

<b>Title: Impact assessment accompanying consultation on a change to the rules on the treatment of extensions to installations under the GB Feed-in Tariffs scheme</b>  <b>Lead department or agency: DECC</b>  <b>Other departments or agencies:</b>	<b>Impact Assessment (IA)</b>
	<b>IA No: DECC0067</b>
	<b>Date: 25/07/11</b>
	<b>Stage: Consultation</b>
	<b>Source of intervention: Domestic</b>
	<b>Type of measure: Regulation</b>
	<b>Contact for enquiries:</b> Sarah Nightingale

## 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.

Since announcing the outcome of the fast track review, there has been evidence that some large scale solar PV developers are intending to use provisions in the FITs legislation on the accreditation of extensions to installations, in order to take advantage of the current 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 loophole created by the current rules on extensions by amending 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.

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

A policy option of addressing the extensions loophole has been considered alongside a 'Do Nothing' option of leaving the loophole in place. Our preferred option is to address the loophole in order to ensure that the outcome of the fast track review is delivered as intended.

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

Date: 26/07/11

URN: 11D/832

**Description: Close extensions loophole**

Price Base Year 2011	PV Base Year	Time Period Years 25	Net Benefit (Present Value (PV)) £180m		
			Low: n/a	High: n/a	Best Estimate: n/a
<b>COSTS (£m)</b>	<b>Total Transition</b> (Constant Price) Years		<b>Average Annual</b> (excl. Transition) (Constant Price)	<b>Total Cost</b> (Present Value)	
Low	n/a		n/a	n/a	
High	n/a		n/a	n/a	
Best Estimate	n/a		£0.4m	<b>£10m</b>	
<b>Description and scale of key monetised costs by 'main affected groups'</b>					
<ul style="list-style-type: none"> <li>- If fewer installations are able to exploit the extensions loophole, this could lead to lower carbon savings. Based on eight 5MW projects exploiting the loophole, closing the loophole would mean the UK needing to purchase approximately £10m worth of EUAs (2011 prices, discounted) over the 25-year lifetime of the projects.</li> </ul>					
<b>Other key non-monetised costs by 'main affected groups'</b>					
<ul style="list-style-type: none"> <li>- Amending the extensions rule may have a negative impact on investor confidence.</li> <li>- There is a risk that the 1 AD project below 500kW could exploit the change to the extensions rule to benefit from higher, post-fast track review tariffs. However, this risk and any potential cost would be limited and small in size compared to the avoided solar PV resource costs.</li> </ul>					
<b>BENEFITS (£m)</b>	<b>Total Transition</b> (Constant Price) Years		<b>Average Annual</b> (excl. Transition) (Constant Price)	<b>Total Benefit</b> (Present Value)	
Low	n/a		n/a	n/a	
High	n/a		n/a	n/a	
Best Estimate	n/a		£7m	<b>£190m</b>	
<b>Description and scale of key monetised benefits by 'main affected groups'</b>					
<ul style="list-style-type: none"> <li>- The key benefit of addressing the extensions loophole is the avoided resource costs that will be achieved by preventing installations from building and commissioning part of an installation pre 1 August and then later extending the installation and banking the pre 1 August tariff levels.</li> <li>- The extent of the avoided resource costs will be dependent on a number of factors including 1) the number of projects built before 1 August that are seeking to use the loophole; 2) the relative size of the original installation compared to the extended installation; and 3) the extent to which the loophole can be exploited before the loophole can be addressed.</li> <li>- Our central estimate is that resource costs of £190m (2011 prices, discounted) would be avoided over the 25-year lifetime of 8 projects that could potentially exploit the loophole.</li> </ul>					
<b>Other key non-monetised benefits by 'main affected groups'</b>					
<ul style="list-style-type: none"> <li>- Closing the loophole will ensure that the extensions rules operate as originally intended, 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.</li> <li>- Addressing the loophole will also prevent other FITs technologies from potentially gaming the extensions rules following the Comprehensive Review of FITs.</li> </ul>					
<b>Key assumptions/sensitivities/risks</b>				Discount rate (%)	
<ul style="list-style-type: none"> <li>- The calculation of NPV for this IA is based solely on large scale solar PV.</li> <li>- 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 addressing the loophole will depend on the number on installations that are prevented from exploiting the loophole.</li> <li>- Figures have been rounded.</li> </ul>				n/a	

<b>Impact on admin burden (AB) (£m):</b>		N/A	<b>Impact on policy cost savings (£m):</b>		<b>In scope</b>
<b>New AB:</b>	<b>AB savings:</b>	<b>Net:</b>	<b>Policy cost savings:</b>		<b>No</b>

## 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 (approx)				
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 <sub>2</sub> equivalent change in greenhouse gas emissions? (Million tonnes CO <sub>2</sub> equivalent)	<b>Traded:</b> - 0.4mtCO <sub>2</sub>		<b>Non-traded:</b> 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?	<b>Costs:</b> n/a		<b>Benefits:</b> n/a		
Annual cost (£m) per organisation (excl. Transition) (Constant Price)	<b>Micro</b> unknown	<b>&lt; 20</b> unknown	<b>Small</b> unknown	<b>Medium</b> unknown	<b>Large</b> 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
<b>Statutory equality duties</b> <sup>1</sup> <a href="#">Statutory Equality Duties Impact Test guidance</a>	No	n/a
<b>Economic impacts</b>		
Competition <a href="#">Competition Assessment Impact Test guidance</a>	No	n/a
Small firms <a href="#">Small Firms Impact Test guidance</a>	No	n/a
<b>Environmental impacts</b>		
Greenhouse gas assessment <a href="#">Greenhouse Gas Assessment Impact Test guidance</a>	No	n/a
Wider environmental issues <a href="#">Wider Environmental Issues Impact Test guidance</a>	No	n/a
<b>Social impacts</b>		
Health and well-being <a href="#">Health and Well-being Impact Test guidance</a>	No	n/a
Human rights <a href="#">Human Rights Impact Test guidance</a>	No	n/a
Justice system <a href="#">Justice Impact Test guidance</a>	No	n/a
Rural proofing <a href="#">Rural Proofing Impact Test guidance</a>	No	n/a
<b>Sustainable development</b> <a href="#">Sustainable Development Impact Test guidance</a>	No	n/a

<sup>1</sup> 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	<a href="http://www.decc.gov.uk/en/content/cms/consultations/fit_review/fit_review.aspx">http://www.decc.gov.uk/en/content/cms/consultations/fit_review/fit_review.aspx</a>
2	
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+ 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 <sub>0</sub>	Y <sub>1</sub>	Y <sub>2</sub>	Y <sub>3</sub>	Y <sub>4</sub>	Y <sub>5</sub>	Y <sub>6</sub>	Y <sub>7</sub>	Y <sub>8</sub>	Y <sub>9</sub>
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 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 is intended 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).
- 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

<b>PV tariffs</b>			
<b>Pre review (before 1 August)</b>		<b>Post review (on or after 1 August)</b>	
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.<sup>2</sup>

#### **Problem under consideration**

What is the extensions loophole?

- 5) Under the FITs scheme, if a generator extends an installation within 12 months of its original commissioning date, then the combined installation (extension + original installation) would be eligible for the tariff that applied at the time of the original installation.

<sup>2</sup> See <http://bit.ly/DECCLEVYQANDA> and [http://hm-treasury.gov.uk/psr\\_controlframerwork\\_decc.htm](http://hm-treasury.gov.uk/psr_controlframerwork_decc.htm)

- 6) The original purpose of these rules was to avoid gaming that could arise because FIT tariffs are higher for smaller scale installations. For example a developer leaving a month's gap between commissioning neighbouring 500kW wind turbines in order to bank the higher, 19.7p/kWh tariff for the first turbine instead of getting the lower, 9.9p/kWh for the combined 1MW capacity of the two turbines.
- 7) There is growing evidence that in the world of sharply decreasing tariffs created by the fast-track review, some companies are positioning themselves to use these rules in order to bank the current tariffs for large scale solar PV beyond 1 August 2011. Without action, this could also set a precedent for any tariff reductions following the comprehensive review of FITs that is currently under way.

#### What is the scale of the risk?

- 8) Information provided to DECC by industry contacts and others suggests that there could be six sites in the south west of England which are 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. There could also be at least another two projects (in Wales and Kent) actively looking into the extensions rules.
- 9) 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 loophole. However, planning permission and grid connection requirements are still required and may act as limiting factors.
- 10) The scale of the risk is potentially significantly increased by the fact that other FITs technologies may make use of the loophole to avoid any reductions in tariffs 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. However, the loophole exists across all FITs technologies.

#### What is the process for addressing the extensions loophole?

- 11) The rules on extensions are set out in the FITs Order and apply to all technologies in the same way. Given that the current loophole could also become a broader issue following the comprehensive review, we are working on the basis that any changes to the rules would cover all technologies rather than carving out a specific application to large scale solar PV.
- 12) The extensions loophole would be addressed by amending the FITs Order so that if an installation is extended within 12 months of its original commissioning date, the combined installation (extension + original installation) would be eligible for the tariff that applied at the time that the extension is commissioned rather than the tariff that applied at the time of the original installation.

### **Rationale for intervention**

- 13) The rules on extensions were not intended to create a loophole whereby investors could effectively bank pre-review tariffs by commissioning part of an installation before the new tariffs set in. Intervention is therefore necessary to close this loophole.

### **Policy objective**

- 14) The policy objective is to address the risk of large scale solar PV developers exploiting a loophole in the FITs rules to bank the pre-fast track tariffs, and to prevent the potential for installers of other FITs technologies from a similar form of gaming following any new tariffs from the comprehensive review.

### **Description of options considered**

- 15) The following options are considered in this Impact Assessment:

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

### ***Do Nothing***

16) The costs of the Do Nothing option are the opposite of the benefits listed under Option 1. In particular, leaving the extensions loophole in place will make it harder to achieve the £40m savings in 2014/15 committed to as part of the Spending Review.

### ***Option 1***

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

#### Costs

- 17) There is a risk that the proposed amendment to the extensions rule will have a negative impact on investor confidence.
- 18) Closing down the loophole would mean that fewer large scale solar installations are likely to be extended. This in turn would result in lower carbon savings than if the loophole were allowed to continue. Based on eight projects originally building at 100kW each and looking to extend to 5MW, closing the loophole would lead to 0.4m 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 £10m (2011 prices, discounted)), rather than on the level of overall carbon emissions in this sector.
- 19) 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 new installation then eligible to receive the higher, post fast-track tariff. However, the risk is very limited in budgetary terms because 1) there is only 1 AD plant of less than 500kW currently accredited for FITs; and 2) the AD tariffs only increased by a small amount (see Table 2 below).

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

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

#### Benefits

- 20) The primary benefits of closing down the loophole are the lower resource costs and avoided costs to consumers that would be achieved.
- 21) It is difficult to estimate the size of this benefit due to uncertainty in the number of projects that are looking to exploit the loophole and also because the earliest that the loophole can be addressed in practice is around October 2011 (i.e. the loophole would exist for up to 3 months after 1 August, when the fast track tariffs take effect).
- 22) DECC estimates that around eight projects are currently contemplating making use of the loophole, amounting to around 40MW of large scale solar. If the 8 projects are originally built at 100kW each, then

avoiding their extension to 5MW each would save approximately £190m (2011 prices, discounted) in resource costs<sup>3</sup> over the 25-year lifetime of the projects.

- 23) In addition to avoided resource costs, there will also be avoided costs to consumers<sup>4</sup> of approximately £170m (2011 prices, discounted) over the 25-year lifetime of the projects.
- 24) The extent of avoided resource costs and costs to consumers will depend on 1) the number of projects built before 1 August that are seeking to use the loophole; 2) the relative size of the original installation compared to the extended installation; and 3) the date at which it can be closed. However, closing down the loophole will ensure that the extensions rules operate as originally intended, 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.
- 25) We expect that if this loophole remains, future installations (across all FIT technologies) may also attempt to benefit from it prior to tariffs being changed following a scheme review. There is no information on which to base an estimate of the extent of this risk.

### **Summary and chosen option**

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

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<sup>3</sup> 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).

<sup>4</sup> Costs to consumers are the costs of paying out the tariffs – these costs are assumed to pass through to electricity consumers.



## 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><b>Basis of the review:</b> [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><b>Review objective:</b> [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><b>Review approach and rationale:</b> [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><b>Baseline:</b> [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><b>Success criteria:</b> [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>No gaming on the size of future installations by developers</p>
<p><b>Monitoring information arrangements:</b> [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><b>Reasons for not planning a PIR:</b> [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.