

Important changes to the UK's electricity market



Save today. Save tomorrow.



The UK Government is in the process of designing and introducing a package of reforms which will restructure the way our electricity market operates.

This follows a period of thorough consultation with stakeholders and builds on a shared understanding that existing market arrangements will not meet our future energy needs.

This paper sets out the steps we and Government are taking to keep electricity supplies secure and affordable for our customers.

What is happening to the UK electricity market?



The Government has proposed a package of reforms that will restructure the way our electricity market operates.

Taken together, the Government's package of reforms will provide a coherent investment framework which will allow the delivery of major new generation projects in the UK.

It is this investment in a range of low carbon generation technology that will play a pivotal role in keeping future electricity supplies secure, affordable and low carbon – powering long term economic recovery.



Why change is necessary

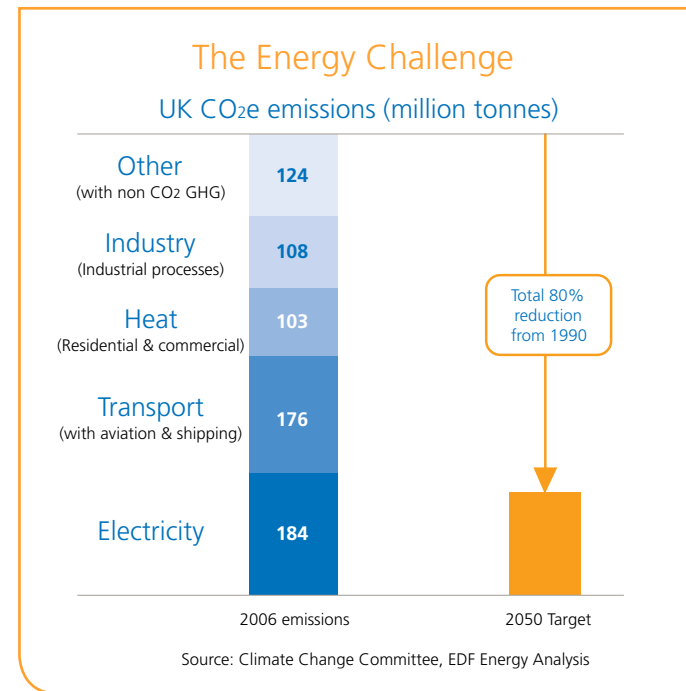
Replacing ageing, carbon emitting generation

The UK currently faces a major challenge, seeking to deliver on its agreed and legally binding carbon reduction goals (reducing our carbon emissions by 80%, by 2050), and addressing the scheduled closure of around 40% of current electricity generation capacity by 2025.

That challenge is compounded further by the planned decarbonisation of the UK's heat and transportation sectors, which will contribute to the expected doubling of electricity demand by 2050.

To meet the challenges of maintaining security of supply, whilst delivering affordable, low carbon energy, an unprecedented multi billion pound investment in capital intensive generation technologies such as wind, nuclear and Carbon Capture and Storage (CCS) is required. Ofgem has estimated that £200 billion of investment in energy infrastructure is needed in the next few years.

Conditions in the UK mean that this country needs to move faster than many other European countries to urgently renew its energy infrastructure. Delay in investment could expose UK energy users to the risk of disruptions in supply and the likelihood of more volatile and higher energy prices.



Reforming market arrangements

Existing market arrangements were established to support an energy market which enjoyed over capacity in generation, and ample North Sea oil and gas reserves, with no decarbonisation imperative. These arrangements encouraged greater efficiency in the electricity industry to drive down costs for consumers. However they also unintentionally created uncertainty over future market conditions, making long-term investments risky and expensive.

Now, whilst some views vary about the precise nature of the desired reforms, a broad range of stakeholders are united in acknowledging changes to the existing market arrangements are urgently required to deliver investment.

Stakeholders ranging from the Committee for Climate Change (CCC), the Confederation for British Industry (CBI), Renewables UK (RUK) and the Carbon Capture and Storage Association (CCSA) have all called for reforms to the UK's electricity market arrangements – reflecting the broad consensus for change that exists.

“Conditions in the UK mean that this country needs to move faster than many other European countries to urgently renew its energy infrastructure.”



How will it work?

The Government is making progress on introducing a coherent package of reforms, the first component of which, a Carbon Price Floor, was set out in the 2011 Budget. A Government White Paper is also expected shortly, and will identify further, complementary reforms of current electricity market arrangements.

Taken together, these reforms will work to significantly reduce the risk premium for investors, and therefore the capital cost of new investment, so ultimately working to reduce the cost of energy for users. The core components of the Government's reform package are set out in this chapter.

“Pricing carbon is not new policy – it builds on the existing European trading scheme for carbon.”

A floor price for carbon

The current Finance Bill which widens the scope of the existing Climate Change Levy (CCL), to include fossil fuels used for electricity generation, will set in place broad powers to establish a steady price path for carbon.

A predictable price for carbon is essential for investor confidence, providing the certainty required to deliver multibillion investments in new low carbon generation that will help to keep energy supplies secure and affordable.

Pricing carbon is not new policy – it builds on the existing European trading scheme for carbon, established under the EU Emissions Trading Scheme (EU ETS), and ensures carbon prices remain aligned to those anticipated by that scheme.

Level and rate

The Government has already signalled that the carbon price floor will be set at £16 per tonne from April 2013, reaching £30 per tonne of CO₂ in 2020 (at 2009 prices). The floor will only be triggered in the event that the EU ETS price is low – if the EU ETS works as was originally intended (the carbon price has been as high as €27/tCO₂ in 2008) then the Carbon Price Support will have very little additional impact on UK energy users.

The price path set out by the Government will strike the right balance for industry and consumers, through allowing for the gradual strengthening of the carbon price signal without distorting the market. It will provide security of supply at an important, transitional time, while aligning the UK with broader, international action to limit any increase in global temperature to 2°C.

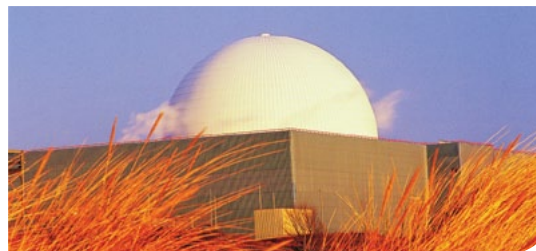
How will it work?

“The Government’s own analysis... expects bills to be around 4% lower in the longer term...”

Maintaining UK competitiveness and delivering stable bills

The new investment in low carbon generation that will be brought forward by a clear carbon price, will help to reduce exposure to fossil fuel prices, so reducing price volatility and maintaining energy security for users.

The Government’s own analysis has estimated that while its price path for carbon may increase bills by around 2-3% in the short run (when compared to what they would otherwise have been), it expects bills to be around 4% lower in the longer term for both business and domestic energy users.



In fact, under many projected scenarios looking at the price of carbon, the introduction of a floor is expected to have limited impact. For example, even if the EU ETS price was as low as £20/tCO₂ in 2020, and the UK floor remained £30/tCO₂, the additional cost to energy users would be in the region of £5/MWh. That would mean UK prices would still remain below current price levels in some other European countries such as Italy and the Czech Republic.

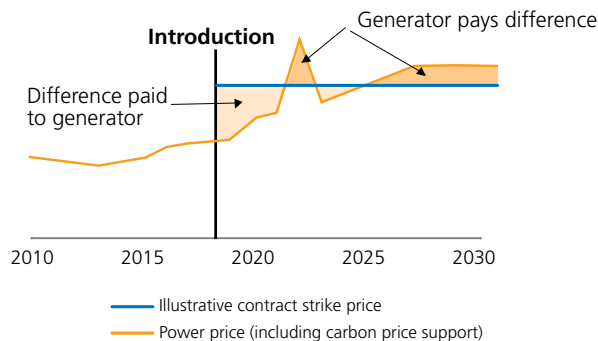
With a strong investment in new nuclear, as is proposed by EDF Energy and many of the other main electricity suppliers, the UK can also expect stronger price stability, as is seen today in countries such as France.

To support businesses now, the Government has already set out plans to increase the Climate Change Agreement discount from 65% to 80% – a move which has been welcomed by the CBI as an important way of helping to keep bills affordable for businesses.

In addition, further moves to reduce corporation tax and withdraw the proposed Carbon Capture and Storage (CCS) levy, will help contain the cost base for UK businesses. The decision not to introduce the CCS levy alone is expected to avoid a 2% increase in electricity bills from 2015.

Feed in Tariffs

Illustrative impact of CPF + CfD on revenues for low carbon generators (£/MWh) – starting 2018



Other related market reforms, which will form the basis of the Government’s forthcoming White Paper, propose complementary policies geared to delivering further price certainty for both investors and energy users, while maintaining security of supply.

Long-term contracts for low carbon generation

The Government has also proposed the introduction of long-term contractual arrangements for new investment in low carbon generation. Where a carbon price floor will address the need to put a value on carbon, these contracts will place a value on security. Both will work to mitigate risks for customers and investors.

The Government’s preferred approach is through Contracts for Difference (CfDs). These will operate as a financial instrument to provide investors with a fixed price for a plant’s output (the strike price) that would be compared with a measure of the wholesale market price (the reference price).

This mechanism would work to not only protect investors against the risk of low wholesale prices, but it would also protect customers against high wholesale prices. If for instance, fossil fuel prices are high, generators will pay back any excess over the settled strike price – keeping prices stable for customers, whilst providing certainty for investors in major new generation projects.

How will it work?

Putting a value on available capacity

Growing levels of intermittent generation in the form of wind generation are expected to connect to our grid over the coming years. Such intermittent generation will require sufficient levels of reliable generation capacity to meet demand when the wind does not blow – maintaining security of supply.

Because of this, the Government is considering the introduction of capacity payments as a part of its reform package. These will reward reliable generation plant to ensure that sufficient capacity is available to meet fluctuating demand and to safeguard security of supply.



“Growing levels of intermittent generation in the form of wind generation are expected to connect to our grid over the coming years.”



Opportunities for your business

To be fit for the future, the changing priorities of the UK energy market need also to be reflected in the energy strategies and tactics employed by businesses.

In today's tough economic climate, businesses face a range of pressures, including: reporting on carbon emissions, meeting higher customer expectations to reduce carbon emissions, managing tighter energy supply contract terms and conditions, and rising energy costs. Sourcing low carbon energy and improving energy efficiency are then clear and increasing priorities.

That is why, with the right long term policy framework in place, EDF Energy is investing in new low carbon generation now, whilst also developing the solutions and tools to allow our customers to better manage their energy use.

“Sourcing low carbon energy and improving energy efficiency are then clear and increasing priorities.”

Our investment will create business opportunities across the supply chain for any company involved in low carbon energy. This investment may also present direct commercial opportunities for you, whilst also benefiting businesses who specifically manage their own, or help others manage their energy consumption.



EDF Energy's role

Delivering energy savings

Our work with our business customers is increasingly focused on integrating supply and energy savings.

We recently finalised an agreement with one of our major retail customers, which includes a yearly £1 million energy saving guarantee. The agreement comprises an innovative bundled contract, which brings together energy procurement and energy services expertise.

Our energy services team is working now with this business' Property and Development Department with an aim of saving at least £3.5m during 2011, through new energy saving initiatives, with the first £1m guaranteed by EDF Energy.

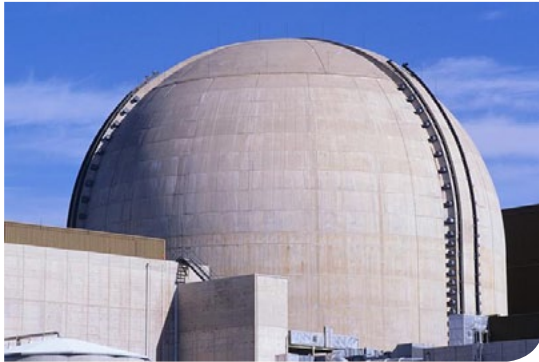
We believe that many businesses have the potential to save significant amounts of energy through engaging their employees and either optimising or upgrading equipment. We're helping deliver verifiable energy savings with inventive engineering based programmes.

Find out more at:
edfenergy.com/saving-energy



“We're helping deliver verifiable energy savings with inventive engineering based programmes.”

Delivering new low carbon generation



We are also playing our part through preparing to deliver major plans to invest in new low carbon generation.

We plan with our co-investor Centrica, to invest £20 billion in four new nuclear power stations in the UK. Our aim remains to be the first to deliver new nuclear generation, at an important, transitional time in our sector.

In addition, we are already investing significantly in our existing nuclear fleet to maintain performance, and extend plant lives. We currently spend £300 million per annum on our existing fleet and will spend around a further £50 million per reactor extending the life of our existing nuclear plant.

It is this investment, guided by a robust carbon price and policy framework, which is helping to maintain security of supply for our customers now.



Please keep in touch...

We would be very happy to talk to you about the issues set out in this briefing note, and how we can work with you to better improve your energy use.



Please feel free to contact:
letstalkpower@edfenergy.com



e-brochures – a better way of working

Why e-brochures? At EDF Energy we are committed to using the most sustainable working practices wherever possible and this includes when delivering communications to our customers. E-brochures significantly reduce the volume of printed material we need, reducing our carbon footprint and contributing towards our 2012 Climate Commitment pledges.

Our customers appreciate e-brochures because they offer timely delivery of easy to access information in an ideal format for the modern screen based working environment.

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These notes are intended as a guide. For further information, participants should refer to the Environment Agency website

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