From: Nigel Cornwall [mailto:nigel@cornwallenergy.com]
Sent: 27 August 2008 17:10
To: Hannah Cook
Subject: The green supply guidelines

This is a response to Ofgem's Updated proposals issued on 16 July.

Introduction

On behalf of Cornwall Energy Associates, I convene a monthly meeting for independent suppliers to discuss pertinent developmental issues across the market, be it emerging regulation or legislation, aspects of the business or residential markets or governance modifications. Green tariff guidelines has been a regular topic for debate over the last eighteen months, with some members of the forum more recently also participating in the Ofgem convened working group established to assist in the development of guidelines and the associated verification scheme.

This response captures areas of the updated proposals for green supply guidelines which have tended to give rise to concern for several independent suppliers and the principles on which most of the diverse group agree. Individual responses will be forthcoming from some members of the forum, which will outline particular points of views. The letter is not sent on behalf of the group severally or jointly, but many of the group members agree with many of the points made.

As an independent market commentator I also have a view on many of the policy issues being debated, especially the potential impacts on the supply market and the nascent markets for low carbon power, and this response is submitted in that capacity.

Impact on general supply market

All suppliers seem to support attempts to update green supply guidelines, particularly the need to ensure offers are clear to the consumer, supplier claims are independently verified and tariffs provide a real environmental benefit. While green energy offers have been a small, but growing, feature of the British energy market since it was fully liberalised in the 1990s and the current voluntary guidelines have not led to an industry wide agreement on what constitutes a green tariff. The continued lack of clarity has created a degree of confusion for consumers and it may explain why the number of retail customers on green tariffs has not grown significantly over the last decade and is estimated to account for approximately 1% of the retail market.

The niche green market has proved to be the most viable route for a new entrant supplier to enter and remain in the retail market. A number of smaller suppliers businesses are predicated on the offering of renewable electricity to customers, backed up by their own generation assets or through contracting with renewable generators, or by pledging to invest profits for the development of new renewable assets. These are models which should be emulated, not penalised.

Other low carbon generation sources such as nuclear, CHP and eventually Carbon Capture and Storage all have a role to play in reducing carbon intensity. There is good reason to believe customer pull-through may play a valuable role in these areas, and supply from these sources could prove more economic than some of the green alternatives. It is clearly erroneous to stigmatise anything that does not meet green additionality criteria as business as usual in a market which is seeking to both innovate and reduce carbon intensity.

Impact on industrial and commercial supply market

The business market for green tariffs is larger, although it too is difficult to define in terms of size, and is being largely driven by the desire for companies to fulfil corporate and social responsibilities.

Defra or Ofgem have not presented any analysis to substantiate its position that consumer pull does not result in the deployment of renewables. Until the announcement by Secretary Benn that carbon reporting guidelines would be retrospectively updated, the green market had boomed. There clearly are problems with aspects of current practice with the latest Ofgem data shows a 70% increase in imported Levy Exemption Certificates (Lecs) in a year and half. The award of non-CHP Lecs was equivalent to 22TWh for the year ending November 2007. This is equivalent to more than 10% of the business power market. With Lecs available to non-UK producers, around a third of these Lecs were imported: Norway provides nearly as many of them as Scotland, for example. Lec producers at home and abroad have enjoyed the boom as their earnings have risen, in some case to greater than the certificate's current £4.56/MWh face value. It is hard to construct an argument in support of incremental investment when renewable power is being imported from established assets in other countries, raising more questions of double-counting green benefits.

Despite this it would be wrong to write-off all the arrangements that have developed to date. Further competition should provide signals of the price consumers are willing to pay and hence provide improved investment signals. Recent business market experience has shown some of the country's largest consumers are prepared to pay a premium for renewables, and this progress should not be allowed to dissipate. Indeed removing the ability for a supplier to offer willing customers electricity that is guaranteed to be matched by renewables could introduce undesirable market consequences.

These include:

- traditional suppliers can and do make different contributions through their procurement strategies before additionality is taken into account. A supplier meeting 100% of its Renewables Obligation (RO) is clearly having a different impact on the green generation market compared to one that buys out its obligation in full. In the early RO days many green offerings were premised on a benchmark of purchasing 10% green to show an active contribution to meeting the initial 10% target adopted by government and that has evidently stimulated the renewables market;

- business customers with green contracts will consider breaking from these as the benefits no longer outweigh the costs. This is now a very real risk and it could have a disproportionate effect on niche suppliers whose business is established on existing green supply arrangements as well as on low carbon producers who will not be caught by additionality criteria. Should they be squeezed and other new entry deterred, we will see less green generation coming forward;

- arguments about consumers being misled should not be generalised. Larger business consumers have different motives and more sophisticated buying skills than smaller users. And any serious ‘greenwash’ claims should be addressed through the normal advertising standards channels. As long as information is clear and verifiable, customers should be able to make informed choices.

Although not the same as bringing forward new renewables, some have businesses have stated that green supply marked the initial phase of their plans that also included funding for production and which would represent “additionality.” The implication is that this investment is now under threat. Nor is it clear why the Defra has not considered the use of fuel mix disclosure information when this data is already provided by suppliers (and overseen by the regulator) and at a supplier level prevents any “slicing and dicing” of generation sources to customers.

Given that Defra plans to consult on carbon reporting guidelines this autumn we believe that the guidelines should focus on the domestic and the smallest of businesses until Ofgem is able to explain how the guidelines could work cohesively and comprehensively with Defra’s policies.

Impact on residential supply market

In general household customers who have already chosen green tariffs are satisfied with the offer they have chosen, and therefore with the claims made and the subsequent environmental benefit. This should not be lost during the development of guidelines, which should deliver a clear framework to allow ‘green’ suppliers to continue their business as usual activity and seek accreditation.

Should guidelines be developed which prevents suppliers from offering renewables backed offers consumers will be effectively prevented from choosing their generation source, dampening investment signals. Looking to 2020 policy proposals currently in development could mean that households will be paying a considerable fraction of their energy bill to support the RO, smart meters, and the post-Carbon Emission Reduction Target (CERT). Removing renewables backed offers from the market will prevent domestic customers from offering extra support for the development of new renewable generation at *least* cost. The current proposals have been presented in such a way that consumers could only ‘do their bit’ by signing up to a green tariff which offers an environmental benefit beyond their suppliers’ ‘business as usual’ activity and therefore in all likelihood the more expensive option.

Energy suppliers are best placed to lever support and finance from their customer base to increase renewable generation. Green tariffs based on charging customers a premium which is put towards an environmentally beneficial fund (such as a conservation project) is an activity which could be offered by any number of institutions or retailers. This is not the case for fund based tariffs, which use customers’ premium to fund new build renewables.

Process

Members of the forum have worked closely with the group convened by Ofgem and several have already submitted responses to the November 2007 consultation. There is a desire to develop guidelines but as the current and previous efforts have often run in difficulty a pragmatic solution would be to publish guidelines for the retail market based on the consensus reached earlier in the year. Once the Defra carbon reporting guidelines have been updated guidelines for the business market could be developed. Although a ranking process is desirable, the debates to date have not reached a workable solution. Ideally this should be based on a carbon metric, to complement the overarching policy to move to a low carbon economy. Until this can be achieved guidelines should focus solely on providing customers with clear and transparent information which can be easily verified by an independent third party. An offer which claims to offer additionality should only apply to renewables-backed tariffs, which can be shown to be above the RO target.

The timescales proposed in the consultation appear unrealistic. Ofgem may be able to publish guidelines next month but work to develop the associated scheme cannot progress in any meaningful way until guidelines are finalised. If the guidelines are broadly similar to the proposals outlined in the current consultation document then it is very likely that the system will be necessarily complex therefore increasing the time required to develop the accreditation process and substantially upping set-up costs.

Ofgem and Defra have an open invitation to join the Energy Suppliers Forum to discuss these issues. Please let me know if and when you would like to join us.

I am also happy to provide further comment if that would be helpful.

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