

January 2007

Reform of the Renewables Obligation Response by the UK Business Council for Sustainable Energy

Introduction

This paper outlines the Council's position on the proposed reforms to the Renewables Obligation (RO).

The Council welcomes the Government's intention to increase the volume and diversity of renewable energy in the UK. The preference of the companies involved in the Council would be to deliver this through mechanisms outside the RO.

Key points

- The RO has successfully stimulated interest in renewable energy projects in the UK. The key barriers to delivering the Government's renewable energy targets relate not to this policy but other issues such as delays in planning.
- The Council supports the current structure of the RO, but recognises that if near-market technologies like offshore wind energy and emerging technologies are to be delivered they will require appropriate and different forms of support for their successful development.
- Any mechanism that supports both delivery of the Government's renewable energy targets and investment in off-shore wind and emerging technologies is likely to require additional funds, not just the redistribution of existing revenue support. These objectives are unlikely to be achieved by the current proposals encompassing the principle of net neutrality without adversely impacting overall delivery.
- The most likely scenario is that the redistribution of revenue support towards offshore wind will come from a combination of reduced support for co-firing of biomass and from some reduction in the overall combination of support for onshore wind from the ROC value, the recycle value, the RPI component and the impact of introducing headroom. It is essential that care is taken to limit such movements to a level that is consistent with grandfathering a sensible level of return consistent with the risks; otherwise the delivery of the baseline output from these technologies will be endangered.
- In general, an enhanced level of revenue support for near-market developments should be focussed on a market derived assessment of the development rather than on a technology specific approach. To minimise unnecessary Government

intervention, the Council supports the introduction of a minimum number of support levels based on a clear definition of market readiness rather than introducing a large number of levels based on particular technologies.

- Regardless of any amendments to revenue support mechanisms, emerging technologies will still require additional capital support.
- Although it is sensible to maintain flexibility into the future, it is critical that the Government does not continue to change the framework for investing in renewable energy in the UK in an unpredictable manner.
- A decision about the RO must be made in a timely manner if investor confidence in renewable energy projects in the UK is to be restored.

Success of the RO to date

The RO has successfully stimulated interest in a range of renewable energy projects in the UK from developers and financiers. There is now a solid pipeline of high quality projects at various stages of development that could make a major contribution to delivering the Government's renewable energy commitments.

However, delays in planning approvals for both projects and the associated network infrastructure has led to a lower than expected delivery. This has resulted in an undersupply of Renewable Obligation Certificates (ROCs) in the market and an associated increase in price.

Problems with the supporting delivery systems, such as planning, are key barriers to renewable energy development. Unless these barriers are addressed, there will still be a bottleneck for projects resulting from any alternative policies, including banding.

National Grid has worked hard with the renewables industry and Government to reduce the barriers to grid connections and has established over 150 new connection agreements in the last 18 months. Despite this activity, further improvements in network capacity and availability should be targeted.

Importance of maintaining investor confidence

A clear, stable and long-term policy framework is necessary to establish investor confidence in new energy infrastructure.

Revisiting existing policies can have significant negative impacts on investment. The impact of opening the RO for consultation is already being felt by a number of companies and the investment community.

Amending the RO will have implications that go beyond the renewable energy industry. There is a risk that investor confidence in major energy infrastructure projects in the UK will be damaged if a perception is created that the Government is not delivering a stable policy framework for investment.

Planning constraints

Delays in the planning approval for renewable energy projects have been a significant factor in the undersupply of ROCs in the market.

The Council is of the view that without radical reform in this area, the renewable energy targets will not be met, whatever policy is implemented.

The Council welcomes the Government's intention to reform the planning framework for large infrastructure projects. We are now actively working with the Government to inform this process and ensure that our concerns about the timeliness of the planning process for future renewable energy projects are addressed. This work is being undertaken by the Council in a parallel process.

Emerging technologies

Emerging technologies, such as marine energy projects, require targeted financial support in the demonstration and deployment phase.

It is the view of the Council that the RO was never designed for this purpose of delivering targeted support to emerging technologies and is not the right means of achieving this policy goal.

However alternative funding sources for grant support should be considered including:

- allocating part of the Environmental Transformation Fund to emerging renewable energy technologies; and
- allocating surplus Fossil Fuel Levy funds towards renewable energy technologies.

Off-shore wind energy

One of the objectives of amending the RO is to direct more support towards off-shore wind energy technology.

Consideration should be given to measures which would benefit the economics of off-shore wind farms.

An example of such a measure could be reducing the ancillary costs by socialising grid-costs – similar to the established policy principles in which island connection costs can be capped and Hydro Benefit is applied. This is a possible option that is not supported by all Council members.

Proposed reforms

It remains the Council view that ideally the RO should not be subject to the amount of change that has been seen since its inception, and any future changes need to be timely and appropriate. This would suggest that to support particular technologies,

other appropriate mechanisms need to be developed with the appropriate degree of funding.

If the Government wishes to pursue changes to the RO the following issues need to be addressed:

Impact on existing and planned projects

The Government has provided a strong indication that if the RO is amended, existing projects will be grandfathered to protect them from any negative impacts arising from the new arrangements.

It is important that the point at which a project is eligible for grandfathering is clearly defined in a way that recognises where project proponents have made significant investments under a particular set of assumptions about the policy environment.

There is a spectrum of points where grandfathering could apply ranging from the submission of a planning application to the generation of electricity.

In addition, the combined impact of the proposed amendments such as removing RPI indexation and guaranteed headroom needs to be modelled so that the impact on existing project revenue is understood and consistent with the objectives of grandfathering.

Net neutrality

In its current form, the RO is a market mechanism designed to deliver the most commercially attractive projects first.

The proposed amendments to the RO aim to redistribute the support from the most mature and cost-effective technologies to support newer, developing technologies including offshore wind.

It is the view of the Council that it is highly unlikely that this could be delivered in a way that is net neutral in terms of costs and amount of renewable energy generated. Either the desired volume will be delivered at a higher cost or a lower volume will be delivered for the same cost.

In particular, delivery of offshore wind energy will require additional financial support in order to deliver an equivalent amount of renewable energy in the envisaged accelerated timescales.

The Council supports removing the principle of net neutrality if banding is introduced. This means accepting that investment in a broader range of renewable energy technologies under the RO means that the Government's renewable energy targets are less likely to be met without additional funding.

To increase the amount of support available through RO, the Council does not support the recommendation to remove the RPI link from the buyout price from 2015/16 onwards.

Banding principles

If banding is introduced, the Council supports an approach that is focussed on the stage of development of a technology rather than a technology specific approach. In general, the number of levels of revenue support should be minimised.

This will allow relatively simple and pre-set principles to be introduced which can be used on an ongoing basis to make any necessary adjustments and reduce the need for ongoing unpredictable intervention to amend banding levels in the future.

Establishing the banding levels will require specialist skills and expertise. The Council is keen to work with Government to ensure this issue is addressed.

Future stability and clarity

It is critical that the Government does not continue to change the framework for investing in renewable energy in the UK.

If changes to the detailed operation of the RO are made, they should be made in a timely and transparent manner with very clear boundaries to minimise the negative impact on investor confidence.

Data and assumptions

The Council understands that the consultation on the RO has been informed by a range of modelling and analysis. It is important that the modelling that underpins the proposed amendments to the RO is made available to Council members, who are willing to work with DTI to provide improved information about overall project costs.

Conclusion

Members of the Council have welcomed this opportunity for dialogue, and look forward to an effective outcome that strikes the appropriate balance between clear policy goals, cost to consumers, and market stability.

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The views expressed in this paper cannot be taken to represent the views of all parts of all the companies in the UKBCSE. However, they do reflect a general consensus.