

NERA

Economic Consulting

Developments Since 1997 in the UK Power Sector: Environmental and Social Consequences

Power Sector Reform and Sustainable Development

UNEP/IEA Brainstorming Meeting

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Marsh & McLennan Companies

How Markets Work SM

Generation

- More divestment, more real competition: no generator now has more than 20% share: prices have fallen markedly
- This has led to permission for some mergers between generators and distributors/suppliers
- Moratorium on new gas-fired investment 1998-2000 to help coal: little long-term effect
- In wholesale market, from Pool to NETA (also mainly to help coal) – a bilateral contract market with no central despatch – damaging for renewables which have suffered excessive discounts

Competition in Retailing

- In 1998/99, choice of retailer extended to all consumers
- Process cost c. £1bn. and was delayed: all consumers pay for this over 7 years
- But retail prices also falling, so no price rises as a result
- Licences for distribution (wires) separated from retailing, though same companies may still do both
- Residual price controls on retail prices may be abolished soon

Social Objectives

- Fuel poverty a major problem in UK due to energy-inefficient housing stock
- Numbers in official fuel poverty (10% or more of income on fuel) have fallen from c. 5 million to c. 3.5 million since 1997 due to retail prices falling
- VAT reduced from 8% to 5% in 1997
- Customers not disconnected for debt, but must accept pre-payment meters, calibrated to recover debt
- Households exempted from new environmental taxes (Climate Change Levy and GHG emissions trading (thus complicating their design)

Environmental Regulation/Policy

- Little new in conventional air pollution (mostly at EU level)
- Nuclear waste has seen no activity in 5 years, except for a new 5-year consultation starting this year
- Main focus has been on Climate Change Programme, including CCL/emissions trading,
- Energy Efficiency Commitment (target for energy suppliers to reduce customers' energy use, especially the fuel poor and vulnerable) for which companies charge all consumers
- A new Renewables Obligation on retailers, requiring them to buy progressively more renewable electricity to reach 10% by 2010 (3% now)
A buy-out price 3p/kWh above wholesale prices. Tradable Green Certificates go with this

Economic Regulation

- OFFER and OFGAS merged in OFGEM – gas and electricity now regulated together
- Utilities Act Of 2000 gives protection of consumers as a primary duty of regulator for the first time
- Act also allows Ministers to give ‘guidance’ to regulators on social and environmental policy. But guidance not yet given, and will not over-ride legal duties – therefore unlikely to have much effect

Energy Policy

- Was mainly a matter of pursuing economic objectives in 1990s (plus help for coal in 1998)
- Re-emergence of security concerns and seriousness of climate change have re-opened a wider energy policy debate
- Prime Minister gave PIU, Cabinet Office, job of reporting on implications of these issues for energy policy – major Energy Review published in February 2002
- Government now promising White Paper on energy/environment/security around turn of year, after public consultation
- Energy Review argues that if countering climate change remains an important objective, then environmental objective will need primacy in energy policy (over economic and social objectives)
- May require new legislation if accepted