

Contracts for Difference for Renewable Generators

Contract for Difference

A Contract for Difference (CfD) is designed to provide the UK consumer with value for money, whilst encouraging investment in low-carbon generation. CfD provides low-carbon electricity generators with price stabilisation for up to 15 years.

A CfD is a contract entered into by a low carbon electricity generator and the Low Carbon Contracts Company (LCCC). The LCCC is owned by UK Government.

UK Government sets a 'strike price' for each low carbon technology, which is a maximum price that it is willing to pay for electricity generation from a specified technology. Strike prices are designed to reflect the cost of investing in a technology. Throughout the term of a CfD, when the wholesale price of electricity is lower than the strike price set out in the contract, the LCCC will pay the difference to the generator. When the wholesale price is above the strike price, the generator will pay the difference back to the LCCC. The purpose of the CfD is to give price stability to generators by reducing their exposure to volatile wholesale electricity prices, whilst protecting consumers from paying higher costs when electricity prices are high. In this way, CfDs provide efficient long-term support for low carbon electricity generation.

Eligibility requirements and auction process

CfD eligibility requirements include: a valid grid offer, land control and planning consent. Proof of eligibility does not guarantee a generator receives a CfD: rather the opportunity to enter a competitive auction to bid below the administrative strike price set by UK Government.

A project provides a sealed bid to LCCC confirming the lowest price it can achieve, along with binding construction and commissioning milestones. The bid must be below the strike price set by UK Government. The lowest competent bid received by LCCC sets the clearing price for all projects in that technology.

Administrative Strike Prices (in £/MWh) are set by UK Government for each target commissioning year (the year a project is required to begin generating). Technologies are split into 'Pots' and allocated strike prices accordingly:

- Pot 1** Established Technologies
- Pot 2** Less Established Technologies
- Pot 3** Biomass conversion

Two CfD Auctions have already taken place thus far:

CfD Round 1	Auction October 2014	Results February 2015
CfD Round 2	Auction April 2017	Results September 2017

The UK Government announced on 23/07/18 that the third CfD auction would take place 'by May 2019', with further auctions taking place every two years after that. The Government expects that, dependant on the prices achieved, the auctions could deliver 1-2 gigawatts of new capacity each year.

Any project on Orkney wishing to enter into CfD Round 3 must provide proof of the eligibility requirements in April 2019.

Support for Remote Island Wind

For over ten years, Orkney Islands Council has worked with Scottish Government, UK Government and other island Councils (Shetland and Western Isles) to overcome the following barriers:

- No grid capacity and a moratorium on new connections
- No transmission interconnector to UK mainland
- Highest grid charges in UK, due to lack of interconnector

In 2013, Remote Island Wind (UK Government term for projects on Orkney, Shetland or Western Isles) projects were promised a strike price of £115/MWh, to reflect the increased project risks and grid costs associated with investing in islands before a transmission cable was built¹.

In 2015, before CfD Auction Round 2, support for Remote Island Wind and marine and tidal projects was removed by UK Government and these projects were unable to participate. As a result of extensive collaboration between Councils, industry and in response to UK Government consultations on the treatment of Remote Island Wind projects, they will have an opportunity to participate in the third CfD auction in May 2019, provided they meet eligibility criteria.

The inclusion of CfD eligible Remote Island Wind project is due to UK Government recognising that island wind projects bring greater benefits to communities than projects on mainland UK and will provide security to justify interconnectors. However, Remote Island Wind projects must now bid directly against offshore wind in Pot 2 – less established technologies. Offshore wind projects cleared CfD Auction 2 with strike prices as low as £57/MWh².

Offshore wind projects have been able to achieve dramatic cost reductions due to their scale – both in terms of numbers of turbines, and also increases in rotor diameter and tip height. By their nature, Remote Island Wind projects are smaller and are subject to greater constraints by being located onshore.

Needs Case

Unlike a mainland onshore wind farm, the grid reinforcements to Orkney, Shetland and Western Isles will require Ofgem approval of an appropriate 'Needs Case'. The objective of the Needs Case assessment is to consider whether:

- There is a well justified need for reinforcement of the transmission system;
- The delivery timetable put forward by the Transmission Operator is appropriate;
- The technical scope of the option for reinforcement being proposed is appropriate; and
- The proposed reinforcement is in the interests of existing and future consumers.

SSE must ensure that the infrastructure proposed offers value for money, as well as taking into account environmental and planning constraints that exist onshore on Orkney. This is a further aspect of the grid complexity that is unique with Island wind development. The Needs Case for Orkney was submitted to Ofgem in February 2018, ahead of Shetland and Western Isles³.

Timeline

February 2018: Needs case submitted to Ofgem for Orkney interconnector, predicated on a critical mass of 70MW of generation

February 2019 Ofgem issue recommendation on Orkney needs case

April 2019 UK Government CfD auction (Projects on Orkney may bid for a CfD if eligible)

Summer 2019 SSEN proceed with interconnector based on generation with consent & route to market (i.e. CfD)

Autumn 2022 Orkney interconnector goes live

¹ <https://www.gov.uk/government/publications/scottish-islands-renewable-project-final-report>

² https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/643560/CFD_allocation_round_2_outcome_FINAL.pdf

³ <http://news.ssen.co.uk/news/all-articles/2018/march/ssen-submits-needs-case-to-ofgem-for-orkney-transmission-link/> & <https://www.orkadian.co.uk/submission-subsea-cable-final-needs-case-welcomed-local-politicians/>