

Electricity Market Reform

Making sure your business is ready

Electricity Market Reform is here

The UK's energy policy is no longer in debate: it's now reality.

On 1 August 2014, the Capacity Market and Contracts for Difference became law.

They join the two other EMR policies introduced in 2014: the Carbon Price Floor and the Emissions Performance Standard.

The new elements will have a more direct impact on your business. So it's time to focus on understanding the ins and outs of these new policies, to work out the best way for your business to respond.

Make sure your business is ready

- This e-factsheet is designed to bring you up to speed on the why, what and how of the Capacity Market and Contracts for Difference.
- You'll get an overview of the impact these two schemes are likely to have on your business.
- And you can use it to help explain EMR to other people who need to know.
- Part of it would even look good as a poster on your office wall (just print out pages 3-6 single-sided).
- On pages 7 and 8 you'll find a handy timeline and a rough guide on how to budget – these are based on information we know today, but may change as the government confirms more details.
- For more specific information about how EMR will affect your business, please get in touch with your relationship manager. They'll do everything they can to help make sure you're ready for EMR.



RISING TO THE CHALLENGES OF AN ELECTRICITY INFRASTRUCTURE FIT FOR 2050

SECURITY | AFFORDABILITY | LOW CARBON

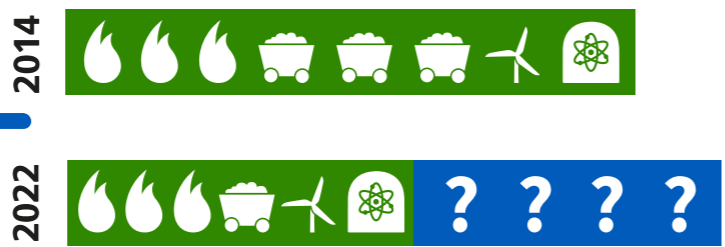
ELECTRICITY MARKET REFORM



CAN THE UK GENERATE ENOUGH ELECTRICITY FOR EVERYONE?

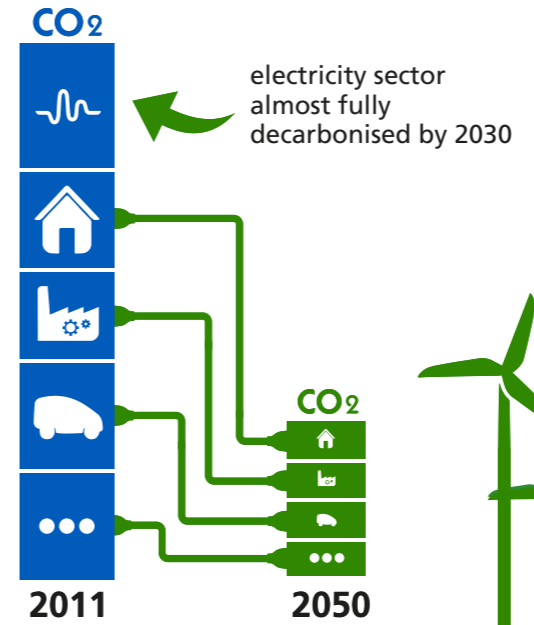
1 DIMINISHING CAPACITY

Demand for electricity is increasing but nearly half of the UK's generating capacity is due to retire within 15 years. And much of the new-build low carbon generation is intermittent. Take wind farms: the amount of electricity they generate depends on when and how much the wind blows. If the UK just stood by and did nothing, there may not be enough capacity to provide electricity for everyone when the network's under pressure.



CAN THE UK MEET ITS TARGETS FOR REDUCTION IN CARBON EMISSIONS?

1 AMBITIOUS TARGETS



The UK has legally binding targets to reduce its emission levels in 2050 to just 20% of what they were in 1990. Which means almost fully decarbonising the electricity sector by 2030. But the UK is not currently building enough new low carbon electricity infrastructure to meet these targets.

The story continues on the next page

Capacity

2 **PEAK PRICE VOLATILITY**

£/MWh

scarce supply causes high prices at peak demand

Energy only wholesale power market

What's more, at those times when there's not enough electricity to go round, prices could spike. And we all pay for that.

Which is why the UK needs to introduce a way of increasing its capacity, particularly for peak times.

Carbon

2 **LOW CARBON PRICE VOLATILITY**

The current UK electricity market is **too volatile and risky for developers to get the finance they need from investors to build new low carbon generation facilities.**

Which is why the UK needs to bring in a way of reducing the volatility and risk, **making it easier to finance and build new low carbon facilities.**

3 **REMOVING VOLATILITY**

So the Government set out to encourage the investment we need to replace older power stations and provide backup for more intermittent low carbon sources, ensuring:

- Generators benefit because they are paid fairly for being on stand-by.
- Large electricity users benefit because they are paid fairly for agreeing to reduce their consumption when required.
- The price of electricity at peak times is less volatile.
- And we all have enough affordable electricity when we need it most.

£/MWh

volatility removed

Capacity Market

3 **REMOVING VOLATILITY IN LOW CARBON**

So the Government set out to ensure revenues from electricity generated by low carbon sources are predictable for over a decade to come, which should mean:

- Developers benefit because they can secure the finance they need to build.
- Consumers benefit because the price they pay for electricity is more stable.
- More low carbon infrastructure is built at a lower cost.
- And the UK meets its decarbonisation target – affordably.

Capacity

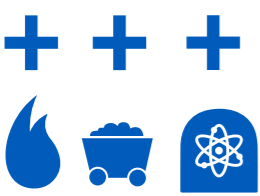
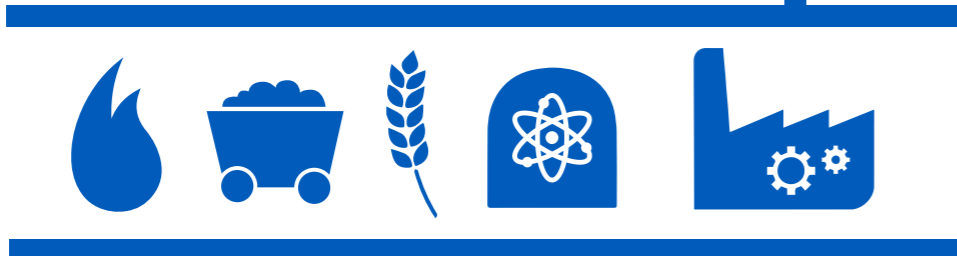
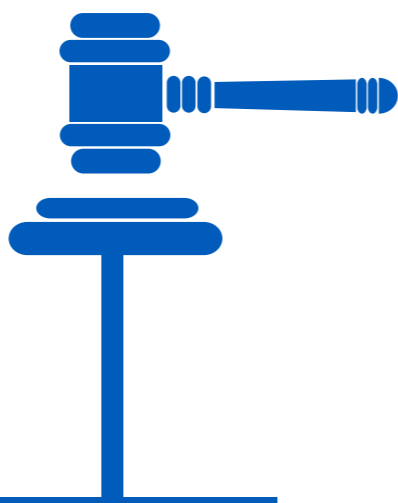
THE CAPACITY MARKET



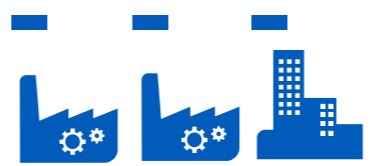
The Capacity Market is designed to encourage **generators to invest and then generate electricity, and large users to use less electricity** when the network most needs it. It's a step closer to more active management of demand in the electricity network.

Generators will be paid regular payments to keep their plant available to produce electricity when required. Large users will receive regular payments for agreeing to reduce consumption when required.

It will be managed through an auction process so that the most competitive prices are set.



GENERATORS IN THE CAPACITY MARKET receive regular payments for agreeing to produce electricity when required.



USERS IN THE CAPACITY MARKET receive regular payments for agreeing to reduce consumption when required.



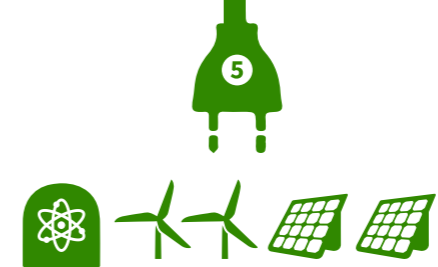
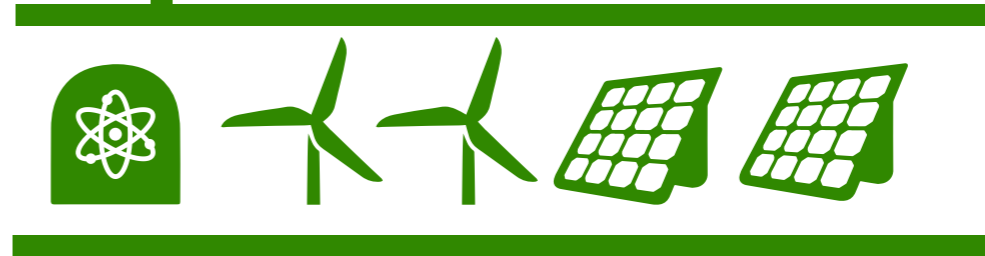
CONTRACTS FOR DIFFERENCE

Carbon



Contracts for Difference will **encourage new investment in low carbon electricity generation** by stabilising the price of electricity from low carbon sources.

Generators will make competitive bids for contracts to ensure that only the best and most cost-effective low carbon projects are supported.



GENERATORS WITH CFD CONTRACTS receive top-ups when the price of electricity falls below the agreed strike price and pay back if the price rises above it.





ESC SET-UP COSTS are estimated to be about £1.4m and will be divided between suppliers based on their market share in Q1 2015.

ESC OPERATIONAL COSTS will be divided between suppliers based on their market share of working day peak consumption (4-7pm) from November to February.

PAYMENTS TO CAPACITY PROVIDERS will be divided between suppliers based on their market share of working day peak consumption (4-7pm) from November to February.

LCCC SET-UP COSTS are estimated to be about £6.5m and will be divided between suppliers based on their market share in Q1 2015.

LCCC OPERATIONAL COSTS will be divided between suppliers based on their market share.

PAYMENTS TO GENERATORS will be divided between suppliers based on their market share.

ELECTRICITY SUPPLIERS

ESC SET-UP COSTS will be passed on to customers after April 2015 as a one-off charge based on their electricity consumption in Q1 2015.

ESC OPERATIONAL COSTS will be passed on to customers from April 2015 by adding them into the Elexon charge.

PAYMENTS TO CAPACITY PROVIDERS will be passed on to customers from October 2016 based on their working day peak consumption (4-7pm) from November to February.

The charges will be small at first, then increase in 2018 as the Capacity Market ramps up.

LCCC SET-UP COSTS will be passed on to customers after April 2015 as a one-off charge based on their electricity consumption in Q1 2015.

LCCC OPERATIONAL COSTS will be passed on to customers from April 2015 by adding them into the Elexon charge.

PAYMENTS TO GENERATORS will be passed on to customers from April 2015 based on their consumption of electricity.

The charges will be small at first, then are expected to increase from 2016 as more Contracts for Difference are awarded.

ADAPTING YOUR ENERGY STRATEGY

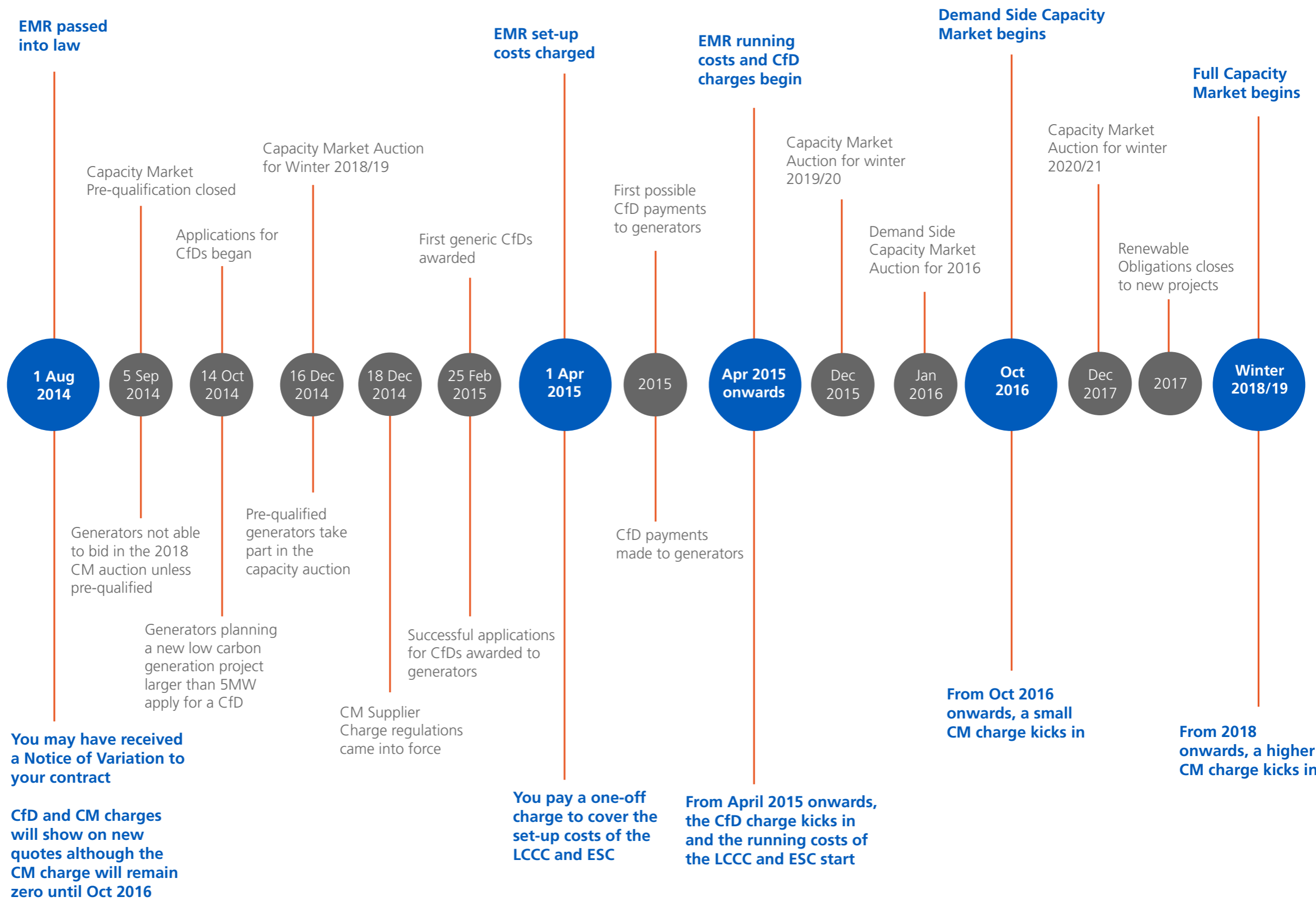
ENERGY EFFICIENCY | TRIAD MANAGEMENT | DEMAND RESPONSE | ONSITE GENERATION



EMR Timetable

What's happening?

What's the impact?





How to budget

LCCC + ESC set-up costs

10p / MWh
A one-off charge in Q2 2015 based on your electricity consumption in Q1 2015

LCCC + ESC running costs

6p / MWh
Included in the Elexon charge from April 2015 onwards

Cost of Payments to Capacity Providers

Our forecast range for 2016/17 is between £0.01 and £0.65 / MWh with a midpoint of £0.33 / MWh.
This cost will rise significantly in 2018/19. Our forecast range is from £3.12 to £5.14 / MWh with a midpoint of £4.13 / MWh.

Cost of Payments to Generators with CfDs

Our forecast range for 2015/16 is between £0.46 and £0.62 / MWh with a midpoint of £0.54 / MWh.
This cost will rise steadily to 2018/19. Our forecast range is from £6.41 to £7.93 / MWh with a midpoint of £7.17 / MWh.





e-factsheet- a better way of working

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