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Norwegian Ministry of Petroleum and Energy
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Norway

For the attention of:
Andreas Eriksen
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16 January 2015

Consultation on the proposal to amend the law on electricity certificates

We are writing regarding the Norwegian Minister of Petroleum and Energy (MPE) proposal of 3rd December 2010 to amend the law regarding electricity certificates (the Proposal), which Proposal resulted from the 2014 Consultation (the Consultation) by the Norwegian Water Resources and Energy Directorate (NVE) on the 2015 "Control Station" under the joint Norwegian and Swedish electricity certificate scheme.

HgCapital is one of the largest investors in Swedish onshore wind and has been actively pursuing investments in Norwegian onshore wind. We submitted comments to NVE as part of the Consultation. (We also submitted comments to the Swedish Energy Agency). Our comments are noted in the Proposal .

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The Proposal - Responsiveness to HgCapital Comments

Raising the quota curve. We are pleased to see the favourable response on increasing the quota curve for electricity certificates in order to reflect what has actually happened with supply and demand.

Quota curve in TWH. We are also pleased that MPE recognizes that expressing the annual quota requirements in TWH is favourable despite the fact that MPE is unable to advance this in light of Sweden's decision not to consult on this point. Given the lack of clarity in the market, and that the current percentage method of setting the quota curve has created many issues, we think that MPE should, if possible, continue to engage on this point in three ways:

1. We recommend that the Proposal be changed to allow for setting the curve in TWH should Sweden later agree to a change in methodology. This would be more expedient should an agreement be reached.
2. Norway should continue to engage with the Swedish authorities on this point.
3. Given that the percentage method of setting the quota curve can produce unintended results, MPE and NVE should carefully review the current electricity certificate supply and demand situation, and forecast supply and demand, to ensure that the new quota curves are accurate and there is a significantly reduced chance of recreating the substantial surplus that exists today.

2020 Deadline for electricity certificate qualification. We support and agree the proposal for extending the deadline for Norwegian Projects, provided that this is by exception and it is clear that projects must be fully in operation to secure certificates; that is an effective and clear policing mechanism that will not allow clearly late projects to qualify.

Supply and demand transparency. In our submissions, we strongly commented that increased transparency of electricity certificate supply and demand, especially reporting of investment decisions is critical to a well-functioning electricity certificate market and providing investors and traders with the information necessary to make long term investment decisions. From your comments, we glean that Norway generally favours increased transparency, but objections from Sweden make it difficult to implement.

Whilst we understand the political difficulties that you might face with Sweden, we would recommend working closely with the industry to increase transparency. In the year since the Consultation was launched market transparency has not increased. In fact if anything, the market has become more opaque. This has led to a major reduction of investment decisions in new renewable energy facilities in Sweden and virtually no new investment decisions in Norway. Should the opportunity arise to reopen the discussions on transparency and reporting, we would encourage the Ministry to do so.

The Proposal - Revision of transition arrangements for small hydro

We are very concerned with the proposed amendments to the transition arrangements in respect of hydro facilities with less than 10MW of capacity. We believe that granting such projects access to the electricity certificate system creates four substantial issues:

1. It sets a precedent for retroactive changes that threaten to undermine the stability and integrity of the electricity certificate system.
2. The proposed changes were not discussed in NVE's Control Station consultation materials and thus the changes and proposed impact have not been subject to industry scrutiny and input.
3. It will increase the supply of electricity certificates in a system that is already in substantial oversupply, threatening to further erode the value of electricity certificates creating economic harm to existing investments and discouraging new investments.
4. It is not consistent with the spirit or the intent of the Norwegian and Swedish electricity certificate system which is to favour new investments and not to provide a windfall reward to investors who could not have relied on the system. It also raises questions of state aid to those projects.

Electricity Certificate System integrity. We believe that retroactively granting electricity certificates to projects built without access to the system sets a dangerous precedent for the system. It introduces into what was intended to be a technology neutral, least cost system, a political element of favouring one technology and group of producers over others. It leads to questions as to what other retroactive changes may occur at the next control station.

In making investments under the electricity certificate system, investors were aware that there would be control stations at scheduled points, and that revisions of the quota curves would be considered. What was never expected was a material retroactive change to increase the supply of certificates for existing investments, except as outlined originally where Norwegian projects surrendered Enova grant funding in return for joining the electricity certificate system. Thus, whilst investors faced uncertainty over how quota curves and the system might develop, it was clear that investments that pre-dated 2012 could be included except in very limited circumstances.

In essence, by including these projects in the regime sets a precedent that the supply, demand and eligibility criteria for green certificates can be changed by either the Swedish or Norwegian government unilaterally, not only on a prospective basis but on a retroactive basis. This does not lead to an efficient market in green certificates and represents a materially increased risk of market intervention that investors can no longer predict. We believe it will further discourage investment not only in Norway but in the entire system.

No consultation; no analysis of market impact. Retroactively granting electricity certificates to hydro projects was not mentioned in the NVE Consultation. As a result, industry stakeholders have not had a chance to consult, analyze or provide information on the impact of the proposed changes. This raises issues about the transparency and integrity of the consultation process and could lead to greater investor uncertainty about future control stations and consultations.

There also does not appear to be any impact of the retroactive changes on the electricity certificate market. Under the proposal, in January 2016 the qualifying hydroelectric facilities will receive 4 years of electricity certificates – up to 8 TWH if all 2 TWH of estimated projects qualify. It is quite likely that the projects will immediately seek to sell all of those certificates. Because they had no expectation of receiving them, they could be less sensitive to price. If these certificates – equal to nearly a third of the annual target, flood the market there is a substantial risk of price collapse. There is no indication that MPE or NVE have made any analysis of market impact, or that simply increasing the quota curve for the new projects will protect the market. This is where the integrity and viability of the system is most at risk. In other countries such a change would have been made with substantial consultation and analysis on market impact.

Excess electricity certificate supply. Whilst we appreciate MPE's proposal to adjust the quota curve for the retroactively granted electricity certificates, we still think this creates substantial problems for the market. As of 31 December there was an accumulated surplus of more than 13 million TWH of electricity certificates. This substantial surplus, which we acknowledge, has numerous causes and is what is holding down certificate prices and generating financial stress for existing investments while inhibiting new investments. Whilst the adjustment in the quota curve to reflect the increased hydro certificates may on its face address the issue by increasing supply, we have substantial doubts that it will and could lead to further price falls.

We do not think that hydro should be rewarded with windfall profits, and encourage you to not make this change. If Norway insists on proceeding, we strongly urge that there be further studies on the impact on the electricity certificate market, particularly on price. NVE and the Swedish energy authorities should look far more carefully at the amount of surplus in the system and should consider further upwards changes to the quota curve to reflect both the surplus that continues to increase and the massive amount of new certificates that will be dumped on the system in 2016.

Windfall inconsistent with the Norway – Sweden Renewable energy treaty; state aid. The electricity certificate treaty between Norway and Sweden clearly states that the intent of the system is to deploy electricity certificates to support the construction of new renewable energy projects, not to provide a financial windfall to existing projects. We think the inclusion of these new additional hydro schemes is inconsistent with the intent of the treaty and undermines both its goal and the integrity of the green certificate market.

We note that MPE cites the low profitability of the hydroelectric projects built during this period as a reason for granting them electricity certificates. By this same argument, Norwegian and Swedish wind farms built under the electricity certificate system at any time up until today could argue that they should receive additional green certificates or benefits because of reduced profitability that has resulted from the poor design of the electricity certificate system.

Finally, has MPE considered the state aid implications of granting certificates to existing facilities. The European Union has announced new state aid guidelines and procedures for renewable support schemes calling for both market based systems and competitive bidding.



It would appear that the grant of certificates to the existing hydro is nothing but a benefit given to investments already made and we struggle to see how it is consistent with the European Union state aid guidelines.

Therefore, we strongly suggest that you reconsider legislation to grant electricity certificates retroactively to existing hydro facilities, and consider discussions with Sweden about whether such actions will be beneficial or detrimental to confidence in the electricity certificate scheme. If you insist on proceeding down this route we believe additional work and study is required to determine whether the increases in the quota curve suggested are sufficient to mitigate the negative impacts of this retroactive change.

Yours faithfully,

A handwritten signature in black ink, appearing to read "T. Murley", with a long horizontal flourish extending to the right.

Thomas Murley
Head of Renewable Energy
HgCapital

c.c. Swedish Energy Agency