Eggborough Power Ltd

Vanja Munerati
Electricity Transmission Policy
Ofgem
9 Millbank
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Dear Ms Munerati

Impact Assessment on National Grid Proposal CMP 192: Enduring User Commitment

Eggborough Power Limited (EPL) is an independent generator which owns and operates Eggborough Power Station (EPS), a 2,000 MW coal fired power station situated in the Aire Valley in North Yorkshire. EPS was previously owned and operated by British Energy (and latterly EDF) to provide flexible and reliable mid merit support to the “baseload” nuclear portfolio. EPL is now owned by two substantial private shareholders, SVP and Bluebay and is operating as an essentially merchant power plant in the wholesale market.

As a merchant plant, with private ownership, EPL’s biggest concerns with CMP 192 have been the ability of generators to forecast their plant closure dates so far in advanced and the resource implications of increasing liabilities.

Forecasting closure 4 years in advance is impossible given the lack of liquidity in the GB power market. EPL simply has no benchmark energy prices to see if our plant will be economic in future years. At the current time there is no market for us to sell power into more than about 18 months forward. Given the “closure tax” created by the original modification, and the lack of a market in which to hedge risks, this simply signals to plant it is likely to be better to close earlier rather than later.

EPL also believes that there is a good case for treating pre and post commissioning generators differently, which we discuss below. We also note Ofgem’s recent decision to treat pre-2005 embedded generators differently, very much recognising the economics and future operating decisions for older plant is different to that of new plant.

While the proposals do not place credit requirements on plant, they do place liabilities onto plant that must be taken into account in financial planning. At a time when the Government wishes to see investment in plant, particularly as environmental legislation becomes increasingly stringent, it is at best unhelpful to tie up resources in this way. While trying to help parties connect new plant, the increasing financial obligations on existing parties is unnecessary and disproportionate.

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Ofgem's Questions

Question 1: We welcome stakeholders' views on whether we have identified all the relevant impacts of CMP 192.

EPL notes that Ofgem believes that DECC expected the connection and transmission booking process to evolve. While we agree that is the case for the "connect and manage" regime, we have seen nothing to indicate that there was an expectation that the arrangements for existing plant would significantly alter. We understand that Grid would like to know exact closure dates in advance, but there is no indication the generators know closure dates and withhold them, but instead older plant are trying to balance their plant lives against a rapidly changing energy market structure.

As a general principle, economic signals are only of value if they create incentives parties can reasonably respond to in an economically efficient manner. EPL is concerned that the liabilities on post-commissioning generators, going out over 4 years, do not create a signal that they can respond to, but simply adds to closure costs. At a time when the Government is concerned about future plant margins, Ofgem risks creating a signal that it is best to notify closure earlier not later. Such plant could then end up being paid capacity payments to keep it on when without the additional liabilities under CMP 192 it may have done so anyway.

Question 2: Do stakeholders agree with our assessment of the potential environmental impacts of the proposal?

Yes

Question 3: We seek stakeholders' views on the potential implications of the potential perverse incentives, and views as to how they may be mitigated.

EPL understands Ofgem's concerns, but suspect the number of projects where this is a substantive issue will be limited. As we would not face these signals we will leave to those who will to comment on their materiality.

Pre-commissioning Generators

As EPL is not involved in any new build we have left to others who are to comment in detail on this section. However, we would note that the principle of "grandfathering" is important for all investors in the market. While these proposals impact only pre-commissioning plant other policies, such as the RO banding, FIT levels, charges for 2005 embedded gencos, etc., need to adopt grandfathering principles in order to give investors the confidence that the background against which they made their investment decisions will not materially alter.

Where investors have sunk large amounts of money into developments they should be allowed to remain with those arrangements (if they want to) to maintain investor confidence at this crucial time in the development of the GB energy markets. It is for both Ofgem and DECC to ensure that all regulatory changes are proportionate, and as Ofgem asserts that all pre-commissioning plant would be better off, it would be reasonable to suspect any not wishing to alter their arrangements are doing so for very good commercial reasons.

In terms of credit cover, we share concerns over the financial burden of credit with other independent players, many of whom like EPL find the credit arrangements onerous and detrimental to competition.

Post-Commissioning Plant

Questions 8: We seek stakeholders‟ views on the extent to which asset health and the associated plant life assessment could hinder generators in providing four-year user commitment notice.

EPL agrees that Ofgem have correctly identified the impacts of plant health on closure decisions. While nuclear plant may have specific issues, all older plant requires persistent maintenance and investment to keep running reliably. To make those investment decisions, owners need to know there is a demand for their product in future years. All merchant plant can more easily make those decisions if it can forward sell power. It is the lack of liquidity that makes investing for the next two years, let alone four years, extremely challenging.

Question 9: We would be interested to hear stakeholders‟ views on whether we have appropriately identified all the relevant interactions with other policy developments, and potential impacts on user commitment arrangements in general and more specifically, our consideration of CMP 192 proposal.

Ofgem seems to have missed the impacts of wider policies like TransmiT, which may make our TNUoS fees far higher, or the RO banding review, which may reduce our earnings for co-firing. Ofgem has also proposed a review of cash-out which may alter revenue from the balancing mechanism actions we undertake.

Along with the UK policies we are also facing changing environmental policies, for example IED/BAT will require substantial investment, changes to the water abstraction regime may also increase costs. For each plant these issues are different, but they may create bigger risks to plant life than EMR policies and their impacts may be more immediate.

EPL also has concerns about the way the SO needs to develop balancing services in the future. We have raised a change to the Grid Code[1] to allow generators to better control their running regime in order to protect their assets from operating in a way that they are not designed, or maintained, to do. If we cannot get greater control over our operating regime then the health of our plant, along with others, will degrade far faster then we hope. While regulatory risks are significant, the general change in the operation of the market as more intermittent plant connects also needs to be considered.

Questions 10: Do stakeholders consider that a level of uncertainty associated with policies currently being developed in greater detail could hinder generators in providing four-year user commitment notice?

EPL is generally concerned that Ofgem underplays the unprecedented regulatory risks that plant is currently facing. Looking at a business model for plant such as ours, going forward for the next two years, it is likely to have lines of costs and income that are simply unknown, with any one able to push a plant from profitable to loss making. EPL therefore does not

[1] The proposal is to formalise the two shift limit parameter to limit the number of starts a plant does in a day.

believe it is realistic or reasonable to ask these generators to commit to operations in four years time. The Government's decision to go with a market wide capacity mechanism, while still undefined, suggests they are also worried that older plant will shut prematurely.

Network Planning

EPL believes that the TO is in an increasingly difficult position when undertaking network planning, but agree that the analysis over plays the uncertainty surrounding the planning process. The group noted that there has invariably been new plant built on the site of older plant. Staythorpe, Pembroke, Severn, Hinkley, etc. also show that this is likely to go on being true into the future. While significant amounts of wind is due to be added to the system, it is widely acknowledged that conventional plant will still be required to balance the system and maintain secure supplies.

Once a plant has financial close and an EPC in place it will almost certainly complete. Grid will therefore have significant notice of plant being built and which will connect, even if a change of ownership occurs. It seems that the Grid's bigger problem has been the ability, or desire, to undertake pre-emptive investment before plant builds. This back-log of required reinforcement is in fact investment in equipment that existing and much new plant needs. There is too much focus on the very expensive projects (like the boot straps) that accounts for enormous value to the TO, but benefit to far fewer generators. So the value at risk from "generators" is in reality at risk from only a few plants.

By moving to a regime where more of the TOs value at risk is smeared over all players, Ofgem is in fact putting new risks on plants, like EPL, that in themselves create little risk. This seems disproportionate. EPL would like to know if it decided to shut tomorrow which investments the TO would stop, what money it could lose and what assets may become stranded? The TO would like to have firm plans, low risks and underwriting of all its investments, but that then begs the question why should they get not insubstantial (in the current climate) rates of return? It is Grid's job to plan and design the network and they are best place to do this, but they should not expect it to be risk free.

EPL therefore feels that the spreading of new risks to older plant, notably those located in the middle of the network, is simply a mechanism to cross subsidise connection and reinforcements being undertaken for new plant on the edge of the network, notably wind. It will increase our costs and results in liabilities which we do not believe are cost reflective. EPL recognise that supporting different types of generation is Government policy, but support is more efficient if aimed directly at the parties who need support.

Notice Periods

EPL raised its alternative proposal to limit the notice period for post-commissioning generators to two years because it provides a signal most generators can respond to. EPL believes that its alternative better fulfils the relevant objectives, for post commissioning generators, as outlined in our alternative form.

EPL believes that until liquidity in the power market improves there is simply no way for generators to be able to tell if their plant will be profitable more than 2 years out (as far forward as power trades). While the larger integrated players may be able to plan to sell their power internally to their supply businesses, for independent players such as ourselves we believe that the market conditions do not allow us to make commercial decisions further forward than 2 years. At the present time there is simply no robust index to price around so no ability to sell forward. This issue is one Ofgem is explicitly trying to address in its work on liquidity.

There is a good case for recognising that the most likely sites for new build are those sites currently used by older plant. It can therefore be argued that even where plant shuts with only 2 years notice, it may well be that the site, and thus the assets, will be reused within a relatively short timeframe by new plant built on the same site. In the case of the old coal plant, following RWE's conversion of Tilbury, some plant may only be off for a short period while converted to other fuels. Others may be rebuilt as gas or new biomass plants. Under all of these scenarios the chance of stranding assets is very limited.

Taking these two factors into account, along with the lack of any evidence of stranded assets, EPL believes that its alternative represents a more economic solution to the desire to increase notice.

Differential treatment

EPL is aware that Ofgem have previously expressed concerns about the differential treatment on pre and post commissioning generators, though its recent decision on pre-2005 generators DUoS charges may have altered their views.

EPL agree that non-discrimination is an important principle, but there are significant differences in the two types of generator. In the case of a pre commissioning plant there is the possibility that a plant will commission late, so having agreed investment is required will not turn up to use it for some time.

A good example is the original connection dates for new nuclear plants of 2016, EDF then said completion in 2018 and now no energy market models show new build before 2020. On the TEC register Hinkley is still connecting in 2017. While the Working Group showed the slippage in new plant to date, EPL feels that the required levels of investment for extremely larger new nuclear and offshore wind farms is far greater than previously seen. The TOs investments are expected to be significantly greater and thus the risks imposed by these pre-commissioning generators is far greater.

The shifting of dates in this manner must create additional uncertainty for TO's investment programmes, compared to an existing plant giving notice to close which they would then follow through. Changing a connection date may incur a "mod app" fee, but it is unlikely to reflect the potential costs to the TO's of shifting investment on the scale required by a nuclear plant. Where a plant that says it is going to close cannot "mod app" his TEC back, but has to formally request a connection.

Given the current outlook for the market as a whole, EPL would argue that the Government and Ofgem have an incentive to keep older generators running, or at least available to run, for longer in case the new nuclear plants and volumes of wind envisaged by EMR do not appear. Both have legal duties to secure supplies and meet reasonable customer demands, which may only be possible by running older plant longer. If plants are required to give 4 years notice they may shut earlier rather than later and thus jeopardise the security of supply in the medium term.

The new pre commissioning plant has every incentive to commission early, but we do not believe that anyone wants to incentivise early closure at the current time. It seems to us the market outlook justifies treating pre and post commissioning generators differently, in the best interests of the consumers.

If you have any questions or wish to discuss any of the points raised in this letter please do not hesitate to contact me.

Yours sincerely

Paul Carter
Business Planning Risk Manager