, for the UK to make use of the statistical transfer mechanism to buy or sell renewable ‘credits’ with other Member States in the next few years and the period approaching 2020?

There seems to be a surplus of renewables in the short term in Europe enabling the possibility to buy statistics for the coming years to meet the interim targets in Annex 1 of the Directive. Securing a firm contract for 2020 will most likely be harder since the rate of increase in penetration required in the later years are much steeper.

4. Do you consider there to be a role for the private sector in implementing the statistical transfer mechanism and, if so, how would that work?

The UK is rather experienced with statistical transfer mechanisms within the country. There are the three renewable obligations schemes covering England & Wales, Scotland and Northern Ireland, and the renewables obligation certificates can be traded freely within the UK. Furthermore the LEC scheme accepts renewable energy under certain conditions to be imported into the UK. Ofgem plays an important role as administer of these systems.

The same logic would apply to implementing a statistical transfer mechanism at a European level. One approach would be to run a competitive tender process for establishing such a framework. No framework for statistical transfer has yet been created by the EU. The UK could be at the forefront of cross-border statistical transfer development in Europe and deliver a working prototype for a later EU system.

5. What do you consider to be the potential costs, benefits and risks to the UK of making use of the statistical transfer mechanism?

The main benefit that might arise is that the UK achieves its renewable target and avoids any potential infringement case. It may also mean lower cost to the consumers if achievement of the renewable targets is based on lower cost projects in other Member States.

The main risk is that the “price” required to effect the transfer reflects the difference in costs. This would mean that the “exporting” Member State would capture this benefit. The

other risk is that the exporting Member State does not, itself, achieve its targets meaning that impact on overall EU renewable penetration is zero.

The generation costs of renewable energy vary strongly across Europe as has been shown e.g. in the EWI study European RES-E Policy and Analysis². Some volumes would be possible to buy but real negotiations would be needed to find out. The UK with its excellent wind sites – on-shore as well as off-shore – could benefit from flexible mechanisms largely as an exporter of energy.

6. Do you consider there to be any financial or non-financial barriers to the UK's use of the statistical transfer mechanism, and how could these be addressed?

The opening for cross border trade would increase the demand for renewables in some countries. There might be problems for some of these regions to transfer the increased electricity production to consumption areas due to grid constraints. The solution is to strengthen the grid, which could mean both the domestic grid and interconnectors. However, Member States with renewable energy potential may argue that a buying country should also pay for grid upgrade costs.

7. How do you think the market for statistical transfers could develop in Europe and how would Member State Governments, the private sector and others work together to put an agreement in place?

At present, a statistical transfer would need to be based on the contract between two Member States. Creating an interface and a suitable application process for interested companies to offer their projects would be helpful to increase the number of suitable projects. Our preference would be to establish a trading platform that would help create a robust price for the value of statistical transfers. However we also reckon that this requires a certain degree of liquidity in order for market participants to have confidence. Therefore, in the short term, a tendering process might be more promising.

8. Do you know of specific Joint Project opportunities which may exist for the:

- **import of renewable energy from another territory;**
- **export of renewable energy generated in the UK to another territory**
- **generation of renewable energy in another territory, where the energy can be consumed in another Member State?**

There are both onshore and offshore wind projects in the Nordic area that are not needed for Nordic countries' target compliance. However, the lack of interconnectors to transport surplus capacity to consumption areas remains an issue unless Joint Projects would involve statistical transfers.

² *European RES-E Policy Analysis, A model-based analysis of RES-E deployment and its impact on the conventional power market* by Institute of Energy Economics at the University of Cologne (EWI), Fürsch, Golling, Nicolosi, Wissen and Lindenberger. Available at : http://www.ewi.uni-koeln.de/fileadmin/user_upload/Publikationen/Studien/Politik_und_Gesellschaft/2010/EWI_2010-04-26_RES-E-Studie_Teil1.pdf

9. What are the costs, benefits and risks of this specific project – we would ask you to provide a high-level summary using Annex A, or if possible, more detailed information using the spreadsheet in Annex B.

This level of detail is not available to EFET at this stage.

10. How do you consider the market for Joint Projects could develop in Europe and how would Member State Governments, the private sector and others work together to put in place the framework to develop such projects?

Joint projects require a suitable institutional framework provided by the EU authorities that make the process accessible to companies and facilitate inter-state agreements. This is a pre-requisite to attract interest from the private sector.

Although only a legal requirement for Joint Projects with third countries, a key success factor for many Joint Projects will likely be the ability to physically export power to one or more member states. Therefore, investments in appropriately sited interconnections will be necessary. Since such investments do not have a short lead time, this is unlikely to materialise on a large scale before 2020. Another key part of the framework will be to decide how generators receive their income stream. There are a number of options for policy makers including:

- allowing a project to allocate a proportion of the total capacity to a Member State's support scheme; and
- making clear statements on willingness to support (pilot) Joint Projects to be developed within a European context, which the EU Commission should provide institutional guidelines for.

11. Do you think there is a role for the European Commission to facilitate and administer renewables Joint Projects?

Not necessarily. Trade between countries would be supported by EU law, even though an approval process has been laid down in the renewables directive.

12. What do you consider to be the financial and non-financial barriers (including any technical issues) which will need to be addressed to enable the Joint Project opportunity to a) import renewable energy and b) export renewable energy to proceed, and how could these be resolved?

Please refer to our answers to questions 6 and 10.