

Title: Impact Assessment accompanying Government Response to the consultation on a change to the rules on the treatment of extensions to installations under the GB Feed-in Tariffs scheme Lead department or agency: DECC Other departments or agencies:	Impact Assessment (IA)
	IA No: DECC0067
	Date: 15/09/11
	Stage: Final
Source of intervention: Domestic	

Summary: Intervention and Options

What is the problem under consideration? Why is government intervention necessary?

The recent fast track review of Feed-in Tariffs (FITs) had a principal objective of preventing a substantial increase in the subsidy costs of the FITs scheme as a result of unforeseen significant uptake of large scale (50kW to 5MW) and all stand-alone solar photovoltaic (PV) installations.

Following the outcome of the fast track review, there was growing evidence of some large scale solar PV developers intending to use provisions in the FITs legislation on the accreditation of extensions to installations, in order to take advantage of the pre-fast track tariffs beyond 1 August 2011. This was not the intended effect of the extensions rules and is inconsistent with the objective of the fast track review. These provisions effectively create a loophole which, were it to remain open, would have a considerable impact on the FITs spending envelope and the integrity of the scheme, undermining the intended effect of the fast track review. Government intervention is therefore necessary to address this loophole as soon as possible.

What are the policy objectives and the intended effects?

The policy objective is to address the unintended 'loophole' effect created by the current rules on extensions, through amendment of the FITs Order. This will ensure that the extensions rules operate as originally intended and that the objectives of the fast track review can be achieved.

A principal objective of the fast track FITs review was to prevent a substantial increase in FITs subsidy costs as a result of unforeseen significant uptake of large scale solar PV. This in turn will limit the impact of the scheme on electricity bills and ensure that Government can deliver the 10% saving in 2014/15 as announced at the Spending Review.

What policy options have been considered? Please justify preferred option (further details in Evidence Base)

A policy option of changing the current rules on extensions has been considered alongside a 'Do Nothing' option of leaving the rules unchanged. Our preferred option is to amend the rules on extensions in order to ensure that the outcome of the fast track review is delivered as intended.

When will the policy be reviewed to establish its impact and the extent to which the policy objectives have been achieved?	Progress will be monitored as part of the Comprehensive FITs Review
Are there arrangements in place that will allow a systematic collection of monitoring information for future policy review?	Yes

SELECT SIGNATORY Sign-off For consultation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Charles Hendry

Date: 23/09/11

Summary: Analysis and Evidence

Policy Option

Description: Amend current rules on extensions

Price Base Year 2011	PV Base Year	Time Period Years 25	Net Benefit (Present Value (PV)) £550m		
			Low: n/a	High: n/a	Best Estimate: n/a
COSTS (£m)					
		Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)	
Low		n/a	n/a	n/a	
High		n/a	n/a	n/a	
Best Estimate		n/a	£0.8m	£20m	
Description and scale of key monetised costs by 'main affected groups'					
<ul style="list-style-type: none"> - If changes to the extensions rules remove the incentive for installations to extend, this would lead to the UK needing to purchase a greater number of EUAs (given that carbon savings resulting from FITs are in the traded sector). 					
Other key non-monetised costs by 'main affected groups'					
<ul style="list-style-type: none"> - Amending the extensions rules may have a negative impact on investor confidence. - There is a risk that the 3 AD projects below 500kW which are currently accredited for FITs could exploit the change to the extensions rules to benefit from higher, post-fast track review tariffs. However, this risk and any potential costs would be limited and small in size compared to the avoided solar PV resource costs. 					
BENEFITS (£m)					
		Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)	
Low		n/a	n/a	n/a	
High		n/a	n/a	n/a	
Best Estimate		n/a	£23m		
Description and scale of key monetised benefits by 'main affected groups'					
<ul style="list-style-type: none"> - The key benefit of amending the extensions rules is the <u>avoided resource costs</u> that will be achieved by preventing PV installations from making use of the current rules to extend existing installations after 1 August 2011 and receive the pre 1 August tariff levels. - The extent of the avoided resource costs is uncertain, as set out in the evidence base. 					
Other key non-monetised benefits by 'main affected groups'					
<ul style="list-style-type: none"> - Changing the rules on extensions will ensure that they operate as originally intended (including in the event of any future changes to FITs tariffs through the comprehensive review), that the outcome of the fast track review can be delivered as intended and that the FITs scheme can deliver the cost savings committed to as part of the Spending Review. 					
Key assumptions/sensitivities/risks				Discount rate (%)	3.5%
<ul style="list-style-type: none"> - The calculation of NPV for this IA is based solely on large scale solar PV installations. - There is a large degree of uncertainty in the number of installations that might make use of the extensions loophole. The scale of costs/benefits of changing the rules on extensions will depend on the number on installations that do not proceed with extensions under the amended rules. - Figures have been rounded. 					
Impact on admin burden (AB) (£m):		N/A		Impact on policy cost savings (£m):	
New AB:	AB savings:	Net:		Policy cost savings:	In scope
					No

Enforcement, Implementation and Wider Impacts

What is the geographic coverage of the policy/option?	Great Britain				
From what date will the policy be implemented?	October 2011				
Which organisation(s) will enforce the policy?	DECC and Ofgem				
What is the annual change in enforcement cost (£m)?	n/a				
Does enforcement comply with Hampton principles?	n/a				
Does implementation go beyond minimum EU requirements?	Yes				
What is the CO ₂ equivalent change in greenhouse gas emissions? (Million tonnes CO ₂ equivalent)	Traded: - 0.9mtCO ₂		Non-traded: n/a		
Does the proposal have an impact on competition?	No				
What proportion (%) of Total PV costs/benefits is directly attributable to primary legislation, if applicable?	Costs: n/a		Benefits: n/a		
Annual cost (£m) per organisation (excl. Transition) (Constant Price)	Micro unknown	< 20 unknown	Small unknown	Medium unknown	Large unknown
Are any of these organisations exempt?	N/A	N/A	N/A	N/A	N/A

Specific Impact Tests: Checklist

Set out in the table below where information on any SITs undertaken as part of the analysis of the policy options can be found in the evidence base. For guidance on how to complete each test, double-click on the link for the guidance provided by the relevant department.

Please note this checklist is not intended to list each and every statutory consideration that departments should take into account when deciding which policy option to follow. It is the responsibility of departments to make sure that their duties are complied with.

Does your policy option/proposal have an impact on...?	Impact	Page ref within IA
Statutory equality duties ¹ Statutory Equality Duties Impact Test guidance	No	n/a
Economic impacts		
Competition Competition Assessment Impact Test guidance	Yes	10
Small firms Small Firms Impact Test guidance	Yes	10
Environmental impacts		
Greenhouse gas assessment Greenhouse Gas Assessment Impact Test guidance	Yes	10
Wider environmental issues Wider Environmental Issues Impact Test guidance	No	10
Social impacts		
Health and well-being Health and Well-being Impact Test guidance	No	10
Human rights Human Rights Impact Test guidance	No	10
Justice system Justice Impact Test guidance	No	
Rural proofing Rural Proofing Impact Test guidance	No	10
Sustainable development Sustainable Development Impact Test guidance	No	10

¹ Race, disability and gender Impact assessments are statutory requirements for relevant policies. Equality statutory requirements will be expanded 2011, once the Equality Bill comes into force. Statutory equality duties part of the Equality Bill apply to GB only. The Toolkit provides advice on statutory equality duties for public authorities with a remit in Northern Ireland.

Evidence Base (for summary sheets) – Notes

Use this space to set out the relevant references, evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Please fill in **References** section.

References

Include the links to relevant legislation and publications, such as public impact assessment of earlier stages (e.g. Consultation, Final, Enactment).

No.	Legislation or publication
1	http://www.decc.gov.uk/en/content/cms/consultations/fit_review/fit_review.aspx
2	
3	
4	
5	
6	

+ Add another row

Evidence Base

Ensure that the information in this section provides clear evidence of the information provided in the summary pages of this form (recommended maximum of 30 pages). Complete the **Annual profile of monetised costs and benefits** (transition and recurring) below over the life of the preferred policy (use the spreadsheet attached if the period is longer than 10 years).

The spreadsheet also contains an emission changes table that you will need to fill in if your measure has an impact on greenhouse gas emissions.

Annual profile of monetised costs and benefits* - (£m) constant prices

	Y ₀	Y ₁	Y ₂	Y ₃	Y ₄	Y ₅	Y ₆	Y ₇	Y ₈	Y ₉
Transition costs										
Annual recurring cost										
Total annual costs										
Transition benefits										
Annual recurring benefits										
Total annual benefits										

* For non-monetised benefits please see summary pages and main evidence base section

Evidence Base (for summary sheets)

Impact Assessment accompanying Government Response to the consultation on a change to the rules on the treatment of extensions to installations under the GB Feed-in Tariffs scheme

Background

- 1) A new system of Feed-in Tariffs (FITs) was introduced in Great Britain on 1 April 2010 to incentivise small scale (up to 5MW), low carbon electricity generation. The scheme was established to encourage deployment of additional low carbon electricity generation, particularly by organisations, businesses, communities and individuals who are not traditionally engaged in the electricity market. Renewable electricity generation incentivised under the FITs scheme will help contribute to meeting the UK's 2020 renewables target.
- 2) On 7 February 2011, the Secretary of State for Energy and Climate Change announced the start of the first comprehensive review of the FITs scheme (including fast track consideration of large scale solar PV and farm-scale AD). As the Secretary of State's announcement made clear, it is crucial that we take a more responsible and efficient approach to public subsidy to ensure that consumers receive value for money. Last year's spending review, made clear for the first time that there are clear spending parameters within which the FITs scheme must operate and the need to make 10% savings in 2014/15 (£40 million) compared with original projected scheme spend.
- 3) The principal objective of the recent fast-track review of FITs was to prevent a substantial increase in the subsidy costs of the FITs scheme as a result of unforeseen significant uptake of large scale (50kW to 5MW) and stand-alone solar photovoltaic (PV) installations across all scales. This was achieved through a reduction in tariff levels for these installations as shown in Table 1 below.

Table 1 – Solar PV tariff levels and tariff bands for 2011/12, pre and post fast track review

PV tariffs			
Pre review (before 1 August)		Post review (on or after 1 August)	
Scale	Tariff	Scale	Tariff
	p/kWh		p/kWh
10-100kW	32.9	50-150kW	19.0
100kW-5MW	30.7	150kW-250kW	15.0
Stand alone	30.7	250kW-5MW	8.5
		Stand alone	8.5

- 4) By reducing overall subsidy costs of the scheme, this control would in turn limit the impact of the scheme on electricity bills and ensure that we are able to deliver the savings committed to as part of last year's Spending Review, complying with the control framework for DECC levy-funded spending.²

Problem under consideration

What are the extensions rules and why have they created a loophole?

- 5) When the FITs scheme was developed, it was recognised that there were likely to be instances where generators would increase the size of their installation over time. For example, a generator might install a solar PV installation in year 1 of the FITs scheme and then seek to increase the total

² See <http://bit.ly/DECCLEVYQANDA> and http://hm-treasury.gov.uk/psr_controlframework_decc.htm

capacity incrementally over a number of years. Where modifications are made to an accredited FITs installation that increase its capacity using the same technology type, this is described as an “extension”. The legislation underpinning the FITs scheme, specifically Articles 15 and 16 of the Feed-in Tariffs (Specified Maximum Capacity and Functions) Order 2010 (as amended) (“the FITs Order”), sets out the rules for accrediting such extensions.

- 6) The existing extensions rules treat installations differently depending on how long after the original installation the extension takes place (with different rules for extension within 12 months of the original installation’s commissioning date, and those after 12 months) .³ The purpose of these extensions rules was to distinguish between installations that are extended over an appropriate period of time and those that are artificially staged to take advantage of tariffs in certain bands.
- 7) Following the fast-track review of FITs there has been growing evidence that in the world of sharply decreasing tariffs created by the fast-track review, some companies were positioning themselves to use these rules in order to bank the pre-fast track tariffs for large scale solar PV beyond 1 August 2011. For example, a 10kW solar PV installation commissioned prior to 1 August (the date from which the fast track solar tariffs apply) and extending to 1MW after 1 August would, under the current extensions rules, be eligible to receive the pre-fast track tariff for the combined installation (i.e. the original installation plus the extension) i.e. 30.7p/kWh. This effectively allows developers to use the extensions rules to ‘bank’ the pre-fast track tariffs for new capacity installed after 1 August. Using the existing extensions rules in this way is inconsistent with the objectives of the fast track review.

What is the scale of the risk?

- 8) At the time of consultation, information provided to DECC by industry contacts and others suggested that there could be six sites in the south west of England which were looking to get 15-100kW of PV on the ground before 1 August, each with the intention of extending to 5MW over the following 12 months. This information also suggested that there could be at least another two projects (in Wales and Kent) actively looking into the extensions rules.
- 9) Since publishing the consultation, we have continued to monitor the situation closely. In doing so, we have become aware of further evidence of the number of projects positioned to use the extensions rules to prolong access to the pre-fast track review tariffs. This information has been derived from data supplied by Ofgem which compares the declared capacity and grid connection size for all PV sites larger than 50kW. On the basis of this further evidence, we estimate that there could be 30 sites that are planning to extend.
- 10) These figures are highly uncertain for two reasons. First, DECC may not have full visibility of all developer intentions in this area. Secondly, unless there is a change in the legislation, developers will have up to a year to act and, theoretically, any projects accredited by 1 August (however small) could be extended and benefit from the current extensions rules. However, planning permission and grid connection requirements are still required and may act as limiting factors.
- 11) The scale of the risk is potentially significantly increased by the fact that, unless changed, the extensions rules could be used in a similar way by other FITs technologies in the event of any changes following the comprehensive review of FITs. This IA focuses on the impact of large scale solar PV given that this technology was a focus of the fast track review.

What is the process for changing the rules on extensions?

- 12) As set out in the Government response to the extensions consultation, an amendment to the FITs Order will be introduced to change the rules on extensions. The Feed-in Tariffs (Specified Maximum Capacity and Functions)(Amendment No.3) Order 2011 will be laid in the Houses of Parliament on 27 September 2011 and will come into force on 18 October 2011.

³ Articles 15 and 16 of the Feed-in Tariffs (Specified Maximum Capacity and Functions) Order 2010 (as amended).

Rationale for intervention

13) As set out above, the rules on extensions were not intended to enable grandfathering of tariffs in the event of a change in tariffs. However, with the fast-track changes in tariffs these extensions rules have effectively created a loophole which, were it to remain open, would have a considerable impact on the FITs spending envelope and the integrity of the scheme, undermining the intended effect of the fast-track review. Government intervention is therefore necessary.

Description of options considered

14) The following options are considered in this Impact Assessment:

- **Do Nothing** – leave rules on extensions unchanged
- **Option 1** – change the rules on extensions

Do Nothing

15) The Do-Nothing option is the counterfactual against which costs and benefits of Option 1 have been assessed. Assessment against this counterfactual demonstrates that leaving the extensions rules unchanged will make it harder to achieve the £40m savings in 2014/15 committed to as part of the Spending Review.

Option 1

16) Option 1 would amend the existing extensions rules so that installations extending within 12 months would be treated in a similar manner to installations extending after 12 months. This would mean that for any extensions, the original installation would continue to receive the tariff it had originally been assigned, whilst the extension would receive the relevant tariff at the time of the extension. E.g. for a 10kW installation built before 1 August and extending to 1MW, the original 10kW would be eligible for a 32.9p/kWh tariff whilst the extension would receive the post-fast track tariff of 8.5p/kWh. This approach should provide greater certainty to generators than under the consultation proposal because it ensures that the tariff for the original installation is not affected by the extension.

Cost Benefit Analysis

17) The costs and benefits of Option 1 are assessed below against the Do-Nothing option.

Benefits

18) The primary benefits of changing the rules on extensions are the lower resource costs and avoided costs to consumers that would be achieved.

19) It is difficult to estimate the size of this benefit due to uncertainty in the number of projects that are looking to extend under the current extensions rules and also because the current extensions rules will have been in place for around 3 months after 1 August, when the fast track tariffs took effect.

20) DECC estimates that around thirty projects are currently contemplating making use of the loophole, amounting to around 150MW of large scale solar PV. If these 30 projects each had an original capacity of 1MW and then extended to 5MW, then under the current extensions rules this would cost the FITs scheme approximately £570m (2011 prices, discounted) in resource costs⁴ over the 25-year lifetime of

⁴ Resource costs here are the costs to the economy of deploying solar PV compared to deploying an alternative source of electricity generation (assumed to be gas CCGT).

the projects. By changing the rules on extensions, and to the extent that the changes mean that these potential extensions are not implemented, this resource cost will be avoided.

- 21) In addition to avoided resource costs, given that the cost of FITs are levied on electricity suppliers who in turn are expected to pass these costs onto their customers, there will also be avoided costs to consumers⁵ of approximately £530m (2011 prices, discounted) over the 25-year lifetime of the projects.
- 22) The extent of avoided resource costs and costs to consumers will depend on 1) the number of projects built before 1 August that we seeking to extend under the current extensions rules; 2) whether and how many of these projects extend before the new rules come into force; and 3) the relative size of the original installation compared to the extended installation. However, changing the extensions rules will prevent the rules from being used in an unintended manner (to bank pre-fast track tariffs), ensuring that the outcome of the fast track review can be delivered as intended and that the FITs scheme can deliver the cost savings committed to as part of the Spending Review.
- 23) We expect that if the extensions rules remain unchanged, a similar loophole could emerge in future (across all FIT technologies) in the event of any future changes to the scheme, e.g. any resulting from the comprehensive review. There is no information on which to base an estimate of the extent of this risk.
- 24) By amending the rules so that installations extending within 12 months are able to receive the original tariff for the original part of the installation (rather than the tariff for the combined installation), we avoid the potential situation whereby if a 10kW installation extended to 1MW, the original installation would also receive the post-fast track tariff of 8.5p/kWh. Instead, the 10kW part of the installation would retain the original 32.9p/kWh tariff and only the 990kW extension would receive the lower 8.5p/kWh tariff. This addresses concerns raised in the consultation and should provide greater certainty to generators.

Costs

- 25) There is a risk that the proposed amendment to the extensions rule will have a negative impact on investor confidence. Consultation responses provided some evidence of this, with those disagreeing with the proposal citing the potential negative impact on investments made on the basis of the current extensions rules.
- 26) Changing the rules on extensions would mean that there would be less incentive to extend large scale solar PV installations. This in turn would result in lower carbon savings than if the current extension rules were allowed to continue. Based on an estimate of thirty large scale solar PV projects, each with an original installed capacity of 1MW and looking to extend to 5MW, if changing the rules on extensions meant that the extensions did not take place, this would lead to 0.9m tonnes of foregone carbon savings over the 25-year lifetime of the projects. Note however that because these are in the traded sector, it will impact on the number of EUAs that the UK needs to purchase (at an estimated cost of approximately £20m (2011 prices, discounted)), rather than on the level of overall carbon emissions in this sector.
- 27) The fast track review, as well as reducing tariffs for large scale solar, increased tariffs for farm-scale (up to 500kW) anaerobic digestion (AD). The proposed new rules on extensions would work in the same way for AD as for PV so there is a slight risk of unintended consequences in that an AD plant already accredited for FITs could be extended, with the extended part of the installation then eligible to receive the higher, post fast-track tariff. However, the risk is very limited in budgetary terms because 1) there are only 3 AD plants of less than 500kW currently accredited for FITs (one of which is 499kW in size and so has limited scope to extend and benefit from the new rules); and 2) the AD tariffs only increased by a small amount (see Table 2 below) and so any incentive to extend in order to benefit from the new rules would be limited.

Table 2 – AD tariff levels and tariff bands for 2011/12, pre and post fast track review

AD Tariffs

⁵ Costs to consumers are the costs of paying out the FITs generation tariffs – these costs are assumed to pass through to electricity consumers.

Pre review (before 1 August)		Post review (on or after 1 August)	
Scale	Tariff	Scale	Tariff
	p/kWh		p/kWh
Up to 500kW	12.1	Up to 250kW	14.0
		250kW-500kW	13.0

28) There is a risk that amending the extensions rules to enable installations extending within 12 months to retain the original tariff for the original part of the installation (with only the extension receiving the potentially lower tariff associated with the scale of the extension), could encourage projects to be artificially staged to enable a proportion of a project to benefit from higher tariffs. However, this risk should be limited by the fact that it is only possible to notify an extension to an accredited FITs installation. We will continue to monitor this situation and if necessary return to it through the comprehensive review.

Specific Impact Tests

Competition and Small-firms assessment

- 29) Given recent evidence of rapidly falling costs of solar PV, amending the rules on extensions to prevent banking of pre-fast track tariffs, will reduce the extent of any economic rents paid to investors and/or installers and in turn be beneficial for competition in the market.
- 30) The amendments may impact on small firms e.g. small installers and may also have a negative impact on investor confidence. There is insufficient evidence to assess the scale of this potential impact.

Environmental impacts

- 31) As a result of amending the extensions rules, it is estimated that the UK may need to purchase additional EUAs to cover 0.9m tonnes of carbon, at an estimated cost of approximately £20m (2011 prices, discounted).
- 32) Any impacts on the wider environment (e.g. on air quality, noise, water pollution etc) will be minimal.

Social Impacts

- 33) Any impacts on health and well being are expected to be insignificant.
- 34) There are no expected impacts on human rights.
- 35) There are no expected impacts on the justice system.
- 36) Any rural impacts are expected to be minimal.

Sustainable Development

- 37) There are no envisaged impacts on sustainable development.

Summary and chosen option

- 38) The extensions rules were not intended to provide a loophole whereby installations are able to bank tariffs after a tariff change. The recommended option is therefore to amend the FITs Order to address the loophole (Option 1).

Annexes

Annex 1 should be used to set out the Post Implementation Review Plan as detailed below. Further annexes may be added where the Specific Impact Tests yield information relevant to an overall understanding of policy options.

Annex 1: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below.

<p>Basis of the review: [The basis of the review could be statutory (forming part of the legislation), it could be to review existing policy or there could be a political commitment to review];</p> <p>Progress will be monitored via the Comprehensive Review of FITs that is currently underway and due for consultation later this year.</p>
<p>Review objective: [Is it intended as a proportionate check that regulation is operating as expected to tackle the problem of concern?; or as a wider exploration of the policy approach taken?; or as a link from policy objective to outcome?]</p> <p>Progress will be monitored to ensure that the identified extensions loophole has been adequately addressed.</p>
<p>Review approach and rationale: [e.g. describe here the review approach (in-depth evaluation, scope review of monitoring data, scan of stakeholder views, etc.) and the rationale that made choosing such an approach]</p> <p>Monitoring data and other information will be used to assess whether closing the loophole delivers its intended effects.</p>
<p>Baseline: [The current (baseline) position against which the change introduced by the legislation can be measured]</p> <p>The baseline will be the status quo (i.e. no change to rules on extensions).</p>
<p>Success criteria: [Criteria showing achievement of the policy objectives as set out in the final impact assessment; criteria for modifying or replacing the policy if it does not achieve its objectives]</p> <p>Investors do not use the extensions rules in an unintended manner e.g. to bank pre-review tariffs.</p>
<p>Monitoring information arrangements: [Provide further details of the planned/existing arrangements in place that will allow a systematic collection of monitoring information for future policy review]</p> <p>Data will be collected as part of on-going management information and for the comprehensive review of FITs.</p>
<p>Reasons for not planning a PIR: [If there is no plan to do a PIR please provide reasons here]</p> <p>Progress will be monitored via the Comprehensive Review.</p>

Add annexes here.