



LOW CARBON
CONTRACTS COMPANY

nationalgrid

Electricity Market Reform
DELIVERY BODY



Contracts for Difference (CFD) **Booklet 2016/17:** **Overview of the CFD mechanism** **and Delivery Partners**

CONTENTS

- 2** CONTENTS
- 3** PURPOSE OF THIS BOOKLET
- 4** WHAT IS A CONTRACT FOR DIFFERENCE (CFD)?
- 4** HOW DO CFD'S WORK?
- 5** HOW DO THE PAYMENTS WORK?
- 6** RESPONSIBILITIES IN THE CFD PROCESS
- 7** ROLES AND RESPONSIBILITIES UNDER THE CFD SCHEME
- 8** DELIVERY PARTNERS – CONTACT DETAILS
- 9** THE CFD APPLICATION AND ALLOCATION PROCESS
- 10** HOW WE PLAN TO ENGAGE WITH YOU

PURPOSE OF THIS BOOKLET

A Contract for Difference (CFD) is a key mechanism of the Electricity Market Reform (EMR) programme, alongside the Capacity Market and Electricity Demand Reduction pilot, that has now been successfully implemented by the Department for Business, Energy and Industrial Strategy.

This document provides stakeholders with an overview of the CFD mechanism, processes and delivery partners for the 2016/17 CFD allocation round.



WHAT IS A CONTRACT FOR DIFFERENCE (CFD)?

Contracts for Difference (CFDs) are intended to provide long-term revenue stability to low-carbon Generators. This allows investment to come forward at a lower cost of capital and therefore at a lower cost to consumers. A CFD is a private law contract between a low carbon electricity generator and the Low Carbon Contracts Company (LCCC), an independent government-owned company.

CFDs support new investment in low-carbon generation. They have been designed to give greater certainty and stability of revenues to low carbon electricity generators by reducing their exposure to volatile wholesale prices, whilst protecting consumers from paying for higher support costs when electricity prices are high.

HOW DO CFD'S WORK?

A generator that is party to a CFD is paid the difference between the 'strike price' – a price for electricity reflecting the cost of investing in a particular low carbon technology – and the 'reference price' – a measure of the average market price for electricity in the GB market – as shown in Diagram 1.

CFD payments are a two-way payment process. Where the 'reference price' is less than the 'strike price' LCCC makes a "difference payment" to the CFD generator. Where the 'reference price' is greater than the strike price, the CFD generator pays LCCC. Strike prices vary depending on the type of technology.

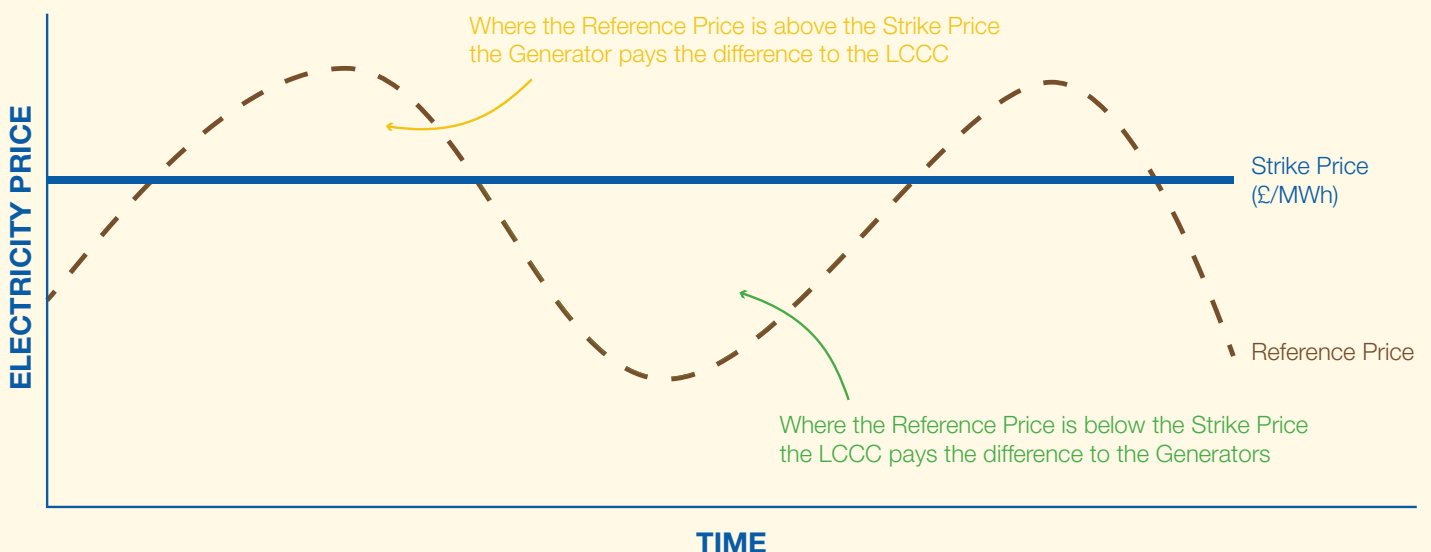


Diagram 1: How CFD's Work

HOW DO THE PAYMENTS WORK?

CFD difference payments are funded by electricity suppliers. Electricity suppliers are required under statutory regulations to fund the CFD payments made by LCCC to generators. This is done through the Supplier Obligation Levy. LCCC determines what amount it will need in each quarter in order to make difference payments to generators and sets the Levy accordingly. The Supplier Obligation Regulations require the Supplier Obligation Levy to be paid by all licensed electricity suppliers in Great Britain.

Suppliers must make daily pre-payments consisting of the Interim Levy Rate, which is levied on each supplier at a £/MWh rate based on the amount electricity they supply. They must also pay a lump sum which is the individual supplier's contribution to the Total Reserve Amount and is payable at the start of each quarterly period. The main purpose of the Total Reserve Amount is to provide security in case the Interim Levy Rate is insufficient in any quarter. The Interim Levy Rate and Total Reserve Amount are set by LCCC quarterly in advance.

RESPONSIBILITIES IN THE CFD PROCESS

Below is a diagram showing the CfD life cycle, from the Secretary of State setting the strike price and budget through to CFD allocation, contract signature and contract management. It should be read in conjunction with the 'Roles and Responsibilities' chart on the next page.

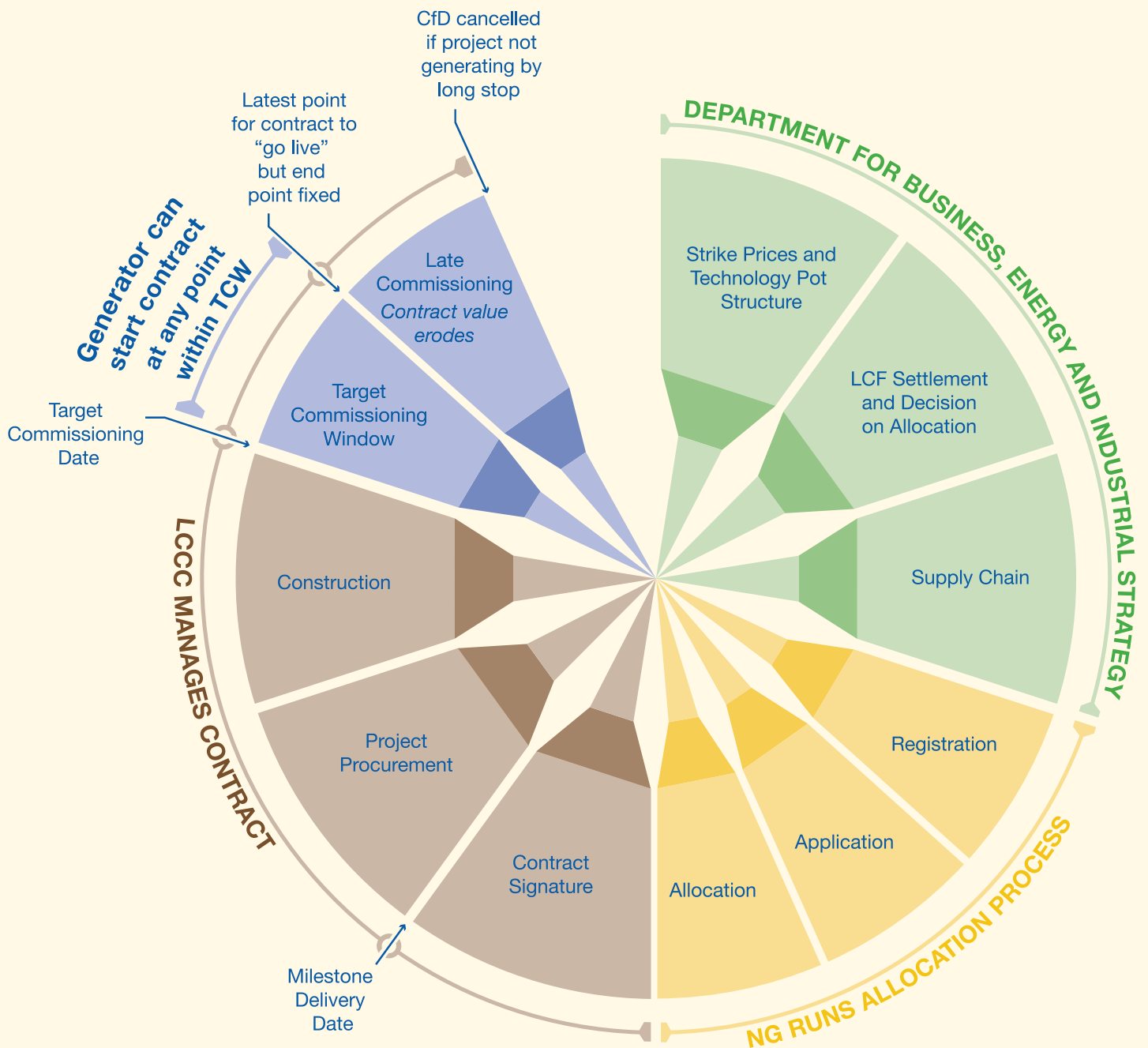


Diagram 2: Responsibilities in CFD process

ROLES AND RESPONSIBILITIES UNDER THE CFD SCHEME

A number of organisations have responsibilities under the CFD scheme. This is depicted below.

Department for Business, Energy and Industrial Strategy

1. Sets policy and terms of the CFD contract and vary terms for contracts issued in future.
2. Sets out eligibility criteria that applicants must meet and is responsible for supply chain plan approvals.
3. Sets auction rules and details process in Allocation Framework and announces Allocation Round.
4. Provides CFD budget information for participants.
5. Takes final decision based on audit report whether to proceed with, re-run or terminate an allocation round.
6. May award CFDs outside the generic allocation process.
7. Is sole shareholder of the Low Carbon Contracts Company, reviews and approves its operational budget.
8. Sets operational costs levy rate for Low Carbon Contracts Company.

National Grid (EMR Delivery Body)

1. Assesses the eligibility of applications for generic CFDs and notifies applicants of eligibility determination.
2. Values applications and assesses whether an auction process is required.
3. Runs the CFD allocation process.
4. Provides the Low Carbon Contracts Company with the information necessary to offer a CFD.
5. Conducts analysis to support Government's setting of administrative strike prices.
6. Determines disputes regarding CFD eligibility (Tier 1 disputes).

Ofgem

1. Ensures that the Delivery Body carries out its duties efficiently, cost effectively and in a timely fashion.
2. Determines disputes regarding CFD eligibility (Tier 2 disputes).
3. Is the body to which suspected market collusion is reported.

Low Carbon Contracts Company

1. Considers requests for Minor and necessary modifications.
2. Signs CFD contracts with projects allocated by Delivery Body and Government.
3. Manages and monitors contracts including Investment Contracts transferred from the Department for Business, Energy and Industrial Strategy in line with terms.
4. Forecasts CFD Payments and fixes Supplier Obligation interim rate and reserve amounts on a quarterly basis.

EMR Settlement Ltd (Settlement Services Provider)

1. Collects payments to/from suppliers and generators.
2. Collects and holds collateral from suppliers.
3. Mutualises unpaid payments.
4. Holding and managing reserve funds and credit cover payments.
5. Other outsourced delivery Such as metering verification and fuel monitoring.

DELIVERY PARTNERS – CONTACT DETAILS

Department for Business, Energy and Industrial Strategy: Policy design and implementation

Web Address: <https://www.gov.uk/government/collections/electricity-market-reform-contracts-for-difference>
Telephone: 0300 060 4000
Email Address: correspondence@decc.gsi.gov.uk

Low Carbon Contracts Company (LCCC): Counterparty to CFDs

Web Address: <https://lowcarboncontracts.uk>
Telephone: 0207 211 8881
Email Address: info@lowcarboncontracts.uk

National Grid (EMR Delivery Body): Responsible for the CFD allocation round

Web Address: www.emrdeliverybody.com
Telephone: 01926 655300
Email Address: box.emr.cfd@nationalgrid.com

Ofgem: Determines disputes in relation to CFD eligibility

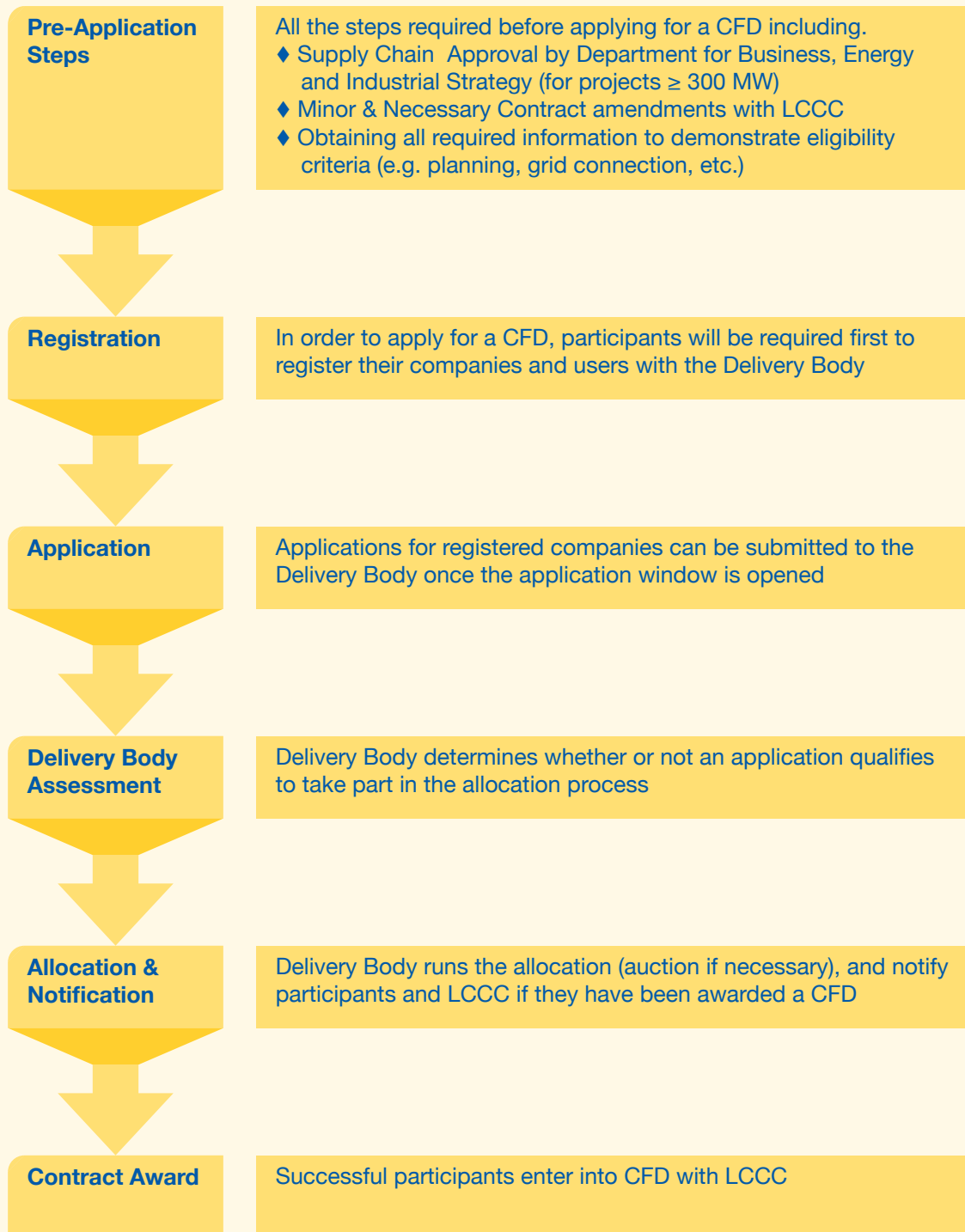
Web Address: <https://www.ofgem.gov.uk/electricity/wholesale-market/market-efficiencyreview-and-reform/electricity-market-reform-emr>
Telephone: 020 7901 7000
Email Address: EMR_DR@ofgem.gov.uk

EMR Settlement Ltd (EMRS): CFD Settlement provider

Web Address: <https://www.emrsettlement.co.uk/>
Telephone: 020 7380 4333
Email Address: contact@emrsettlement.co.uk

THE CFD APPLICATION AND ALLOCATION PROCESS

The diagram below outlines the key steps involved in applying for a CFD.



HOW WE PLAN TO ENGAGE WITH YOU

1. Stakeholder events

Events will be held during the period leading up to the allocation round, these will be focused around the following:

- ◆ The CFD process and Round timelines
- ◆ Pre-application requirements, registration applying for a CFD and the Minor and Necessary process
- ◆ Allocation rules, and how to submit sealed bids prior to running an auction
- ◆ Post CFD award contract signature and, initial conditions precedent and milestone delivery requirements

Future events will be announced on the Delivery partner's websites. Please ensure you visit the websites and subscribe to get all the latest information

2. 1:1 Meetings/Surgeries

For participants keen on applying in the next CFD Allocation Round, the Delivery Partners will arrange for 1:1 surgeries at key points in the process to:

- ◆ Run through the CFD Application Process (including pre-application requirements) and how to apply into the Delivery Body system
- ◆ How to Submit Sealed Bids and the Auction process
- ◆ Notifications throughout the Allocation process
- ◆ Key CFD terms and conditions and the Minor and Necessary process

Contact the Delivery Body if you wish to have 1:1 sessions

3. Email Notifications/ Updates

Notifications and updates will be sent out via email and through system generated notifications on the Delivery Body website. These updates and notifications will relate to key Department for Business, Energy and Industrial Strategy announcements, news, publishing of CFD guidance documents and CFD timeline updates.

You have to subscribe to the Delivery partner's websites to receive system generated information



