

CONSULTATION ON A  
PROPOSAL TO MAKE A  
MARKET INVESTIGATION  
REFERENCE IN RESPECT OF  
THE SUPPLY AND ACQUISITION  
OF ENERGY IN GREAT BRITAIN

*InterGen's response*  
*23 May 2014*

# Consultation on a proposal to make a market investigation reference in respect of the supply and acquisition of energy in Great Britain

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## About InterGen

InterGen is one of the UK's largest independent generators, operating a portfolio of three high efficiency, low emissions producing, flexible gas-fired power stations (totalling 2,490MW; an investment of some £2.1bn in today's money). These stations are located at Rocksavage (Cheshire), Spalding (Lincolnshire) and Coryton (Essex). We have operated in the UK since 1996 and actively sell our power directly to retail companies through long term contracts or in the prompt and forward wholesale power, carbon and gas markets.

InterGen is owned by Ontario Teachers' Pension Plan (one of the world's largest pension fund investors in infrastructure projects), China Huaneng Group (the world's second largest power generator) and Guangdong Yudean Group (the largest energy group in the Guangdong province of China).

InterGen is also ready to build new CCGT projects at two sites, Spalding (Lincolnshire) and Gateway Energy (Essex), having undertaken a highly competitive invitation to tender process in 2013 and selected Siemens as our construction, technology and long term maintenance partner. We have secured a very competitive package and believe this represents a once-in-a generation opportunity to build these projects. The new stations, which are "spade ready", will cost around £1billion to construct including interest over their three year build programmes in today's money. These projects, which are the only two gas-fired projects to appear in the National Infrastructure Plan (ref: Autumn Statement 2013), will:

- create approximately 3,000 direct and indirect jobs during construction and long-term skilled jobs thereafter;
- contribute towards the UK's security of supply;
- provide consumers with low cost generation; and
- help to promote competition in the generation sector which is presently dominated by the Big 6.

Further investment in these new projects will only be made if the gas-fired generation sector is attractive for InterGen and its shareholders – this depends upon the profitable operation of our existing assets, a well-designed and bankable Capacity Market, and a contracted (or equivalent) route to market for the power generated by the stations to ensure bank debt can be raised.

## InterGen's consultation response

InterGen welcomes Ofgem's decision to make a market investigation reference to the Competition and Markets Authority (CMA) in respect of the supply and acquisition of energy in Great Britain. We would make the following points in respect of the scope of the proposed investigation:

### *1. A full and complete review of the supply and generation of electricity is necessary*

We would urge Ofgem to expand the terms of reference to give the CMA a clear and unambiguous mandate to investigate thoroughly competition in the GB generation sector as well as the supply sector. In particular, the terms of reference should allow the CMA to examine carefully barriers to entry and exit for independent generators in the wholesale market. Allowing independent generators to compete on a level playing field with vertically integrated utilities is critical both in terms of promoting effective competition in the sector and ensuring independent parties play a more prominent role in investment in new UK generation infrastructure.

### *2. Particular attention should be given to the vertically integrated nature of the energy market*

The vertically integrated utilities control over 95% of the retail market in GB as well around 74% of the GB generation capacity. With the principal purchasers of electricity having access to their own generation assets, independent generators have found it increasingly difficult to access forward market products which allow these market participants to exercise an appropriate hedging strategy thereby reducing their cost of capital and competing fairly with the Big 6. Reforms aimed at improving liquidity in the wholesale market have recently been introduced but it is too early to determine how effective these will be at providing a robust wholesale reference price along the forward curve.

### *3. The structure of the proposed capacity market may inhibit new entry by independent CCGT developers and should be analysed carefully*

The Government has stated that the CMA should play, "a key role in challenging government where Government is creating barriers to competition"<sup>1</sup>. We would urge the CMA to consider not only the existing energy market in Great Britain but also to consider whether Energy Market Reform under the Energy Bill 2014 facilitates effective competition in the best interests of consumers. We note in this respect that the Government declined a proposed amendment to the Energy Bill that would have required the 'promotion of competition' as a key objective of this legislation.

Independent developers currently own approximately 40% of consented CCGT development projects in the UK. An independent thermal power project needs a bankable route to market for its power sale revenues in order to enter construction. As DECC has acknowledged, revenues from the capacity market alone are unlikely to be sufficient and therefore access to 'bankable' (i.e. contracted) energy market revenues will also be necessary. Independent equity will only invest and banks will only lend if power sale revenues are contracted long term with a creditworthy counterparty.

In our view, the proposed structure of the Capacity Market is anti-competitive as it favours the vertically integrated business model as it enables such companies to bid at a lower capacity price than an independent developer into the Capacity Market auction even if the cost of constructing and operating the vertically integrated company's project is higher. This is illustrated in the table below which we have provided to DECC previously.

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<sup>1</sup> Strategic Steer for the CMA 2014-2017

£/kW	Big 6	Independent
Price needed to make CCGT economic (e.g. independent secures a lower cost construction and maintenance contract than a Big 6 company)	125 (A)	100
Auction price bid	75 (B)	75
Market revenue needed	50 (A – B)	25
Best for consumers	X (as higher cost project)	✓
Route to market for “market revenue”	Pass to retail arm – stable	None – no PPA/toll appetite
Reach construction	✓ (if balance sheet)	X

We are aware of only around 4GW of thermal capacity which is currently contracted under long term PPA / tolling agreements with independent generators.

This access to market issue has been recognised by the Government. For example, it has included a mechanism in the Energy Act which allows it to mandate a power purchase scheme, requiring licensed suppliers to contract with renewable generators, with costs shared amongst suppliers. In this respect, it has responded to the concerns of independent renewable generators to provide a backstop route to market that is bankable. We would urge the CMA to consider whether a similar mechanism is necessary to support investment by independent thermal generators.