

Energy UK Response to BEIS consultation: Contracts for Difference for Low Carbon Electricity Generation – Consultation on further drafting amendments to the CfD contract for Allocation Round 4

29th October 2021

About Energy UK

Energy UK is the trade association for the energy industry with over 100 members spanning every aspect of the energy sector – from established FTSE 100 companies, right through to new, growing suppliers and generators, which now make up over half of our membership.

We represent the diverse nature of the UK's energy industry with our members delivering over 80% of both the UK's power generation and energy supply for the 28 million UK homes as well as businesses.

The energy industry invests £13bn annually, delivers £31bn in gross value added on top of the £95bn in economic activity through its supply chain and interaction with other sectors, and supports 738,000 jobs in every corner of the country.

Introduction

Energy UK welcomes the opportunity to respond to the BEIS consultation on Contracts for Difference (CfD) – consultation on further drafting amendments to the CfD contract for Allocation Round 4.

Whilst we understand the government's aim is to align CfD standard terms and conditions with the final decision expected from Ofgem on the removal of BSUoS charges from generators, we disagree with the proposed approach in the consultation. Our response will focus specifically on the illustrative drafting around this issue.

Energy UK suggests that the CfD standard terms and conditions are amended prior to the auction to remove BSUoS charges from the Strike Price indexation formula. We believe this will create a level playing field between parties applying to connect to the transmission and distribution networks, avoid artificially inflated bids and avoid further deduction from the strike price when Ofgem implements its decision to remove charges.

Should you have any questions regarding this consultation response then please do not hesitate to get in touch via the details below.

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Response to Q7: The Government welcomes views on the illustrative drafting which reflects the possible decision by Ofgem to remove generators' liability to pay BSUoS charges in respect of CfD generators.

Energy UK shares the government's ambition to strengthen the UK renewable energy sector by ensuring that the CfD continues to function as originally intended. We also recognise the government's aim is to align CfD standard terms and conditions with the final decision from Ofgem on the removal of generators' liability to pay BSUoS charges.

However, our overall concern is that the current drafting as it stands will introduce an unintended competitive disadvantage to transmission-connected generators compared with distribution-connected generators, as a result of having to take into account potential system balancing charges, which will not have been priced into the developers bids.

For transmission connected generators, the existing CfD contains Terms and Conditions (T&Cs) to set an Initial Balancing System Charge level and to then adjust this for subsequent changes to BSUoS charges, year on year. This is to keep the CfD contract broadly long-term neutral to changes in balancing system charges, which are outside of generators' control. This feature of the CfD T&Cs reduces the risk to generators of a variation in this cost component and has been a welcome mechanism in previous CfD rounds.

Ofgem is now considering whether to remove generators' liability to pay BSUoS charges (CMP308, CMP361 and CMP362¹) and plans to publish their minded to decision on this by end December 2021. We understand that is highly likely that Ofgem will decide to remove BSUoS charges from generators because:

- the Connection and Use of System Code (CUSC) Panel has made a clear recommendation² to do so (which Ofgem has historically tended to follow) and;
- Ofgem has explicitly stated³ its intention to remove BSUoS charges in its response to the publication of the final report of the second Balancing Services Use of System (BSUoS) Task Force on 10th December 2020 where they stated: "...we agree with the Task Force's recommendation that BSUoS should be recovered from Final Demand only".

We recognise the government's position of not wanting to unduly influence the outcome prior to Ofgem's final decision however, given that Ofgem has given a clear indication of its final decision we believe that by removing BSUoS charges would simply reflect Ofgem's latest statement on their decision. Some transmission connecting applicants may simply not be able to risk the Ofgem direction being reversed. We consider it is therefore reasonable for BEIS to amend the T&Cs to match Ofgem's latest published statement of their intention.

If the current proposals of deducting the I base from future strike price calculations were retained, this will oblige generators to include this value in their CfD bid, because it will definitely be deducted irrespective of what assumptions a transmission-connected generator has actually made in building up their CfD bid.

¹ <https://www.nationalgrideso.com/industry-information/codes/connection-and-use-system-code-cusc-old?mods=>

² <https://www.nationalgrideso.com/document/210846/download>

³

https://www.ofgem.gov.uk/sites/default/files/docs/2020/12/response_to_the_second_bsuos_task_force_report.pdf

Subsequently, this approach will increase the CfD bids of transmission-connected generators relative to distribution-connected generators. The value is very significant (e.g. it amounted to £3/MWh in CfD Auction Round 3) particularly in what is expected to be a highly competitive auction.

The overall effect on the CfD auction of including the deduction for I base will be two-fold:

- It will significantly disadvantage transmission-connected generators in bidding in the CfD auction, for a cost that will not in fact arise and is effectively an artefact of the proposed drafting.
- It will raise the supply cost curve of eligible projects and result in a higher clearing price for the auction. That in turn will increase the cost to consumers, as distribution-connected generators will receive all of the uplifted strike price, as no deduction will be applied to them.

In light of the above, Energy UK would suggest that the CfD standard terms and conditions are amended prior to the auction to remove BSUoS charges from the Strike Price indexation formula. This would create a level playing field, avoid artificially inflated bids and avoid further deduction from the strike price when Ofgem implements its decision to remove charges. This increase in competition will result in savings to the end consumer.

Alternatively, we would suggest that the CfD standard terms and conditions are amended prior to the auction, to allow for transmission-connected generators to proceed on the basis that BSUoS charges will be removed, but with a provision which outlines the possibility of BSUoS charges being reintroduced in the unlikely event that Ofgem decides not to proceed with removing the charges.

We believe that both of the approaches outlined will provide more clarity and importantly more fairness in the bidding process.