EXPLANATORY MEMORANDUM TO

THE FEED-IN TARIFFS (AMENDMENT) (No. 3) ORDER 2015

2015 No. 2045

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department of Energy and Climate Change and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 The Feed-in Tariffs scheme ("FIT scheme") is the Government's main policy measure to encourage the deployment of small-scale low-carbon electricity generation in Great Britain, and is implemented by the Feed-in Tariffs Order 2012 ("the 2012 Order") (as amended) and modifications to Conditions 33 and 34 of the standard conditions of electricity supply licences ("the Standard Licence Conditions").

2.2 The Feed-in Tariffs (Amendment) (No. 3) Order 2015 and the associated modifications to the standard licence conditions make changes to the 2012 Order and to the Standard Licence Conditions to, among other things, set out a revised level of generation tariffs to be paid under the scheme and to introduce a cost control mechanism in the form of a limit in the aggregate capacity (measured in megawatts) that can be applied for per quarter per type of installation under the scheme.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

Other matters of interest to the House of Commons

3.2 As this instrument is subject to the negative procedure and has not been prayed against, consideration as to whether there are other matters of interest to the House of Commons does not arise at this stage.

4. Legislative Context

4.1 Sections 41 to 43 of the Energy Act 2008 provide powers to establish a feed-in tariff scheme for the small scale generation of electricity.

4.2 The 2012 Order, made under section 41(4), 43(3)(a) and 104(2) of that Act, sets out the functions of the Gas and Electricity Markets Authority ("the Authority") and the Secretary of State in connection with the administration of the FIT scheme including the procedure in which the Authority will accredit installations applying to the scheme.

4.3 The Modifications to the Standard Licence Conditions impose requirements on electricity suppliers to pay a generation tariff and an export tariff to generators of accredited installations under the scheme. The modifications set out the level of tariffs to be paid. They also set out a degression mechanism under which the level of tariff decreases over time and in response to deployment levels, to reflect that the costs of installation continue to decrease and to provide a protection for the public purse.

5. Extent and Territorial Application

5.1 This instrument extends to Great Britain.

5.2 This instrument applies to Great Britain.

6. European Convention on Human Rights

6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

What is being done and why

7.1 The Government is committed to cost-effective decarbonisation of our electricity supply and to protecting consumer bills by controlling costs under the levy control framework. Levy control framework projections published in July showed a significant overspend due to, among other things, demand-led schemes providing unchecked support for the renewables industry.

7.2 To this end, DECC announced a package of proposed cost control measures including a consultation on the future of the Feed-in Tariffs (FITs) scheme, launched on 27 August 2015. The consultation proposed a number of measures to meet two core objectives. Firstly, to comply with our State aid approval a review of the support offered by the FITs scheme every three years. Secondly, proposals aimed at controlling the cost of the scheme to limit the impact on consumer bills.

7.3 The FIT scheme now supports over 780,000 installations with a total of 4.2 Gigawatts (GW) of renewable electricity generating capacity. FITs is funded through the Levy Control Framework (LCF). Support for FITs projects is currently projected to cost at least £1.74 billion in 2020/21 if measures are not taken to control spend. This is much higher than was anticipated when the £7.6 billion LCF 2020/21 cap was set in 2013, due to significantly higher levels of deployment than were projected. Action therefore needs to be taken to bring this projected spend down in order to responsibly manage the LCF impact on consumer bills.

7.4 Overall, these measures seek to maintain a viable solar industry which, in the medium term, can continue to reduce its costs and move towards subsidy-free deployment, and to provide other technology sectors with tapered support over the coming years. We have sought to balance the different needs of industry, consumers and communities - and to target support where it is most needed.

7.5 To that end, the amending instruments make the following changes to the scheme:

Modifications to the standard licence conditions:

7.6 Updated generation tariffs: the consultation document proposed revised tariffs based on evidence produced by an independent consultant for hydro, wind and solar photovoltaic. These proposed tariffs have in turn been revised in response to evidence on technology costs received during the consultation. Tariffs have been set to ensure a viable scheme while maximising value for money and to enable us to remain within the scheme's state aid approval.

7.7 A degression mechanism that means that tariffs will automatically reduce each quarter in order to reflect the continuing decreases in the costs of installation. For each type of installation (including anaerobic digestion), the tariffs will degress even further each quarter if the deployment cap described below is met.

7.8 Changes to require appropriate Energy Performance Certificates to be obtained for properties prior to the commissioning date for solar PV installations (as oppose to their eligibility dates). This is necessitated by the implementation of deployment caps and will better align the scheme with our energy efficiency objectives of making consumers consider options for improving the energy performance of buildings before installing microgeneration equipment.

The amending order:

7.9 Introduction in the New Year of a temporary pause in the scheme where between 15 January and 7 February the Authority will not be able to accredit applications. This will allow time for the implementation of cost-control measures and will preserve budget for the future of the scheme.

7.10 Introduction of deployment caps in the guise of a limit on the aggregate total installed capacity of installations that can be applied for within any quarter (tariff period) . This enables us to limit spend on the scheme to £100m up to the end of 2018/19. Applications for the accreditation of commissioned installations will be determined by Ofgem in the order in which they are received and (for MCS-certified installations in the order of issuance of their MCS certificates). If the cap is reached, Ofgem will stop accrediting installations and any remaining applications will wait until the next quarter for Ofgem to redetermine whether they should be accredited.

7.11 The reintroduction of preliminary accreditation for solar PV and wind generators over 50kW and all hydro and anaerobic digestion generators, though all such applications will be subject to the limit described above.

7.12 Removal of the ability to claim the generation tariff for extensions for all scheme participants. This removes the right of participants to extend their capacity and claim a separate tariff for the extension. This measure will help control costs, prevent gaming and is also important in the successful implementation of deployment caps. A modification to the licence conditions means that in the future, where an accredited FIT installation extends, the supplier will pay the FITs in respect of the accredited part of the installation only. We have also modified the rules regarding the site of an installation so that hydro generating stations sourcing their water from the same reservoir will no longer be treated as extensions but will apply to be accredited as separate FIT installations.

7.13 Changes to limit exemptions from the FIT levelisation process for imported renewable electricity. These changes will restrict the impact on the levelisation process of a sudden rapid increase in imported renewable electricity.

7.14 A technical drafting change so that the definition of "MCS-certified installation" given in the Order now references specific versions of Microgeneration Certification Scheme (MCS) installation standards. This will end an inadvertent sub-delegation of powers to MCS.

7.15 Changes granting Ofgem the power to access levelisation fund interest to part-fund its costs incurred in implementing the changes required as part of this review.

8. Consultation outcome

Consultation outcome

8.1 A consultation paper was published on 27 August 2015 and closed on 23 October 2015. The consultation ran for a shortened period of eight weeks because of the urgent need to implement cost-control measures, given the forecast overspend on the levy control framework. Government officials engaged directly with a number of trade associations and held stakeholder events across the country seeking views from various sectors, groups and individuals, as well as an online web-chat available for all. For this reason, despite the shorter consultation period, we consider that we were able to receive all necessary comment on the consultation. In total, DECC received 54,630 written separate responses to the consultation. This included 2,634 unique responses addressing the questions in the consultation and 51,996 as part of e-mail campaigns run by Greenpeace and 10:10.

8.2 Specific responses were received from a wide range of stakeholders across a number of sectors with an interest in the FIT scheme.

8.3 The Government's response to this consultation was published simultaneously with the laying of this legislation on xx December 2015. This sets out a detailed analysis of the consultation responses and policy decisions and is available at https://www.gov.uk/government/consultations/consultation-on-a-review-of-the-feed-in-tariff-scheme.

Generation tariffs

8.4 The majority of respondents disagreed with the proposed generation tariffs, mainly on the grounds they were too low to bring forward investment. Many respondents criticised various aspects of the evidence base, as well as the proposed rates of tariff reduction and the proposed triggers for these reductions. Only about 100 respondents to the consultation supplied usable and evidenced data in the form of receipts, company invoices or other official documents.

8.5 Where possible, DECC was able to use this evidence to revise the generation tariffs proposed in the consultation. A full account of the changes made here and their rationale is provided in the Government response document and Impact Assessment.

Deployment caps and pre-accreditation

8.6 Most respondents objected to the proposed implementation of deployment caps. Reasons included objection to constraining renewables deployment, impacts on tackling climate change and the creation of uncertainty to invest and make plans. Several respondents argued that if caps were introduced, the re-introduction of preliminary accreditation would be essential to reduce some of this uncertainty. Respondents provided comments on the design of caps, including how they should be implemented, their frequency, the metric for measuring caps and ways of allocating the cap between individual technologies.

8.7 Government's view is that deployment caps are necessary if the scheme is to continue and if its impacts on consumers' bills are to be properly controlled. Government recognises the strength of opinion that the £100m budget is too low, but this remains the maximum amount Government considers affordable, given the significant level of deployment and support already provided. To mitigate some of the uncertainty inherent in a system of capped deployment, we have reintroduced preliminary accreditation. Government has also taken into account views expressed in the consultation on the design of caps, in particular the widely expressed preference for a "rolling" cap with a queue system. Further detail on the allocation of caps can be found in the Government response.

Scheme pause

8.8 DECC consulted on the impact of pausing applications to FITs for a short specified period to allow full implementation of cost control measures. The majority of respondents focused on the negative impacts of a pause on their business or the renewables sector more widely. Reasons cited related to the uncertainty which a pause would create in the industry and the cash-flow impact on businesses. A number of respondents felt a pause, although undesirable, was a better option than the alternative option in the consultation of closing the scheme. Respondents stated that a pause should be short and clearly defined, with a clear message on what the scheme would look like after the pause.

8.9 Government has decided to implement a scheme pause from 15 January to 7 February, to preserve the £100m budgetary cap from January. Government notes concerns raised in the consultation and recognises that this may create uncertainty for some organisations. However, Government must balance this against the long term viability of the scheme. We consider the fact that the pause is only three and a half weeks with a clear beginning and end date should mitigate this effect.

Extensions

8.10 DECC sought views on the proposal to remove the ability of all (i.e. both existing and future) installations to extend their capacity and receive a generation tariff for such extensions. There was some limited support for the proposal, on the grounds it would allow a greater number of new installations to deploy. Those who disagreed claimed that extensions often represented good value for money (for developers) due to economies of scale, and bring additional investment to the supply chain. A number of respondents also asserted that applying the proposal to existing installations, rather than future installations only, was unfair as it was retrospective.

8.11 Government has decided to remove the right to receive a generation tariff for extensions for all installations. We believe that the ability to extend creates the potential for gaming of tariffs (the opportunity to receive an incrementally higher tariff than if the full capacity was deployed in one go). This measure will therefore incentivise generators to install the maximum capacity achievable and eliminate the potential for generators to lock in higher tariffs for some of the capacity installed. We do not consider that applying the proposal to existing installations would be retrospective given this change has been flagged from the end of August, giving installations over four months to adapt their plans.

Changes to energy efficiency criteria

8.12 There was a limited number of responses to the proposal to require that an Energy Performance Certificate (EPC) is obtained prior to the commissioning date of solar PV installations under 50kW. It was pointed out that PV installations contribute significantly to the EPC rating requirements; and that this change would increase hassle and cost for participants who wished to install energy efficiency measures and renewable plant at the same time.

8.13 DECC's aim in this proposal was to ensure the FIT scheme's energy efficiency requirement for solar PV installations encourages improvements in the energy efficiency of properties more generally. We do not consider the arguments made by respondents against this proposal address this particular concern, and so intend to implement this change.

Changes to FIT levelisation process exemptions

8.14 Government sought views on proposals to limit the type and amount of overseas renewable electricity that can be used for the purposes of claiming an exemption from suppliers' shares FITs costs. Many respondents considered the change would encourage greater levels of domestic renewable energy production. In opposition, respondents disagreed with the principle of restricting the use of imported electricity, both for levelisation and more generally.

8.15 Having considered the views presented, Government intends to implement these proposals so as to apply for FIT year 7 and for subsequent years. DECC considers the current incentive distorts the market as suppliers seek to import greater quantities of renewable electricity than would otherwise be the case. Imposing a restriction should reduce this distortion, bringing the FIT levelisation exemption in line with other exemptions from levy costs, such as that for the Contract for Difference Supplier Obligation, and may help level the playing field between established suppliers and new entrants.

MCS standards

8.16 Government proposed to make a drafting change so that it is clearly set out in the FITs legislation the relevant MCS installation standards that apply to the installation of MCS-certified installations. . Those respondents who agreed or disagreed were split evenly between those who felt the proposal would protect against abuse of the system; and those worried it would undermine or reduce the role of MCS in the FIT scheme.

8.17 This proposal seeks to address a technical issue relating to what can and cannot be done in secondary legislation. DECC does not consider the objections raised by stakeholders amount to a substantive challenge to the need to amend the legislation, nor to the structure of the proposal. Therefore, we intend to implement the proposal.

Levelisation fund interest

8.18 The Government proposed using interest accrued on the FIT Levelisation Fund to part-fund changes to the scheme required to implement the proposals in the consultation. Most respondents neither agreed nor disagreed with this proposal; and slightly more agreed than disagreed, noting the relatively small sum involved and the administrative complexity of the alternative: redistribution among FIT licensees. The most common dissenting view was that any interest accrued should be spent on deploying more renewable generation.

8.19 Having given careful consideration to the views expressed, Government has decided to allow grant Ofgem to use the levelisation fund interest to part-fund its reasonable costs incurred in administering the FITs scheme (to be determined by the Secretary of State). We have considered the views of those who disagreed with our proposal but feel that the value of the levelisation fund is so small that, in terms of deployment, the impact on the sector would be negligible.

9. Guidance

9.1 Ofgem already provides detailed guidance for electricity suppliers and potential participants in the FIT scheme in a variety of forms. That guidance will be updated to reflect these changes to the FIT scheme.

10. Impact

10.1 Business, charities and voluntary bodies are subject to rising electricity costs under the levy control framework, and this measure is intended to mitigate these costs. These bodies may also deploy low carbon technologies under the FIT scheme. This ability to deploy may be affected by the introduction of a cap on overall deployment. This effect, however, should be mitigated by the reintroduction of pre-accreditation, especially for community organisations who have a longer validity period in which to deploy.

10.2 These changes will have an impact on the public sector, which is subject to rising electricity costs under the levy control framework. The public sector may also deploy low carbon technologies under the FIT scheme. This ability may be affected by the introduction of a cap on overall deployment.

10.3 An Impact Assessment is submitted with this memorandum and is published alongside the Explanatory Memorandum on the legislation.gov.uk website.

11. Regulating small business

11.1 The legislation applies to activities that are undertaken by small businesses.

11.2 Small businesses are affected by increasing electricity costs under the levy control framework, and this measure is intended to mitigate those costs. Small businesses operating in the sectors supported by the FIT scheme will also be affected by this legislation, which introduces a cap on overall spend and deployment under the scheme.

12. Monitoring & review

12.1 The changes implemented by these two instruments aim to ensure that tariffs provide an appropriate level of compensation for new participants and that overall spending on the scheme is subject to suitable cost control. The Department will continue to carry out ongoing monitoring of the FIT scheme to ensure that its objectives are delivered in a way which ensures value for money, particularly to consumers who ultimately pay. The Authority also carries out monitoring to ensure compliance by electricity suppliers and participants in the scheme with their obligations.

13. Contact

13.1 Joseph Wilkinson at the Department of Energy and Climate Change (Telephone: 0300 068 6574 or email: joseph.wilkinson@decc.gsi.gov.uk) can answer any queries regarding the instruments.