

## SUBMISSION FROM COMPETITION AND MARKETS AUTHORITY

I am writing to you in follow up to our hearing with the Economy, Energy and Tourism Committee on 2 September 2015.

In the hearing we undertook to share with you the potential remedy in our Notice of possible remedies (the Remedies Notice) relating to the administration of Contracts for Difference (CfDs). Potential remedies relating to CfDs are set out in paragraphs 21 to 30 of the Remedies Notice, which are attached at Annex A. You will see that Members are considering two potential remedies:

- Remedy 2a - DECC to undertake and consult on a clear and thorough impact assessment before awarding any CfD outside the CfD auction mechanism
- Remedy 2b - DECC to undertake and consult on a clear and thorough assessment before allocating technologies between pots and the CfD budget to the different pots

Full versions of the Remedies Notice and Provisional Findings document, which provides a more detailed analysis of CfDs, are available here:

[https://assets.digital.cabinetoffice.gov.uk/media/559fc933ed915d1592000050/EMI\\_provisional\\_findings\\_report.pdf](https://assets.digital.cabinetoffice.gov.uk/media/559fc933ed915d1592000050/EMI_provisional_findings_report.pdf)

[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/442489/EMI\\_Remedies\\_Notice\\_-\\_Final.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/442489/EMI_Remedies_Notice_-_Final.pdf)

A specific question was asked in the hearing regarding Dynamic Teleswitched (DTS) meters. We confirm that we would be happy to receive any evidence on this topic. Indeed, in the Remedies Notice (paragraph 59b), we seek views on two related questions relating to DTS meters: "Will the roll-out of smart meters address the barriers to switching faced by customers with Dynamic Teleswitched (DTS) meters? If not, what additional remedies should we consider to address this feature?".

We also agreed to draw the Committee's attention to any updated analysis relating to the expected impact of the introduction of locational charging for transmission losses. We have recently published an updated cost-benefit analysis on this topic submitted by RWE npower ([https://assets.digital.cabinetoffice.gov.uk/media/55e8568140f0b6467a000023/RWE\\_note\\_and\\_NERA\\_report.pdf](https://assets.digital.cabinetoffice.gov.uk/media/55e8568140f0b6467a000023/RWE_note_and_NERA_report.pdf)) and announced our intention to conduct further analysis in this area to help us assess the merits of this potential remedy ([https://assets.digital.cabinetoffice.gov.uk/media/55f92854e5274a151b00000f/Notice\\_regarding\\_assessment\\_methodology\\_for\\_Josges\\_remedy.pdf](https://assets.digital.cabinetoffice.gov.uk/media/55f92854e5274a151b00000f/Notice_regarding_assessment_methodology_for_Josges_remedy.pdf)).

We will also alert the Committee to the publication of the Provisional decision on remedies, when that is available, and would be happy to appear before the Committee again to discuss our Final Report, once it is published, should the Committee find that helpful.

Yours sincerely,  
Simeon Thornton  
*Project Director*

## **Annex A: Excerpt from Notice of Possible Remedies Notice on the Administration of the Contracts for Difference mechanism**

21. As set out in Section 5 of our provisional findings, we consider that it is reasonable to assume that had the projects that were successful under the Final Investment Decision enabling for Renewables (FIDeR) scheme instead participated in the competitive Contracts for Difference (CfD) allocation process, they would have had to bid below the level of support they were awarded under FIDeR in order to secure CfDs. This would have resulted in lower electricity prices for customers. We consider that without further constraints on DECC's ability to award contracts outside the competitive process (ie via the CfD auction mechanism), further contracts may be awarded that do not benefit from competitive pressures.

22. In addition, decisions relating to the division of the technologies into separate pots, and the allocation of budgets to each pot, determine the level of support granted to each technology and therefore are critical to assess the impact, and expected gains, of this support.

23. Given the large amount of support due to go to renewable generators through CfDs (CfD payments are due to rise to £2.5 billion per year in 2020/21), we regard it as extremely important that the Department of Energy & Climate Change (DECC) bases such decisions on robust analysis, and communicates its findings to stakeholders in a transparent manner.

24. Overall, we have reached a provisional finding that the mechanisms for allocating CfDs are a feature of the GB wholesale electricity market giving rise to an AEC due to the absence of an obligation for DECC to:

- carry out, and disclose the outcome of, a clear and thorough impact assessment supporting a proposal to use its powers to allocate CfDs outside a competitive process; and
- regularly monitor the division of technologies between different pots, which form the basis of CfD auctions, and provide a clear justification when deciding on the allocation of budgets between the pots for each auction.

### ***Remedy 2a - OECC to undertake and consult on a clear and thorough impact assessment before awarding any CfO outside the CfO auction mechanism***

*How the remedy would work*

25. This remedy would seek to ensure that DECC allocates any future CfDs that it awards outside the competitive process only in situations in which it can demonstrate not only that the benefits of doing so outweigh the costs, but also that the proposed CfD award is the most desirable in terms of the ratio of benefits to costs among the options considered. We would expect DECC to meet this requirement by carrying out and consulting on a clear, detailed and thorough impact assessment for each such award. This assessment should clearly set out the likely impact of awarding the CfD, both in terms of customers' bills, and in terms of each of the three elements of the trilemma. It would require DECC to clearly state any assumptions being made and the relative weight attached to each of the factors taken into account in coming to a decision on whether to make an award outside the CfD auction mechanism, highlighting, for example, the trade-offs implied in terms of the trilemma objectives. This should both prevent further CfDs being awarded at strike prices that overcompensate projects, and being awarded to inefficient projects, and should ensure transparency over policy tradeoffs.

*Issues for comment 2a*

26. We invite views on the effectiveness and proportionality of this remedy and invite responses to the following questions:

**(a) Would the remedy ensure that CfDs that are allocated outside the auction mechanism are awarded only when the benefits of doing so outweigh the costs?**

**(b) How much discretion should DECC retain in terms of the weight it places on each factor that it takes into account in coming to a decision on which projects to award CfDs outside the CfD auction mechanism? Should DECC be required to consult on and determine these factors and their relative importance in advance to enhance transparency? Should the weighting of each factor be constant across projects?**

**(c) In which, exceptional circumstances should DECC be able to allocate CfDs outside the auction process? For example, for reasons of industrial policy, where there are wider market failures, or where there may be insufficient competitors to hold an auction?**

***Remedy 2b - DECC to undertake and consult on a clear and thorough assessment before allocating technologies between pots and the CfD budget to the different pots***

*How the remedy would work*

27. This remedy would seek to ensure that DECC considers explicitly the trade-offs it faces in allocating technologies between pots and the CfD budget to the different pots:

**(a)** on a regular basis, DECC would be required to review the allocation of technologies between pots; and

(b) in advance of each future auction, DECC would be required to publish a clear justification for its proposed allocation of the CfD budget to each pot.

28. This should ensure that CfDs are allocated in a way that ensures the decarbonisation of GB electricity generation at the lowest long-term costs.

*Issues for comment 2b*

29. We invite views on the effectiveness and proportionality of this remedy and invite responses to the following questions:

**(a) Would the remedy ensure that future decisions by DECC on the allocation of technologies and the CfD budget to the different pots are taken in a robust and transparent manner?**

**(b) Is the remedy likely to result in a positive change in how DECC makes decisions regarding the allocation of the CfD budget to the different pots?**

**(c) How regularly should DECC review the allocation of technologies between pots? What information should DECC publish when deciding to amend the allocation of technologies between pots? Should it also on a regular basis consult and/or publish reasons for not amending the allocation of technologies between pots?**

**(d) Should DECC be limited in the maximum proportion of the CfD budget that it can allocate to each of the different pots?**

30. We note that we are not considering any remedies that would seek to 'undo' any of the efDs that have already been awarded.