



Department
of Energy &
Climate Change

Nuclear and CCS CfD allocation Stakeholder Workshop

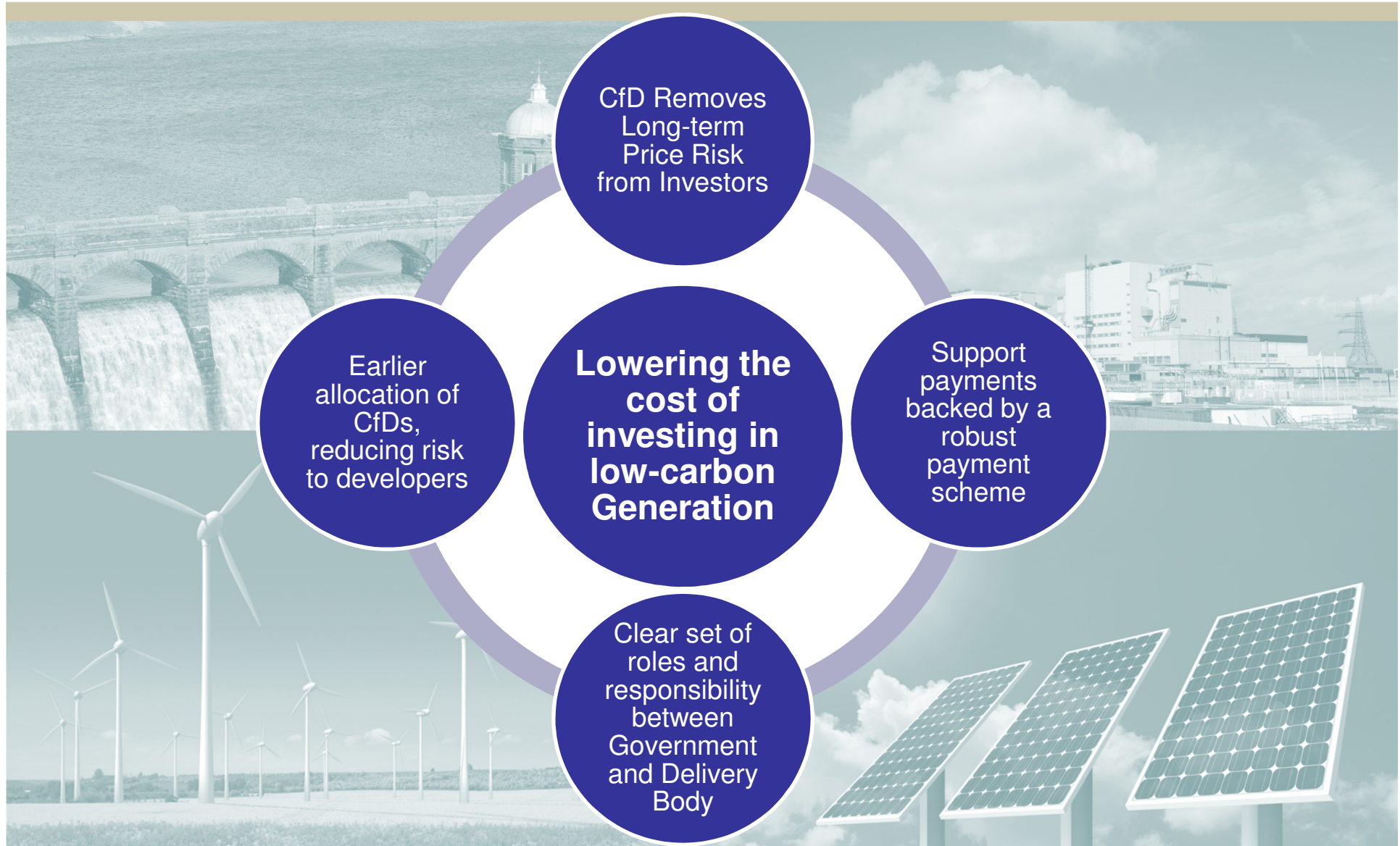
9 October 2013



0930-0945	Arrival
0945-1000	Introduction
1000-1100	High level models for competitive allocation
1100-1115	Break
1115-1215	Further design details
1215-1230	Wrap-up / next steps

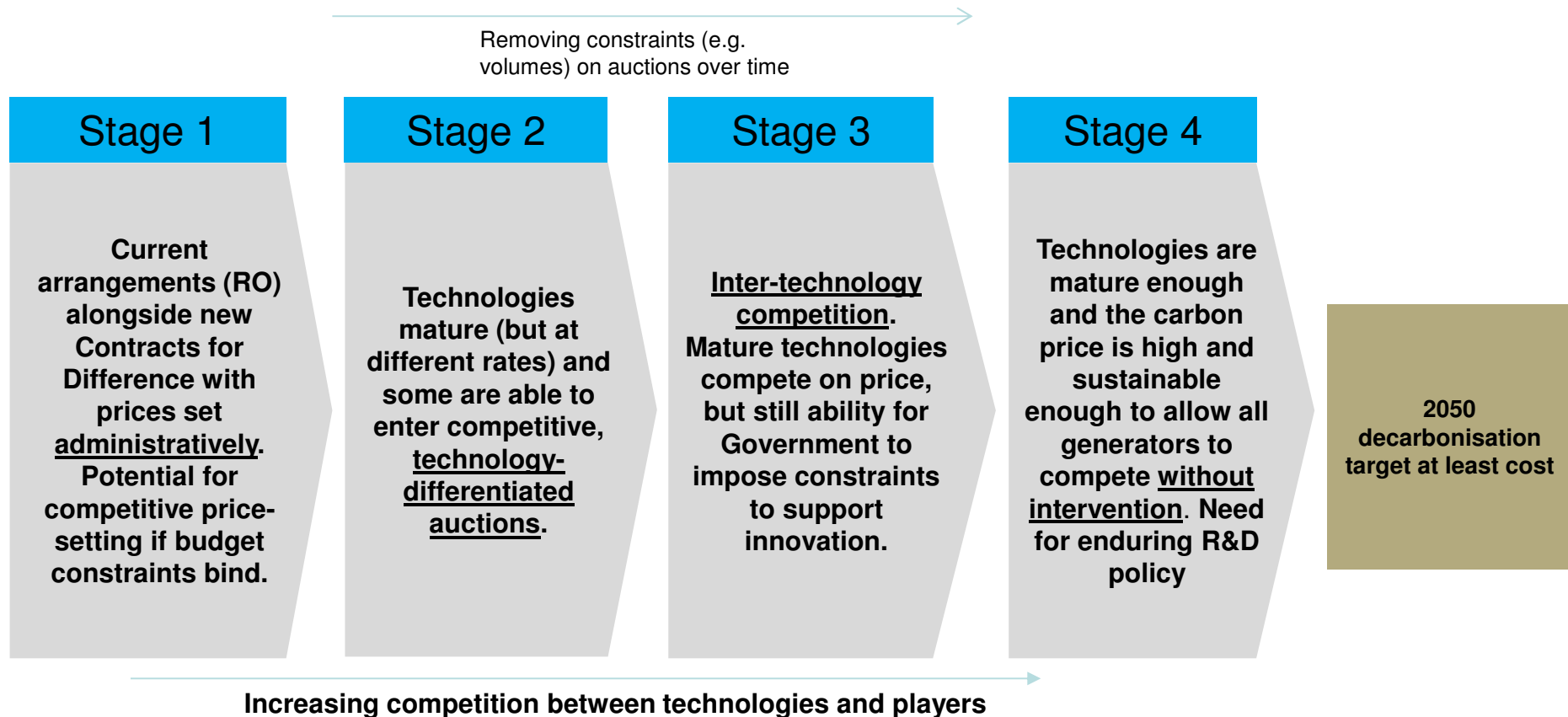


The allocation process is a key part of how the CfD drives low-cost decarbonisation





SoS has spoken about “blazing a trail” to competition



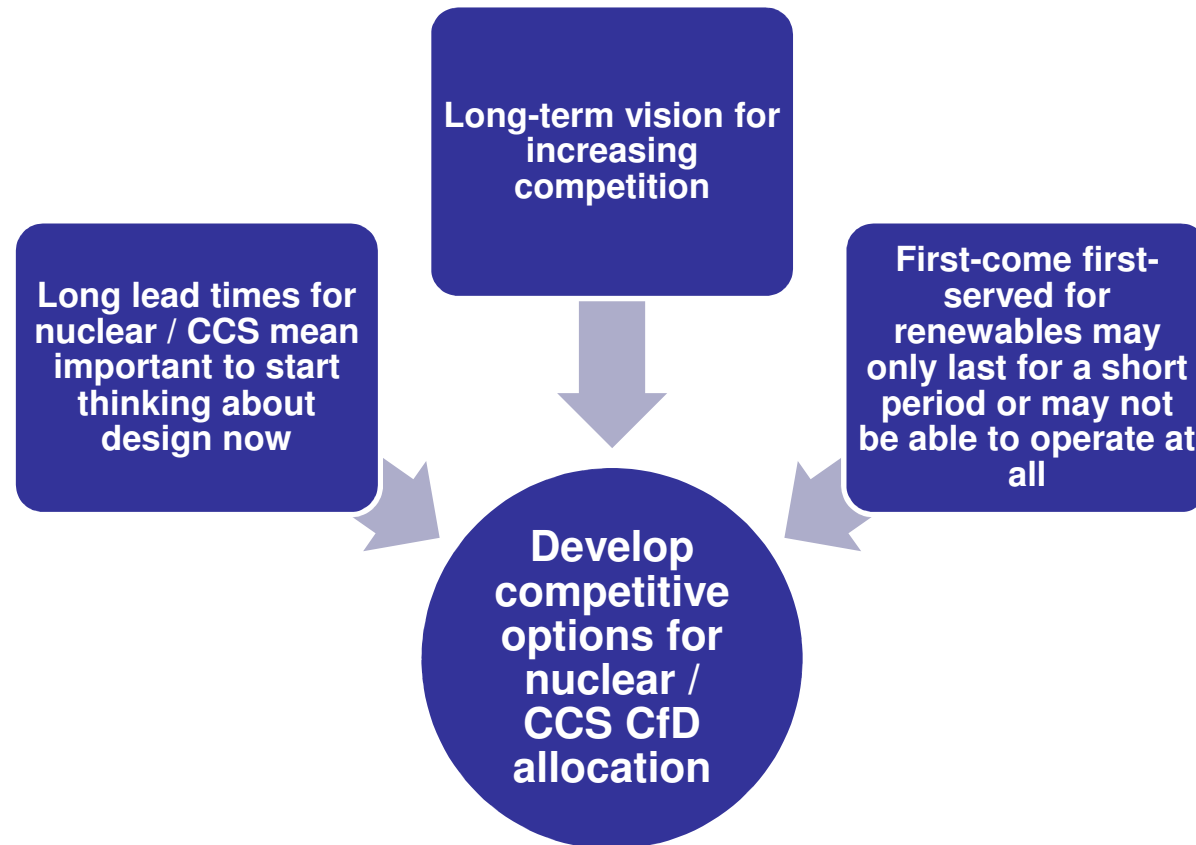
Our focus on competitive allocation for nuclear and CCS is line with this vision



- August 2013 CfD overview document:
 - “...Government’s intention is that future CfD allocation for nuclear and CCS projects takes place through competitive project selection processes, wherever practical and effective... Bilateral negotiation remains an alternative for nuclear and CCS CfD allocation where competitive processes are not practical. In such circumstances, any final allocation decision would still be subject to strict value for money considerations and an assessment of overall budget constraints.”
- Today’s objective is to stimulate discussion and gather views on:
 - High-level conditions required for competitive CfD allocation
 - Competitive allocation models and what’s needed to make them work, including key areas of interaction between allocation and contract terms
- Note: not considering today:
 - contract design features that apply during operational phase (e.g. fuel price indexation, reference price)
 - Wider decisions on the technology mix or LCF spend



Several drivers for thinking now about how competitive allocation might work for nuclear / CCS





Range of possible mechanisms to allocate CfDs, which have all been used before in some context

More competitive processes

.....→

	Bilateral negotiation	Admin. price-setting (FCFS)	Tender	Auction
<i>More competitive tension (between techs)</i>	Tech-specific	e.g. current HPC process; MoD procurement	e.g. RO banding exercise; small-scale FiTs	e.g. CCS competition; UAE nuclear; or highways agency procurement
	Multi-technology / criteria		e.g. CCS competition; rail franchises; or NDA Sellafeld	e.g. Bank of England liquidity auctions
	Tech-neutral			e.g. Capacity Market

.....↓

Generic schemes can support investment in a range of low-carbon generation



- Renewables Obligation: open to a wide range of technologies (wind, biomass, solar, hydro, etc)
- Has successfully supported a broad range of projects
 - 3,377 sites accredited under the RO (as of 5 September)
 - Has included smaller projects, such as Delabole Wind Farm (Cornwall, 4MW, repowered to 9MW – first wind farm in UK)
 - Also supported investment in the largest offshore windfarms in the world – London Array (630MW) and Greater Gabbard (500MW)
- Generic CfDs (i.e. applying to most renewables) will offer certain flexibilities/variations within a largely standardised contract:
 - Commissioning Date
 - Proof of Financial Close
 - Capacity Adjustment
 - Different Corporate forms
 - Delivering across multiple years (phasing)



MODELS FOR COMPETITIVE ALLOCATION



Policy design can facilitate competitive processes

- Competitive tension requires:
 - the development capacity of the potential participants to exceed the volume of new development sought;
 - enough (potential) participants;
 - new entrants to not be systematically disadvantaged relative to incumbents, and being discouraged from participating in future allocation rounds (which would lower competitive pressure)

“Lumpiness”

- Less frequent rounds / grouping together projects commissioning over a wider time horizon?

High barriers to entry

- Allow application earlier in the project life cycle?

Limited number of
players

- Indirect competitive tension between low-carbon technologies through LCF management?



We consider two high-level models for competitive allocation

Auction

- More similar to generic CfD “rationing” process
- Lowest-price bids accepted (subject to being under reserve price and meeting demand / affordability constraint)
- Projects must be comparable on price
- Limited risk-sharing in the construction phase

Tender

- Describes a range of models, with the potential for:
 - More emphasis on negotiations with (short-listed) projects to set prices
 - Including evaluation criteria other than price
 - More risk sharing in the construction phase
 - Some degree of negotiation on contract terms

Some features likely to be common to both models (and we consider these separately):

- Periodic (technology-specific) allocation rounds for CCS and nuclear
- Could be similar set-up in terms of eligibility criteria, incentives for timely delivery of projects, etc.



Intended outcomes	Summary of position for generic CfDs
<p>Ensuring the projects selected are those that best contribute to meeting Government's objective for least-cost decarbonisation over the long-term</p> <p>Efficient allocation of risks between consumers and generators</p>	<p>Constrained allocation mechanism: projects selected on the basis of lowest Strike Price via an auction process. No negotiation on price</p> <p>Strike Price the only evaluation criterion.</p> <p>Strike Price largely fixed from the point of allocation (apart from inflation indexation, change-in-law adjustments, or adjustments due to amendments to level of capacity delivered).</p> <p>No negotiation on contract terms during the allocation process; contract terms largely standardised across technologies</p>



Questions

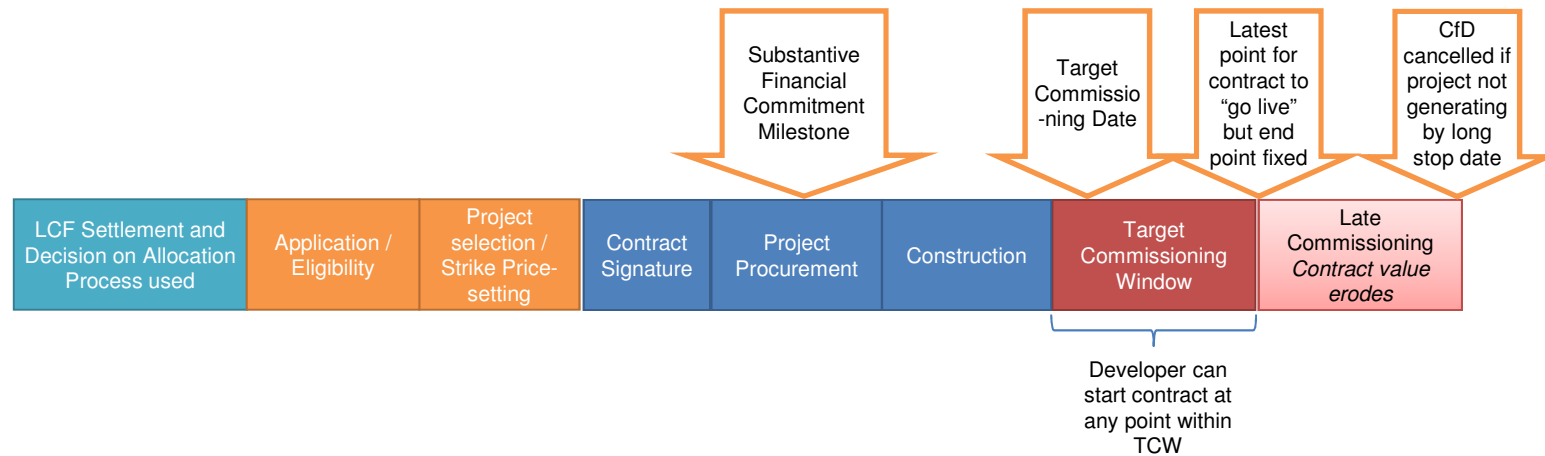
1. Are there barriers (specific to nuclear and CCS) to further improvements in underlying competitive conditions?
2. If so, what steps can industry and Government take to resolve these barriers?
3. Are tenders and auctions the right high-level options to be considering?
4. Does the structure of evaluation and price-setting under the generic process work for nuclear and CCS?
5. Would competitive tendering on price work for nuclear and CCS?
6. Are there criteria other than price that are important in selecting nuclear and CCS projects? If so, which? Can these be valued objectively in advance of the allocation round?
7. Does the position under the generic process on adjustments to the Strike Price reflect an efficient balance of risks, given the specifics of nuclear and CCS projects?
8. Can contract terms for nuclear or CCS projects be largely fixed ahead of launching the allocation process?



FURTHER DESIGN DETAILS



Framework for “generic” CfD allocation is a useful basis for exploring the detailed design



But need to consider whether changes might be needed to reflect considerations, in particular on:

- Eligibility
- Milestones
- TCWs and LSDs
- Flexibilities to adjust capacity



Eligibility, Milestones, TCWs/LSDs all interact to ensure project delivery

- Key principles:
 - Provide developers with certainty of CfD award at earlier stage
 - Ensure that applicants are those with a strong chance of progressing to commissioning and that the available budget is absorbed by highly speculative projects
 - Once the CfD is allocated, provide the CfD counterparty with a means to assess whether a developer is committed to developing its project



Summary of generic CfD position

Eligibility	Milestones	TCWs/LSDs
<ul style="list-style-type: none"> • Planning Permission or Development Consent secured • Grid Connection Offer has been accepted • Evidence that applicant is validly incorporated • Evidence that the project has a valid supply chain plan 	<ul style="list-style-type: none"> • Generator has to provide ‘Evidence of Substantive Financial Commitment’, or face termination • One year after CfD contract signature for all technologies • E.g. Major construction contracts signed, environmental permits received, FID secured 	<ul style="list-style-type: none"> • Generator flexibility to deliver within a nominated ‘target commissioning window’ (e.g. 1 year for onshore/offshore wind) • Payments for generation output commence once specified standards are met relating to connection, metering, capacity instalment (e.g. 70% of original installed capacity estimate), and contract payment/collateral requirements. • The Longstop Date will be a point beyond the end of the Target Commissioning Window after which a project that has failed to meet the contractual Further Conditions Precedent will face having its CfD terminated • Satisfaction of conditions precedent following end of the Target Commissioning Window leads to a reduction in the contract’s payment term. • Failure to satisfy by the long stop date (e.g. 2 years after the end of the TCW for offshore wind) could lead to termination



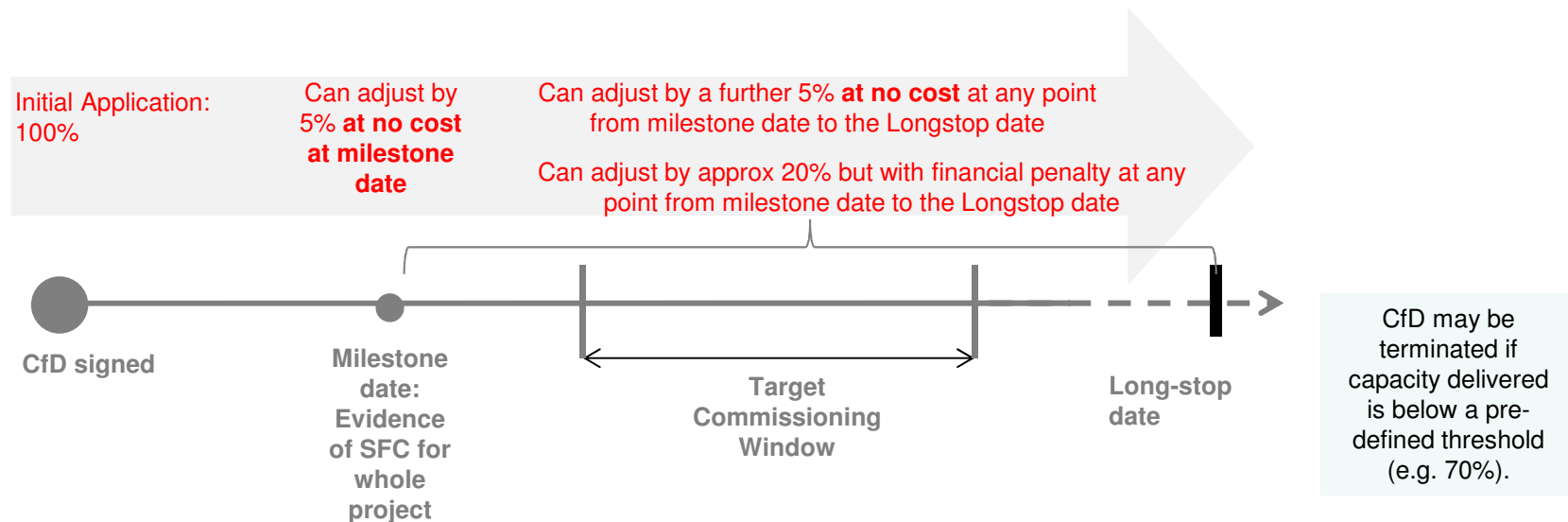
Questions

1. Does the broad structure of the generic system to ensure project delivery work for nuclear and CCS?
2. How does DECC ensure that only applicants with a strong chance of progressing to commissioning are allocated a CfD?
3. How does DECC/CfD Counterparty ensure developers make progress towards getting the necessary approvals (and eventually commission)?
4. Would the proposed eligibility criteria work for nuclear or CCS? What additional eligibility checks might be needed?
5. What might demonstrate suitable evidence of financial commitment for nuclear and CCS projects?
6. What variations to the parameters (e.g. length of target commissioning windows) might be needed for nuclear/CCS?



Capacity Adjustment

Generic CfD capacity adjustment provisions should provide the right amount of flexibility at the right point(s), without offering protection against incompetent project management



Questions



1. Is the structure appropriate for nuclear / CCS?
 - Free adjustment at the Substantive Financial Commitment milestone?
 - Further free adjustment of capacity within specified parameters anytime from Substantive Financial Commitment milestone to the Longstop Date?
 - The ability to adjust down to the Condition Precedent at a cost, then Termination?
2. Are the flexibilities suggested adequate for nuclear / CCS?
3. Would more flexibility at the milestone date reduce the need for further flexibilities?
4. If a project has already exercised its ability to adjust its capacity is it appropriate to have a termination event at the Longstop Date if the adjusted level of capacity has not been achieved?
5. Would the charge for the non-free adjustment need to be increased if the scope for free adjustment is increased?



NEXT STEPS

Next Steps

We will now seek more detailed written feedback



Department
of Energy &
Climate Change

- We are now looking for more detailed views – supported by evidence by possible, on all the questions included in the slides
- These views, in conjunction with any wider decisions (e.g. on use of the LCF), will inform our views on preferred options and the level of required work going forward
- Written feedback requested by 31 October
- We will publish an updated position alongside, or shortly after, the final Delivery Plan in December