

# PARLIAMENTARY DEBATES

HOUSE OF COMMONS  
OFFICIAL REPORT

Second Delegated Legislation Committee

DRAFT ELECTRICITY SUPPLIER PAYMENTS  
(AMENDMENT) REGULATIONS 2018

*Monday 19 March 2018*

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**The Committee consisted of the following Members:**

*Chair:* IAN PAISLEY

- |  |   |
|--|---|
| † Afolami, Bim ( <i>Hitchin and Harpenden</i> ) (Con)                    | Mahmood, Shabana ( <i>Birmingham, Ladywood</i> ) (Lab)          |
| † Brown, Alan ( <i>Kilmarnock and Loudoun</i> ) (SNP)                    | † Perry, Claire ( <i>Minister for Energy and Clean Growth</i> ) |
| Bryant, Chris ( <i>Rhondda</i> ) (Lab)                                   | † Robinson, Mary ( <i>Cheadle</i> ) (Con)                       |
| † Charalambous, Bambos ( <i>Enfield, Southgate</i> ) (Lab)               | † Skidmore, Chris ( <i>Kingswood</i> ) (Con)                    |
| † Cleverly, James ( <i>Braintree</i> ) (Con)                             | † Smith, Nick ( <i>Blaenau Gwent</i> ) (Lab)                    |
| † Graham, Richard ( <i>Gloucester</i> ) (Con)                            | † Whitehead, Dr Alan ( <i>Southampton, Test</i> ) (Lab)         |
| † Harris, Rebecca ( <i>Lord Commissioner of Her Majesty's Treasury</i> ) | † Wragg, Mr William ( <i>Hazel Grove</i> ) (Con)                |
| † Johnson, Diana ( <i>Kingston upon Hull North</i> ) (Lab)               | Lauren Boyer, Nina Foster, <i>Committee Clerks</i>              |
| † Kendall, Liz ( <i>Leicester West</i> ) (Lab)                           |   |
| † Lord, Mr Jonathan ( <i>Woking</i> ) (Con)                              | † <b>attended the Committee</b>                                 |

## Second Delegated Legislation Committee

Monday 19 March 2018

[IAN PAISLEY *in the Chair*]

### Draft Electricity Supplier Payments (Amendment) Regulations 2018

6 pm

**The Minister for Energy and Clean Growth (Claire Perry):** I beg to move,

That the Committee has considered the draft Electricity Supplier Payments (Amendment) Regulations 2018.

It is a pleasure to serve under your chairmanship for the first time, Mr Paisley. The draft regulations will amend existing regulations to secure sufficient funding for the Low Carbon Contracts Company and the Electricity Settlements Company to enable the continued smooth operation of the capacity market and the contracts for difference scheme over the next three years. They are based on the consultation that we held in November, the responses to which broadly supported our proposals but asked for levies to be set on a three-year basis.

The LCCC has demonstrated its value through excellent management of CfDs and ongoing operational efficiencies; indeed, its costs per contract over the period are projected to fall significantly, by approximately 30%. The ESC is now managing increased market complexity and a number of participants in the capacity market. We propose that its funding be increased so that it can continue to provide a robust and effective settlement service.

The CfD and capacity market schemes were designed to incentivise the significant investment required in our energy infrastructure, to keep costs affordable for consumers, to drive down the costs of low-carbon technologies and to keep our energy supplies secure. I believe that the schemes are doing all those things. They provide long-term price stabilisation to low-carbon generators, allowing investment to come forward at a lower cost to capital, which in turn reduces costs for consumers. The capacity market is our main policy for maintaining a healthy surplus of electricity capacity at an acceptable cost. Regular payments are made to generators and demand-side response providers in return for making capacity available when needed.

In both schemes, participants bid for support via a competitive auction process, which ensures that costs to consumers are minimised. The success of the policy was demonstrated by the 2017 auction, in which the clearing price of offshore wind was half what it was in the first auction only two years before. The 2017 auction secured 3.3 GW of renewable electricity—enough to power an estimated 3.6 million homes.

Following four successful four-year-ahead auctions, the capacity market is already securing the capacity we need until 2021-22 at a low price. The main auctions have all cleared at between £8.40 and £22.50 per kW per year, which is well below industry estimates and supports our view that the process is highly competitive and delivers value for consumers.

A number of partners work with the Government to make the capacity market and CfDs a success. The LCCC and the ESC are operationally independent GovCos that play an important role in both schemes. The LCCC was established as the counterparty for CfDs; its primary role is to manage CfDs with generators through their lifetimes, managing contracts as well as collecting and making CfD payments. The ESC was established as the capacity market settlement body to oversee all financial transactions that relate to the market, including by making regular payments to capacity providers that have agreed to provide capacity at times of system stress.

The draft regulations will revise the levies on electricity suppliers, which fund the operational costs of the LCCC and the ESC. Historically, the levies have been set annually, but the regulations will set them for each of the three financial years from 2018-19 to 2020-21, as proposed in the consultation responses, to enable both companies to recover their expected operational costs over that period.

The draft regulations will also make a minor amendment to correct an unfortunate grammatical error—something that very rarely happens—in the Electricity Capacity (Supplier Payment etc.) Regulations 2014. *[Interruption.]* I see that the hon. Member for Southampton, Test wants to know exactly what the error was; perhaps my officials will make a note so that I can answer him.

Given the critical role of the LCCC and the ESC, it is essential that they are funded sufficiently to perform effectively. However, we are focused on delivering low-cost energy to consumers, so we want to ensure that costs are minimised. The budget-setting process aims to strike the right balance. We do of course scrutinise their cost budgets to ensure that they accurately reflect the operational requirements, and they are benchmarked against other similar operations. The budgets were also subject to external scrutiny through consultation, to which there were three responses. As well as consulting on the budgets, as I mentioned, we asked stakeholders for their views on setting the three-year budgets, and it was agreed that it was a sensible approach. Of course, it saves parliamentary time—we do not have to come back and test the patience of Committee Chairs on an annual basis.

I want to mention something important, which is the value-for-money improvements that are being delivered. The operational budgets have been set out to reflect the expected activity required to manage the CfD scheme and the capacity market. The LCCC's budget will be £16.5 million in 2018-19, increasing by about £500,000 per year for the subsequent two years. The ESC's budget will be £7.6 million in 2018-19 and will decrease slightly to £7.5 million in 2020-21. The core operating costs for the LCCC are slightly down year on year, but the increase in total costs reflects the inclusion of contingency provision for managing potential contract disputes. We have assumed that additional contracts will be awarded in future allocation rounds, but the budget assumption is that the cost of management per CfD contract is projected to come down a healthy 30% over the contract period.

The ESC is managing a significant increase in the amount of capacity and the number and type of capacity providers covered by the scheme, and there will also be ongoing requirements to refine the operation of the capacity market and deliver more successful auctions.

The company has submitted that it requires investment to manage that activity, and to ensure that it continues all financial transactions for the capacity market effectively. The budget changes reflect those requirements.

The regulations revise the levies currently in place to reflect the expected operational cost requirements over the next three years. Subject to the will of the Committee, the levy to fund the ESC's operational costs is due to come into force on the day after the regulations are made. The operational costs levy for the LCCC will be operational from 1 April. The only other change to the regulations that are being amended is that the words "is responsible" were removed because they were considered superfluous.

6.7 pm

**Dr Alan Whitehead** (Southampton, Test) (Lab): It is a pleasure to serve under your chairmanship, Mr Paisley.

The regulations, as the Minister set out in some detail, are about providing for the operational costs of the counterparty body, as far as contracts for difference are concerned, and the Electricity Settlements Company, as far as the capacity market is concerned. They are not concerned with the success of the market or of CfDs, but with the operational costs of the bodies that essentially stand between the people who are supposed to put money into the system, and the people who are supposed to take money out of it. That, at its heart, is the arrangement as to what those two bodies do.

It is worth spending a moment looking at what the operational costs are. The Minister spent a little while stating that they are good value for money and that they are a good representation of what the LCCC and ESC do. It is not easy to find out the total cost of LCCC operational activities, because the amounts presented for 2018 to 2020 are expressed per MWh for any day during that period; they do not represent the total operational cost of the body's activities.

**Claire Perry:** I would be happy to share information about the gross cost; I apologise if it has not been made clear, but I will write to the hon. Gentleman—indeed, I may be able to share it with him during this debate. It may reassure him to know that the average cost per household bill of the total budget for these bodies is estimated at 30p per year in 2016 prices, but I am happy to share the gross numbers with him or any other member of the Committee.

**Dr Whitehead:** I thank the Minister very much for that intervention, which to some extent anticipates what I was going to say. It appears that the cost per MWh has remained reasonably stable for the LCCC since the original regulations were made, but it would be helpful to know the total cost over the period as far as CfDs are concerned. The 30p that the Minister mentions, which I assume represents the total cost of both arrangements to the consumer, is not an enormous amount, but it is not insignificant either. I am therefore slightly surprised that the explanatory note states:

"A full-impact assessment has not been produced for this instrument as no, or no significant, impact on the private, voluntary or public sectors is foreseen."

Frankly, the impact on customer bills is not insignificant, so I would have hoped for some assessment of it, particularly in comparison with the impact of other measures on bills. I appreciate that it may be a relatively

small amount compared with the consequences of other levies on bills, but it is not insignificant. I think it ought to be looked at in that light.

The Electricity Capacity (Supplier Payment etc.) Regulations 2014, which are the original regulations relating to the operational costs of the ESC, give a rather different picture from that of the costs relating to the LCCC. The 2014 regulations specify a total operational cost of £1,374,000, which was subject to annual amendment, as the Minister says. By 2016, the figure had risen to £4,283,000, and by 2017 it stood at £6,241,000, which is the figure that the draft regulations seek to amend. Article 3(1) states:

"in regulation 9(2), for "£6,241,000" substitute"

£7.6 million, £7.5 million and £7.5 million for the years 2018 to 2020. The figure of £6,241,000 comes from the most recent iteration—the Electricity Supplier Payments (Amendment) Regulations 2017—not the original 2014 regulations. It is difficult to tease that out in this statutory instrument, but that appears to be what has happened.

Frankly, we are faced with an inflation of costs from £1,374,000 in 2015 to £6,241,000 in 2017, and then a further increase to £7,629,000 in 2018. That series of costs does not strike me as carefully under control and good value for money. It may be, if the ESC's work has expanded sevenfold since it was originally given the task of carrying out the administration of capacity markets under the 2014 regulations—other things may also have taken place to increase some of those costs—but I am not entirely convinced that the ESC's activities have increased over the period by a factor of 700%, justifying those increases in operational costs.

Can the Minister give a satisfactory explanation of why those costs have inflated so much over that period? There may be a good explanation, but perhaps we are not paying sufficient attention to the considerations that go into the operational costs of these organisations. I do not know whether there is a body to oversee how those costs are brought about and what they relate to. On the face of it, they appear to have inflated considerably over the period in which the ESC has been in post, as it were, overseeing the activities of the capacity market and their results.

I do not want to divide the Committee. Clearly, these organisations need to have a period to set out what their organisational costs will be and what the supplier companies will contribute to those costs. However, this afternoon, or by subsequent communication, I would like to hear whether the Minister shares my view about the apparent enormous inflation of the operational costs, as set out by the preceding statutory instruments. In her view, is that enormous cost inflation justified by the sort of activities she has set out?

The Minister will not necessarily have a complete and instantaneous response to all my points. It would be wonderful if she did, but I do not blame her at all if she does not. It is a fairly arcane point, but it is important to raise it as we look at the operational costs of the bodies in this statutory instrument.

6.19 pm

**Alan Brown** (Kilmarnock and Loudoun) (SNP): It is a pleasure to serve under your chairmanship, Mr Paisley

I was on a Public Bill Committee last week where I made a joke about being a man of few words, and I will not say too much tonight. We are interested to hear the

[Alan Brown]

Minister's response on the operational costs. It makes a change to hear the Labour Opposition lecturing a Tory Minister about cost controls. We will see where that goes. The point raised is important: in the big scheme of things, if the impact on people's bills is 0.1%, as reported, I am certainly supportive of the draft measure getting through.

The Minister reminded us in her opening remarks of how costs for offshore wind have come down to £57.50 per MWh. If we really want to minimise the impact on people's bills in the future, onshore wind operations need access to future contracts for difference auctions as well.

**The Chair:** Everybody else seems to be able to contain themselves and to not wish to speak, so I call the Minister.

6.21 pm

**Claire Perry:** I like to please, so I have responses to the questions. It is an outbreak of great consensus in that we are all focused on keeping down costs for consumers and bill payers.

The hon. Member for Kilmarnock and Loudoun is always consistent. My reply to him is that I agree, and that we need to work on a way, within the current CfD auction structures, that ensures that our manifesto commitments are not breached but that we bring on onshore wind where we know we have strong support from local communities.

I will address some of the points from the hon. Member for Southampton, Test. He rightly raised the issue of whether we could see the aggregate numbers. I am told that, buried in the draft explanatory memorandum,

at paragraph 8.6, there are the aggregate numbers—he may not have had chance to look at them—and they were, indeed, put out with the original consultation.

The hon. Gentleman raised an important question about impact assessments. An assessment was done when the electricity market reform proposals were made. The cost will amount to less than 0.03% of consumer bills, which is a relatively small amount. Nevertheless, we know that pennies do add up into pounds.

The hon. Gentleman also raised a series of important questions about the rapid ramp up in costs. Those are the right questions to ask, but to reassure him, let us take, in particular, the ESC. It was set up in 2014. It has gone through its set-up period, and we can now see a steady-state operational position. We have seen a phenomenal increase in what we are actually asking the company to do. In 2016-17, we asked it to, essentially, look at 0.6 GW of capacity. That will increase to 55 GW during the course of this year, with the number of providers going up from 46 to 447, which is a great testament to the capacity market delivering what we want: better competition driving down prices.

To reassure the hon. Gentleman, if he looks at the operational costs as part of the whole scheme, he will see they are dropping from 1.6% last year to 0.6% in 2020, so we are actually delivering more value in a wider scheme. He is absolutely right, and he knows that I am always keen to run the calculator over these companies' calculations. As the Minister ultimately responsible, I will continue to do so. I thank both hon. Gentlemen for their valuable contributions, and I commend the draft regulations to the Committee.

*Question put and agreed to.*

6.23 pm

*Committee rose.*