



12/02/2014

Dear Colleague,

### **Update on Contract for Difference Allocation**

The August 2013 Allocation Methodology summarised how auctions for CfDs (“constrained allocation”) would operate if required<sup>1</sup> with further detail set out in the October 2013 Consultation on EMR Proposals for implementation<sup>2</sup>. In addition, there has been on-going engagement with a range of stakeholders on these issues, including through workshops and the CfD Expert Group, which have explored a range of design choices, including the choice between sealed-bid and descending clock, and between cleared-price and pay-as-bid approaches.

We recognise that the process of allocation is of particular interest to stakeholders. We are also mindful of the need to focus on-going engagement onto the detailed design of a single option, not least to facilitate the effective procurement and design of systems to implement the allocation process to allow the award of CfDs at the earliest opportunity.

Having considered the responses to the August publication, October Consultation and the discussions with stakeholders, the Secretary of State has asked us to develop a CfD allocation approach based on a sealed-bid model.

Reflecting this, DECC and the Delivery Body will now develop the auction design based on a sealed-bid format, engaging with stakeholders further on the detailed design of this sealed-bid approach.

Some stakeholders were particularly concerned about the use of bid information under a sealed-bid approach and, in particular, that concerns about confidentiality would distort bidding behaviour and reduce the effectiveness of the allocation. In response, we are taking forward the auction design on the basis that the Delivery Body will be required, by provision in the Allocation Regulations, to treat sealed-bids confidentially (albeit that the independent auditor will require access, subject to appropriate confidentiality clauses).

Stakeholders also sought greater clarity about the treatment of offshore wind projects in any constrained allocation. In this respect, we can confirm that phased offshore wind projects will be treated as a single indivisible project from the point of view of the rationing process, and

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<sup>1</sup>Page 19 [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/226976/Allocation\\_Methodology\\_-\\_MASTER\\_-\\_6\\_Aug\\_v\\_FINAL.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/226976/Allocation_Methodology_-_MASTER_-_6_Aug_v_FINAL.pdf)

receive a single Strike Price across all phases. This is consistent with previously announced policy intent on phased projects<sup>3</sup>.

## Next Steps

Government intends to publish further information on the detail of the auction process in spring 2014. The Allocation Framework will be published in advance of the first allocation round, building upon the spring update. We will be discussing auction design features with stakeholders as part of the development of the Allocation Framework. For example we expect to engage on:

- **The auction payment rule.** We continue to explore the case for a pay-as-clear or pay-as-bid system.
- **Whether to offer bidders flexibility on some bid parameters and how any flexibility might be implemented.** We will investigate whether it is possible and desirable to allow bidders to specify a range of different capacities for their projects and/or different potential delivery years.
- **Tiebreaker rules.** How to choose between two or more projects that propose the same strike price, were they to be the last affordable projects in the auction.
- **Ensuring successful bidders do not decide to reject the offer of a CfD.** We are exploring ways to mitigate gaming and speculative bidding in the auction, such as measures to discourage the refusal of an offer of a CfD, and to discourage projects from participating when they do not have a reasonable prospect of meeting the Significant Financial Commitment milestone. These measures will help to mitigate against the risk of “bed-blocking” and gaming of auctions.

We will be engaging further with the CfD Expert Group and other stakeholders on the above design features. You can find further updates and information on our website <https://www.gov.uk/government/policies/maintaining-uk-energy-security--2/supporting-pages/electricity-market-reform>.

Kind regards,



Chris Hemsley  
Deputy Director, CfD Design & Implementation

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<sup>3</sup> Page 10, “Investing in renewable technologies – CfD contract terms and strike prices”, December 2013 (“[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/263937/Final\\_Document\\_-\\_Investing\\_in\\_renewable\\_technologies\\_-\\_CfD\\_contract\\_terms\\_and\\_strike\\_prices\\_UPDATED\\_6\\_DEC.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/263937/Final_Document_-_Investing_in_renewable_technologies_-_CfD_contract_terms_and_strike_prices_UPDATED_6_DEC.pdf)”).