



Inveralmond House
200 Dunkeld Road
Perth
PH1 3AQ

Mrs Fay Geitona
ERGEG

Telephone: 01738 456488
Facsimile: 01738 456415
Email:
samantha.ridsdale@scottish-
southern.co.uk

Date : 27th April 2010

Dear Mrs Geitona,

Generation Adequacy Treatment in Electricity – Call for Evidence

Thank you for the opportunity to respond to this consultation.

SSE is the second largest generator in the UK, with over 11.5GW of generation capacity, 2GW of which is renewable. Additionally, we are the UK's second largest energy supplier, with more than 9 million gas and electricity customers, and we have an electricity networks business which is responsible for around 127,000km of overhead lines and underground cables. We also hold a 50% stake in Scotia Gas Networks (a UK gas distribution business) and operate telecoms, contracting and gas storage businesses. We have a generation and supply operation in Ireland and are currently developing our renewable generation portfolio in Portugal, Sweden and the Netherlands.

We agree that generation adequacy measures should be coordinated on a European level. However, there are a number of existing domestic and European barriers to achieving Europe-wide generation adequacy which should be resolved before any additional measures are implemented. One of the key hurdles to overcome is regulatory uncertainty, which could be exacerbated by implementing European measures prematurely.

Our responses to the specific questions are contained in the annex below.

If you would like to discuss our response or require further information, please do not hesitate to contact me.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Samantha Ridsdale', written over a horizontal line.

Samantha Ridsdale
Regulation and European Affairs

1 What are the key elements for ensuring generation adequacy in the competitive electricity market in EU MS and the EU as a whole?

Generation adequacy can be ensured in EU MS and in the EU as a whole by securing sufficient investment in both diverse generation assets and transmission infrastructure. These two areas are equally important and a balance of investment should be encouraged in both.

In order to encourage investment, the regulatory framework within each MS and across the EU must be clear, stable and sustainable. Any regulatory or political interventions in the energy markets which increase risk and uncertainty must be minimised and regulators should be encouraged to coordinate their work in order to provide long term investment signals to the market.

2 Do you observe any barriers for investing in new generation capacity? If yes, please list and explain them.

There are currently several barriers to investment in both generation and transmission infrastructure capacity. As stated previously, we believe that both of these investment areas are critical to ensuring generation adequacy and cannot be dealt with in isolation.

- Uncertainty surrounding the long term regulatory framework

Over the past few years, there have been a number of cumulative domestic and EU regulatory changes which have introduced uncertainty into the market. Examples of these are –

- Progressively tightening environmental legislation which initially sets out limits and restrictions for generators but is then superceded by additional legislation which undermines the generator's initial investment decision. Indications are that this trend is to continue with agreements under the current Industrial Emissions Directive potentially being undermined by an additional European Safety Net proposal and a future National Emissions Ceiling Directive. Although it is obvious that the general direction of travel is for tighter limits, generators cannot confidently make "future-proof" investment decisions whilst the goal posts are constantly being moved.
 - There is considerable uncertainty surrounding the carbon framework post-2020. This is exacerbated by ongoing proposals for a carbon tax and other specific national schemes. Uncertainty in this area produces uncertainty in the likely rate of return for generation projects, thereby increasing project financing costs and also the likelihood of projects not going ahead. A stable, long-term carbon framework must be implemented in order to reduce uncertainty for investors.
 - Both the European energy regulators and financial regulators have commenced work on tightening the regulatory framework for energy trading. Whilst this work is undoubtedly useful and may assist in the harmonisation of markets, the regulators are not coordinated in their actions and there exists a high likelihood of regulatory overlap, again introducing uncertainty to the internal market.
- Ineffective and volatile domestic locational signals for generators

The current GB methodology for transmission charging presents volatile and excessively wide-ranging locational signals for generators. Charges range from £22/kW in the North of Scotland to a **subsidy** of £7/kW in the South of England. Whilst it might be perceived that these are

strong and positive signals to locate generation in an appropriate area, in reality they inhibit investment by –

- Discouraging new renewable generation from locating in the North of Scotland where the best resources for renewable energy exist.
- Encouraging existing generators located in high charging areas to close earlier than originally planned to avoid excessive transmission costs. This has recently occurred in the case of Peterhead power station where part of the generator may close earlier than expected in order to reduce the impact of transmission charges.
- Providing short-term and volatile locational signals, which can swing up to 60% from year to year, to an industry which requires stable and long-term signals.

Generators require certainty for a 20 – 25 year period to support investment decisions. Uncertainty can lead to new projects being withdrawn completely or the financing cost of the project increasing to cover the increased risks.

- Disparity in transmission charging regimes across the EU

It is important to encourage cross-border trade if EU-wide generation adequacy is to be achieved. It is critical that excess generation in one area can be transferred to where it is required and the harmonisation of charging arrangements, in particular, is required for efficient cross-border transfer of power to occur.

However, even with the recent adoption of the Inter TSO Compensation Mechanism Regulation, there are unclear signals presented to encourage cross-border trading.

An example of this is the current and planned interconnection between the UK and Ireland. In order to participate in cross border trading, generators in the Republic of Ireland must pay transmission charges in the Irish Single Electricity Market and also in the GB BETTA market via their use of the Moyle Interconnector. The Moyle Interconnector lands in the South of Scotland in a zone which imposes transmission charges of around £11/kW. However, once the planned E-W Interconnector is finished, it will land in Wales where the transmission charge is around £3.60/kW. This gives generators in the Republic of Ireland a clear signal to flow power through the E-W Interconnector rather than through the Moyle Interconnector. However, it also gives generators in Northern Ireland a signal to flow power south through the North/South tie line and subsequently through the E-W Interconnector to GB. This routing of power will cause unnecessary congestion in the North/South tie line, thereby increasing costs to customers in Ireland. Similarly, the Moyle Interconnector will not receive efficient use as the economic signals discourage it. The investment signals here are skewed, suggesting that the North/South tie line should be upgraded whereas efficient use of the Moyle Interconnector would avoid the need for this.

Given the forecast for the increase in renewable generation in Ireland, significant export capacity will be required. Whilst the harmonisation of transmission charging regimes has the ability to ensure efficient use of interconnectors and effective delivery of power to the markets where it is required, the current arrangements clearly send mixed signals to both generators and TSOs. This uncertainty is likely to hinder the delivery of generation adequacy across Europe.

- Delays to planning consents for transmission infrastructure and generation projects

The length of time it takes to secure planning consent for power stations and transmission infrastructure in the UK is a considerable obstacle to investment. The average time to get consent for onshore wind in the UK is over 2 years and for fossil plant, the time is significantly longer. Furthermore, transmission upgrades are faced with delays of 7 years or more. The



delays serve to discourage investment in generation and transmission infrastructure and hinder progress on generation adequacy.

3 In case of additional measures for ensuring generation adequacy, what would be the key issues to take into account?

If measures additional to removing the barriers presented above are deemed to be necessary, which we believe at present is not necessarily the case, they should be coordinated, transparent and ensure a level playing field for all generators both domestically and across Europe.

There is certainly a risk from having variant and possibly contradictory approaches in neighbouring Member States. As with achieving a stable and long-term regulatory framework, this will require coordination on a European level.

Secondly, we would strongly disagree that locational signals should be incorporated into any adopted generation adequacy methodology. Whilst, superficially, these may appear to ensure that generation is located in the “correct” places, our experience of locational signals within the GB market is that they discourage investment and distort trading both domestically and from a cross-border perspective. It is highly likely that locational signals on a European scale would lead to a tilted playing field, significant distortion of trade and deficiencies of generation in peripheral areas, which is exactly what the Third Package seeks to avoid. These signals would exacerbate existing regulatory risk and hinder the achievement of European-wide generation adequacy.