

PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Second Delegated Legislation Committee

DRAFT CONTRACTS FOR DIFFERENCE
(MISCELLANEOUS AMENDMENTS)
REGULATIONS 2016

Tuesday 28 June 2016

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The Committee consisted of the following Members:

Chair: † NADINE DORRIES

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| † Ansell, Caroline (<i>Eastbourne</i>) (Con) | McKinnell, Catherine (<i>Newcastle upon Tyne North</i>) (Lab) |
| Boswell, Philip (<i>Coatbridge, Chryston and Bellshill</i>) (SNP) | † Murray, Mrs Sheryll (<i>South East Cornwall</i>) (Con) |
| † Davies, Chris (<i>Brecon and Radnorshire</i>) (Con) | † Quince, Will (<i>Colchester</i>) (Con) |
| Elliott, Julie (<i>Sunderland Central</i>) (Lab) | † Smith, Henry (<i>Crawley</i>) (Con) |
| † Gardiner, Barry (<i>Brent North</i>) (Lab) | † Smith, Julian (<i>Skipton and Ripon</i>) (Con) |
| Johnson, Alan (<i>Kingston upon Hull West and Hessle</i>) (Lab) | † Stuart, Ms Gisela (<i>Birmingham, Edgbaston</i>) (Lab) |
| † Leadsom, Andrea (<i>Minister of State, Department of Energy and Climate Change</i>) | † Throup, Maggie (<i>Erewash</i>) (Con) |
| † Lopresti, Jack (<i>Filton and Bradley Stoke</i>) (Con) | † Tracey, Craig (<i>North Warwickshire</i>) (Con) |
| † Lynch, Holly (<i>Halifax</i>) (Lab) | Katy Stout, <i>Committee Clerk</i> |
| † McCaig, Callum (<i>Aberdeen South</i>) (SNP) | † attended the Committee |

Second Delegated Legislation Committee

Tuesday 28 June 2016

[NADINE DORRIES *in the Chair*]

Draft Contracts for Difference (Miscellaneous Amendments) Regulations 2016

2.30 pm

The Minister of State, Department of Energy and Climate Change (Andrea Leadsom): I beg to move,

That the Committee has considered the draft Contracts for Difference (Miscellaneous Amendments) Regulations 2016.

Before I turn to the detail of the regulations, I want to make clear the Government's commitment to delivering the secure, affordable and low-carbon energy supply that the country needs and which the Secretary of State set out in her reset speech in November of last year. *[Interruption.]* That sounds like an aeroplane taking off in the corridor—sorry, it completely threw me.

The decision that the country made last week to leave the European Union does not change the Government's approach to the challenges, and we remain fully committed to delivering on our priorities, including encouraging the development of offshore wind, where we see great potential, and where good progress is already being made, to get costs down and to deploy at scale. The ability to provide quality jobs and apprenticeships and to support industrialisation of the supply chain, including UK companies, is just one of the elements that makes the industry attractive. We are proceeding with plans to hold a competitive allocation round for the less established technologies later this year, and we hope to announce the details as soon as we can.

The instrument amends regulations concerning the contracts for difference scheme. The scheme is designed to incentivise the significant investment that we need in our electricity infrastructure to address the challenges I mentioned earlier: to keep our energy supply secure; to keep costs affordable for consumers; and to help meet our decarbonisation targets.

Contracts for difference, or CfDs, give eligible generators increased price certainty through a long-term contract, which allows investment to come forward at a lower cost of capital and therefore at a lower cost to consumers. Participants in the scheme bid for support via a competitive allocation, which ensures that costs to consumers are minimised. As I said, we plan to run the next allocation round late in 2016.

Hon. Members will be aware that the first CfD allocation round was held in October 2014, leading to contracts being signed with 25 large-scale renewable generation projects, at significantly lower cost than if the projects had been carried out under the renewables obligation scheme. Although the scheme is operating successfully, the Government are looking to make a number of minor amendments, first to ensure that an application for a CfD cannot be made where there is a pending application for a capacity agreement in respect of the

same unit and, secondly, to improve the efficacy of the allocation process, including by making available non-price bid information to enable evaluation of the allocation rounds.

To implement our proposed amendments, four sets of regulations need to be amended: the Contracts for Difference (Definition of Eligible Generator) Regulations 2014, the Contracts for Difference (Allocation) Regulations 2014, the Contracts for Difference (Standard Terms) Regulations 2014 and the Electricity Market Reform (General) Regulations 2014. The instrument under consideration makes a number of minor and technical amendments to the current regulations, and I will run through the amendments briefly.

The amendments are designed to improve the effectiveness of the CfD schemes. The most significant of the amendments include, first, ensuring that an application for a CfD cannot be made where there is a pending application for a capacity agreement in respect of the same unit. That ensures that an applicant cannot apply to participate in the CfD and the capacity market auction at the same time and then make a choice of scheme, potentially distorting the allocation for both processes. Secondly, the connection requirements applicable to generators who connect to the national transmission or distribution system, or to a private network, are set out, to align with the allocation framework.

Callum McCaig (Aberdeen South) (SNP): May I take the Minister back to the point about the two models for which generators can apply? I understand why one would look to separate the two, and I think that is supported, but will it lead to any potential projects falling off? When looking to bring something forward, one would want to keep as many options as open as possible. What does the Minister see as the potential for projects not getting beyond the drawing board because they have only one avenue to pursue?

Andrea Leadsom: The hon. Gentleman is right to ask the question. Essentially, it is saying that the consumer subsidy for each is sufficient to bring forward investment, so it would not be right or fair either to allow double subsidy for the same project—effectively twice the amount of subsidy or thereabouts—or to bid for one and the other and choose between them. Neither of those things would be right and fair. Our assessments show that it should be perfectly possible to decide either to apply for a CfD or for a capacity market auction bid. No one should need to do both, so I am ensuring that they cannot do both.

The most significant amendments include setting out the connection requirements applicable to generators who connect to the national transmission or distribution system, or to a private network, to align with the allocation framework. Those are key qualification requirements for applicants who connect to the grid in that way and, by having the detail in regulations, we will provide greater certainty to generators in advance of a future allocation round.

We also seek to refine the procedures that apply if there is a need to delay or rerun the auction or allocation round, which again will lead to greater clarity for investors. We make a distinction between confidential price information and non-price information in a sealed-bid

submission, which will ensure that the Secretary of State can obtain information relating to non-price sealed-bid data, in order to evaluate the efficacy of the allocation round.

The amendments enable unincorporated joint ventures to participate in the CfD regime, and ensure that only those bank holidays observed in England and Wales are considered within the definition of “working days”. The proposal to focus on a single jurisdiction to define a working day allows for consistency of time periods and deadlines throughout the CfD regime. The amendments also allow the Secretary of State to issue a direction to the CfD counterparty to amend signed CfD contracts where the sustainability criteria have been altered in subsequently published versions of the CfD.

All of the proposals being implemented by the instrument were publicly consulted on and received a largely favourable response. Some concern was expressed about the proposal to split non-price data from confidential price information in a sealed-bid submission. We are confident that the non-price data can be effectively disaggregated from confidential price information and anonymised in such a way that individual projects cannot be identified. That will enable us to evaluate the efficacy of the allocation round.

As a final point, I take this opportunity to assure all Committee members that the Government will continue to evaluate and monitor the reforms following implementation, ensuring that the measures put in place remain effective and continue to represent value for money for the consumer.

2.38 pm

Barry Gardiner (Brent North) (Lab): It is a pleasure to serve with you in the chair, Ms Dorries, albeit you are at a lower elevation than might have been supplied with a cushion. I would like to start by saying that I, too, am very sad that my hon. Friend the Member for Southampton, Test (Dr Whitehead) is not standing here to respond to the Minister. He has served this cause of energy in the UK very well as shadow Minister. I think we would all wish to pay tribute to him, with this being the first opportunity.

This is quite extraordinary. On the purpose of the instrument, we read in the explanatory memorandum that:

“These amendments will not change the way in which Contracts for Difference (CFDs) are allocated, but will make minor changes to the existing allocation methodology”.

I do not know how contracts for difference are allocated if they are not allocated by the existing methodology.

2.39 pm

Sitting suspended for Divisions in the House.

3.06 pm

On resuming—

Barry Gardiner: If I may pick up where I left off, I was pointing out that the explanatory memorandum seems entirely contradictory:

“These amendments will not change the way in which Contracts for Difference (CFDs) are allocated, but will make minor changes to the existing allocation methodology”.

I do not know what

“the way in which CFDs are allocated”

means, unless it is the existing methodology. To say that it will do what it will not seems a contradiction rather than an explanation. I urge the Minister to make sure that the explanatory memorandum does what it says on the tin, namely explain rather than confuse.

The other confusing aspect is the impact assessment. The regulations are dated 2016 and they amend regulations made in 2014, yet the impact assessment for these regulations predates those made in 2014. Quite how this is supposed to be an impact assessment of what we are considering today, I do not know.

Ultimately, the Opposition will not seek a Division on these regulations, but certain points of housekeeping should be noted. Many aspects of the regulations that the Minister discussed simply tidy up existing problems. I ask her to clarify whether anyone, to date, has received double subsidy or been known to game the system. Those were the two reasons the Minister rightly gave for these regulations. I therefore think it is important to know whether there has been a problem and these regulations are being introduced to stop more horses bolting from the stable, or whether they are simply preventive, because officials have realised there is a potential issue here and we need to tighten up the regulations in that respect.

The aim here is to prevent applicants from taking a flyer on a possible capacity payment and, at the same time, putting in for a CfD and then discarding whichever one seems to be less promising later in the application process. The regulations have been amended to introduce the notion of determination or establishment. That is entirely understandable. If someone holds a capacity agreement on a plant, they cannot apply for a CfD as things stand. However, there may be marginal cases in the pre-qualification process. It would be helpful if the Minister confirmed that there will be two amber lights, so that if someone puts in for a CfD and for the capacity market, there is an amber light for both those applications, and that at the point at which pre-qualification is determined to allow them to bid in the capacity auction, their CfD application will be invalidated.

I would also like to ask the Minister why this seems not to be symmetrical. It seems as if applying for a CfD while a capacity agreement is being considered is not outlawed by the amendment in the same way. What happens if somebody has a CfD under consideration and then applies for a capacity payment? There is a question of symmetry. It is clear that the regulations will tighten up the process one way round, but it is not clear that they will do the same the other way round. Will the Minister clarify whether there is symmetry, and I have just missed it, or whether we need a further tightening exercise to achieve the objectives that she and I share?

The Minister’s introduction was welcome. She spoke of the need to reassure investors that the referendum has not changed the Government’s energy objectives. In effect, she said that nothing has changed. I trust she knows that Siemens has said within the past couple of hours—I am sure it has been in touch with the Department before putting this out publicly—that it is freezing its plans for the existing blueprint to export offshore wind turbine machinery from the Hull hub. That is now in

[Barry Gardiner]

the public domain, and it seems to go against the reassurances that the Minister gave in her introduction. Brexit has changed the way in which investors in the market look at the UK as a destination for energy investment. Although the Minister rightly tried to reassure investors that the Government want investment to continue, the fact is that investors take a very different view of this.

3.13 pm

Callum McCaig: It is a pleasure to serve under your chairmanship, Ms Dorries. The changes are relatively uncontentious, but I would like some clarity on the issues and the broader horizon for contracts for difference, which the Minister touched on in her opening remarks. Before I do that, I want to add to the comments about the hon. Member for Southampton, Test, who, in the year I have been here, has been an absolute titan on energy policy. I will miss his enlightening contributions and his approach to cross-party working. I have already spoken to Labour's new Front-Bench spokesperson, and I hope that will continue.

I thank the Minister for responding to my intervention about double bidding, but I ask that she explain a little further why she sees that to be such a problem. I accept to a degree that it may provide the Department with clarity, but there is a limited pot to be applied for, both for the capacity market and for CfDs. Allowing businesses a greater opportunity to bid for those pots of money would perhaps add to the sense of keeping the capital costs lower, which the Minister talked about at the start. I am not in a position to oppose this, but I request a little more clarity. As and when this is implemented, it would be welcome if there was ongoing monitoring of that aspect to ensure that it is not freezing people out unnecessarily because of the cost of bringing projects to markets.

I would also ask the Minister what she sees as the obstacles or impediments to companies or projects bidding too low. How will she ensure the deliverability of projects in the forthcoming CfD budget rounds? The process is welcome and has delivered considerable savings over the previous funding mechanisms, but there is a genuine risk that companies will bid too low in order to win, and then deliverability might fail and we will not see things coming forward at all, which is not in anyone's interest. Does she think that the existing penalties are effective? It is not clear to me that missing out a subsequent round is necessarily the greatest impediment.

We talked about the Government's efforts to provide the clearest long-term strategy for the investment framework in low-carbon technologies. What progress are the Government making on publishing their response to the fifth carbon budget?

3.17 pm

Andrea Leadsom: I am grateful to the hon. Member for Brent North for his comments and I share his tribute to the hon. Member for Southampton, Test. It was a great pleasure to spar with him in Committee over the last year, and his knowledge of the energy sector has been a huge plus in our debates. I shall certainly miss him and I sincerely hope that his grape

vines will do very well this summer. That is a bit of an in issue, but I was very interested to learn that he was a grape pruner.

The hon. Member for Brent North asked whether there has been an attempt to bid for a capacity market auction and a CfD. The answer is that it has not happened yet. The 2014 allocation rules already prevent an application for a CfD where an applicant has secured support under the capacity market scheme. That prevents an application for a CfD where an applicant has a pending application to the capacity market scheme. Obviously, any project that does not secure support in either a CfD or a capacity market scheme can participate in future rounds for either scheme. I hope that clarifies that point.

To clarify further, the CfD scheme is designed to bring forward low carbon generation, specifically to meet our decarbonisation targets. On the other hand, the capacity market scheme is designed to bring forward dispatchable electricity, to give the confidence for energy security. They therefore have different aims, but we are trying to make sure that no one project can benefit from both or, indeed, cherry pick between the two. Of course, CfDs will be allocated via a competitive process, to make sure that there is best value for money for consumers. These regulations are minor and technical in nature. They are designed to make the competition more efficient, not to change the criteria by which a CfD is awarded.

The hon. Gentleman for Aberdeen South asks whether projects could be encouraged to bid too low. Obviously, this is a competitive auction: we want to see bids come in as competitively as possible. We believe there is room for costs to come down as deployment increases and the supply chain is better developed. If projects fail to sign contracts after bidding, or if they fail to deliver against key milestones, they are prevented from bidding in future rounds, so there is a penalty for not being realistic and deliberately underbidding. There is also evaluation of the non-price parts of a bid to make sure that it is realistic. We have absolutely considered that and taken steps.

Callum McCaig: I appreciate the Minister's response. Yesterday in this room, we discussed changes to penalties in the capacity market. Will she keep this measure under review? Sensible changes were made yesterday and, as we come forward with further CfD rounds, that is potentially something worth looking at.

Andrea Leadsom: Yes. I am grateful to the hon. Gentleman and that will absolutely be the case.

National Grid, as the delivery body, monitors both the capacity market and the CfD schemes and is very alert to issues of gaming or underbidding and so on. We are focused on looking for best value for consumers as we bring forward both our decarbonisation and our energy security strategies.

The hon. Member for Brent North asked why the impact assessment has not been updated. The impact assessment for the original order was approved and published in 2014 and these minor and technical amendments are not enough to alter the balance of costs and benefits discussed in that assessment, which is why a further one has not been produced.

Finally, the fifth carbon budget is a top priority. As I have made very clear, nothing has changed following the referendum decision to leave the EU. Our commitment to meeting our UK Climate Change Act 2008 decarbonisation goals is as strong as ever. I disagree with the hon. Member for Brent North about the impact on investment. It is true that Siemens has said it is waiting to see what Government policy is, but it is also true that it is going ahead with its turbine plant in Hull. It behoves all of us, as MPs, not to try to create uncertainty—we should be determined to avoid that. I welcome DONG Energy's commitment and its important

announcement today of continued investment in UK offshore wind, which is fantastic. We will make announcements on the fifth carbon budget as soon as possible.

Question put and agreed to.

Resolved,

That the Committee has considered the draft Contracts for Difference (Miscellaneous Amendments) Regulations 2016.

3.22 pm

Committee rose.

