ECOHZ Origin Matters

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Consultation on market coupling and Levy Exemption Certificates and call for evidence on wider impacts

I refer to your consultation published on March 24th 2015. This letter gives the views of ECOHZ. ECOHZ is a Norwegian company focusing on trading green values related to electricity from renewable sources. Our head office is in Oslo, Norway.

The main business of ECOHZ is related to administrative services and trading of Renewable Energy Guarantees of Origin (REGOs) from power plants in the Nordic countries and some Southern European countries. Last year we delivered our services to electricity producers owning about 250 power plants and electricity suppliers selling green products in 15 different countries. Our traded REGO-volume reached 40 TWh in 2014. We are also involved in the Swedish-Norwegian Renewable Obligation Certificate System and trade such support certificates in the Norwegian and Swedish markets. Some years ago we were involved in support schemes in the Netherlands and Belgium based on documentation by electronic REGOs.

So far we have chosen not to trade UK Levy Exception Certificates, even if many of the power plants in our portfolio probably will qualify for the scheme. Some years ago we carried out LECs-considerations and discussed various aspects of the system with Ofgem, HMRC and National Grid. Our conclusion was that business risks were difficult to quantify so we decided not to get involved directly. Our main concern was related to the ability to document electricity consumption in the UK in a 100 % reliable way when power plants are located outside UK. We assist several producers involved in LECs-trading to cancel REGOs from their production in their national registries to notify local authorities that the electricity is exported to the UK and should be withdrawn from the residual-/grid-mix calculated in the production country.

Based on our experience we feel we have the necessary competence to answer the questions in your Consultation on market coupling and Levy Exemption Certificates and call for evidence on wider impacts. Our answers and comments follow below.

Question 1: Where renewable electricity is traded implicitly across coupled markets, is it possible to evidence the electricity is consumed (or to be consumed) in the UK? Please explain your answer.

It is no problem to document consumption of electricity in the UK or elsewhere in the world. This is simply done by the meters measuring the off-take from the grid. If meters are in the UK the metered electricity is consumed in the UK.

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The challenge is to document which power plant (inside or outside the UK) that is producing and delivering to the grid electricity to balance the consumption. You need a connection outside the national grid directly from the power plant to the consumer to track electricity physically in a way that is 100 % correct. This solution is not possible in reality.

Tracking challenges will be even greater if there are several balancing areas involved that are connected by interconnectors. The problem will be the same whether the various balancing areas are inside or outside the UK, but with foreign balancing areas involved it is difficult to decide if consumption is balanced by national or foreign production.

Since this memo is discussing the situation of foreign power plants claiming LECs I will only comment on the situation where the power plants are located in Continental Europe and the balancing areas are connected by the interconnectors from France and the Netherlands.

When the various balancing areas/markets are coupled into a single market it is no more possible to trade explicit physical day-ahead-capacity between France/the Netherlands and UK. The situation for the whole NWE-market is very similar to the situation inside the UK where transmission capacity is handled and optimized by TSOs and power exchanges.

We have had discussions with National Grid/IFA and due to the market coupling the Day-Ahead (DA) capacity allocations have ceased to be conducted via explicit auctions. Long-term capacity products i.e. any period ahead of the DA continue to be allocated through auctioned PTRs with the option to either physically nominate or release via a Use-It-Or-Sell-It rule into the DA implicit auction. The UIOSI-rule combined with a directional netting rule ensures that physical flows are maximized in the correct price direction. Since the interconnector operators will optimize the physical flow through a combination of physical PTR nominations, directional netting rules and the Price Coupling algorithm within the overall NWE Price Coupling solution, there is no guarantee any more that interconnector-flows will follow from nominated PTRs.

The physical interconnector flows will instead be a result of PTR nominations, directional netting and all external nominations in the single market handled through the NEW Price Coupling algorithm. In principle a nomination for physical delivery anywhere in the single market on the continental side of the interconnectors combined with nominations of physical off-take anywhere in the single market on the UK side of the interconnectors will influence physical interconnector flows the same way as nominated PTRs from France/the Netherlands to the UK.

PTRs bought at auctions and nominated to interconnector operators will still result in physical deliveries at agreed ends of the interconnectors and therefore hedge the cost/price risks linked to any interconnector congestions.

Physical electricity nominated through PTRs for delivery to the interconnectors at one end could be delivered back to the market at the same end and electricity nominated for off-take from the interconnectors at the other end could be procured in the market at the same end to optimize flow and price coupling. PTRs nominated for physical transmission give no guarantee that English electricity is delivered in France/the Netherlands or vice versa even if PTRs are nominated for physical transfer.

Since the physical flows now will are handled much the same way as in the Single Electricity Market (SEM) operating in the Republic of Ireland and Northern Ireland and in the other coupled electricity markets in North-West Europe, I recommend you to accept documentation of electricity consumption in the UK the same way NIAUR accepts for the Single Electricity Market (SEM) and that Ofgem already accepts for interconnections between other coupled NWE-market segments.

We therefore recommend that you establish the following routine:

- Production of electricity and deliveries to the grid in areas being part of the Single NWE-market is documented by issuance of Guarantees of Origin according to EU Renewable Directive (Directive 2009/28/EC) and national legislation in the production countries.

- Consumption of electricity in the UK is documented by cancellation of REGOs in the exporting country. An even better solution will be that Ofgem base their REGO-routine on the international EECS-standard and connect the UK REGO-registry to the EECS-hub making it possible to import foreign REGOs and cancel them in the UK.
- Cancellation is carried out within dead-lines in exporting country and in the UK securing that the relevant electricity is deducted from the residual-mix of the exporting country and included in supplier-specific or residual-mix in the UK.
- Physical deliveries to end-consumers in the UK will be documented by UK electricity suppliers as a physical flow from the grid to the end-consumer. Volume of cancelled foreign REGOs should be equivalent to the metered deliveries to the end-consumers.

The solution I propose for sales of foreign Renewable LECs to UK suppliers should be in line with the requirements in chapter 4.8 in the NIAUR guidance for handling imported LECs:

> *4.8 Generating stations participating in the Single Electricity Market (SEM) must have a relevant arrangement with a supplier in Northern Ireland (NI) in order to claim LECs. A relevant arrangement is a contract stating that a supplier will take out of the SEM pool an equivalent amount of generation that the operator produces.*

If Ofgem accept s documentation based on Guarantees of Origin as described above, such a change of the documentation routine will improve the effectiveness of the international LECs market considerably. Improved effectiveness is in my opinion an important step to give consumers a better possibility to stimulate renewable energy by choosing electricity from renewable sources. Today the major share of the support intended to stimulate renewable energy consumption ends up with a small number of electricity companies active in PTR auctions. As long as the markets are coupled these payments do not any more give access to physical flows and are only used to produce paper required by the current Ofgem documentation routine. This cannot be the intention of the possibility to import Renewable LECs.

Establishing a routine making Guarantees of Origin the main instrument for documentation of foreign electricity to be consumed in the UK could also contribute to lower costs in the accreditation and auditing routines. If you accept foreign Guarantees that are issued according to EU Renewables Directive and national law, then you can use the information in the Guarantees also in the accreditation and auditing processes. The Guarantees give most of the information you need for the accreditation. Your work and controls can therefore focus on each countries routine and not on every single power plant.

Question 2: What evidence might generators use to demonstrate that an overseas LEC represents electricity that is consumed or is to be consumed in the UK when that electricity has been traded implicitly across coupled markets?

Generators should use Guarantees of Origin issued according to EU Renewables Directive as evidence of production and delivery to the interconnected NWE grid. UK suppliers should use cancellation of Guarantees of Origin for UK consumption as documentation of origin of the electricity they deliver to end consumers and claim Levy Exception for, See more comments under question 1 above.

Question 3: Are stakeholders aware of any reasons for limiting the issue of overseas LECs to electricity that has been or is to be explicitly traded? Please explain your answer.

I see two reasons for limiting LECs.

1: CCL income will be reduced and thereby the ability to finance public sector.
2: Electricity will be cheaper and therefore consumption of electricity can increase. As long as the cheaper electricity will be from renewable energy sources, the environmental problem will not increase, but the renewable electricity could alternatively replace fossil energy and therefore an increase in consumption is not favoured..

Question 4: Are stakeholders aware of alternative ways of demonstrating proof of GB supply of overseas electricity that do not involve LECs, and, if so, what are they?

LECs is a scheme to stimulate consumption of renewable electricity. It is not a documentation of origin in line with EU Renewables Directive. If UK politicians should change or abandon the LECs scheme, it would become a problem to document the origin if LECs also are used for such purpose. A better solution for proof of foreign origin and information about the relevant power plant is to use Guarantees of Origin issued according to EU Renewables Directive and handled in a reliable way including exclusion from residual-mix in country of production and cancellation for consumption in the UK.

Question 5: Do stakeholders currently acquire LECs purely for non-CCL purposes?

I do not know, but as long as LECs also have some value related to other schemes than CCL I guess there are some import to combine CCL exemption with FIT and/or fuel-mix declaration.

Question 6: What do stakeholders foresee as potential impacts if:
6.1 Overseas renewable electricity can be demonstrated as consumed (or to be consumed) in the UK where it has been implicitly traded, and LECs are issued for this accordingly?

I anticipate that the whole-sale prices of LECs in the UK market will fall. Today the interconnector capacities (3000 MW) are too low to handle imports from all accredited power plants outside the UK (13000 MW). Therefore there is a huge difference of LECs values in the UK and in continental Europe. If documentation by PTRs is replaced by documentation by REGOs, the limited interconnector capacity will not be a problem anymore. The total LECs supply can become larger than demand giving a much higher competition for end-consumers and probably the levy exemption will end up at as reduced electricity prices to end-consumer buying LECs documented electricity. Today there are less LECs in the UK market than the demand and most of the value ends up with UK suppliers and intermediaries involved in the import documentation work.

6.2 Overseas renewable electricity was only accepted as consumed (or to be consumed) in the UK (and LECs issued accordingly) where there is explicit booking and nomination of interconnector capacity?
It would be helpful to have responses to this question cover what the impacts would be on: The electricity markets (volume, price, distributional issues) CCL and UK Renewable Electricity schemes, including FMD, FIT, CFD, and SLC 21D

As I mentioned in my answer to question 1 the market coupling has stopped the possible to acquire explicit physical capacity in the interconnectors. Booking of PTRs and nomination of physical flows related to the PTRs offered by National Grid does not represent any guarantee for any physical flow into the UK. A requirement of buying PTRs to document physical flow is therefore a solution to support the document industry (people producing papers and reports) and does not give any extra influence on the market other than an extra cost of handling the various Renewable Electricity schemes.

Fuel-Mix disclosure should be based on Renewable Electricity Guarantees of Origin and the most effective solution would be to include the UK REGO-scheme in the international EECS-standard and linking the UK registry to the EECS-hub.

I expect that most of CCL electricity will end up with LECs over some time. Therefore the most cost effective solution for other schemes where costs are allocated to electricity sales except LECs-documented sales will simply be to allocate such costs to electricity without the CCL obligation only. Then all extra costs related to handle LECs in relation to the schemes cost allocation will be avoided.

There is a risk involved to use LECs for other schemes than LEC. Politicians can change CCL and LECs on short notice. It will be much better to make REGOs the main instrument since this is regulated by international and national law and can be expected to last for a much longer period than LECs.

We believe that consultation is at the heart of good policy development. We are keen to consider any comments or complaints about how this consultation has been conducted. We are keen to get your views on the following:

1. **Do you have any comments about the overall process, which was adopted for this consultation?**
2. **Do you have any comments about the overall tone and content of the report?**
3. **Was the report easy to read and understand, could it have been better written?**
4. **Please add any further comments?**

It has been a good process and the report was easy to read. I really hope that the responses you receive will contribute to improve the LECs scheme and the routines for using the LECS in other schemes as well.

If you do have any questions or want me to explain some of my answers in more detail, please do not hesitate to contact me.

Regards

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