Why the Market Needs a Public Service Obligation

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Costs and Prices: The PSO tariff is not a tax

- It is widely assumed that Public Service Obligations (feed-in tariffs for wind power etc.) disturbs an efficient market allocation.
- My view is that this assumption is wrong and electricity markets cannot work without these non-market institutions.
- **This point is especially important for understanding the economics of renewable energy systems**
The Fundamental Change in Costs

In the transition to a renewable energy system:
- The change does not happen in cost level.
- The change happens in cost structure.

![Electricity production costs chart]

- **Coal**
  - Investment
  - O&M
  - Fuel

- **Wind**
  - Investment
  - O&M
  - Fuel
The change in cost structure affects the market outcome

- **Price** levels will go down but total **costs** are stable.
- Capacity costs are not **avoidable** in the very short term; hence they do not enter the economic considerations that shapes the market prices in the electricity exchange.
The electricity exchange market is marginalised as a source of revenue.
The empirical trend confirms the theoretical presumptions
Our ‘Price+PSO’ system is basically in economic balance

Given the change in cost structure, the PSO system is a vital component of the energy economy.
The PSO must be internalised in the electricity trade

Removing the PSO from the electricity bill to the state budget subsidises energy production.
International Electricity Markets and the Real Challenge

- The problem is not that imported electricity is subject to a PSO tariff.
- The problem is that exported electricity is not subject to a PSO.
Summarising

1) The PSO tariff is a capacity payment.
2) Capacity payments are here to stay.
3) Capacity costs should be/remain internalised in the energy trade.
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