

UK Capacity Market Auctions and Payments Postponed Indefinitely Following General Court Ruling

Background

On 14 November 2018, the General Court found in favour of Tempus Energy, against the European Commission (Commission), annulling the Commission's decision not to raise objections to the aid scheme establishing a Capacity Market in the UK. The judgment suspends the state aid approval for, and therefore the legality of, granting aid through the Capacity Market.

Tempus Energy contended that scheme privileges generation over demand side response (DSR) in a discriminatory and disproportionate manner that goes beyond what is necessary to achieve its objectives and satisfy the state aid rules.

The UK Commission now has two months to appeal the ruling before the Court of Justice or adopt a new decision taking into account the ruling of the General Court.

What Does the Judgment Mean?

The ruling imposes a "standstill period on the Capacity Market", which prevents the UK government from **holding any Capacity Market Auctions, making any capacity payments under existing agreements**, or undertaking any other action, which could be seen as granting State Aid, until the scheme can be approved again.

The Secretary of State has today instructed National Grid to **postpone indefinitely the upcoming T-4 and T-1 Capacity Market Auctions for Delivery Years 2022/23 and 2019/20 respectively**, in accordance with Regulation 26(3)(a) of the Electricity Capacity Regulations 2014.

Rationale of the Decision

The General Court examined the claim to determine whether the Capacity Market raised doubts as to its compatibility with the UK's internal market in the light of, *inter alia*, the EU guidelines on State Aid for environmental protection and energy. The General Court found, *inter alia*, that:

- a. The Commission failed properly to assess the role of DSR within the capacity market.
- b. The Commission was not in a situation where it could simply rely on the information provided by the UK without carrying out its own investigation in order to examine and, if necessary, seek relevant information from, where appropriate, other interested parties for the purposes of its assessment.
- c. The concept of "doubts" as to the compatibility of the Capacity Market with the UK's internal market is exclusive, thus, the Commission may not decline to initiate the formal investigation procedure in reliance on other circumstances, such as third-party interests, considerations of economy of procedure or any other ground of administrative or political convenience.

In the present case, in order to prove the existence of doubts, Tempus had to establish that the Commission had not researched and examined all of the relevant information in such a way that, when it adopted the contested decision, it had at its disposal assessment factors that could reasonably be considered to be sufficient and clear for the purposes of its assessment or that, while it had those factors at its disposal, the Commission failed duly to take them into account in such a way as to eliminate all doubt as to the compatibility of the notified measure with the internal market.

In this context, the General Court found that the length of the discussions between the UK and the Commission, the scale of the area of investigation covered by the Commission during the preliminary examination and the circumstances surrounding the adoption of the contested decision are indications that may establish that there were doubts.

What Happens Next?

National Grid (the Capacity Market Delivery Body) in its communication to Capacity Market agreement holders and Capacity Market applicants, has said that:

- a. National Grid is able to continue with activities which do not involve granting state aid, including completing the prequalification process for 2019 in case it is required for future Capacity Market Auctions.
- b. The Department for Business, Energy and Industrial Strategy (BEIS) is doing everything it can to re-obtain state approval from the Commission as soon as possible. The Commission will be required to undertake a formal investigation before providing state aid approval for the Capacity Market, and BEIS will support the Commission's investigation, where required. As part of the process, BEIS will carefully consider whether any changes to the design of the Capacity Market are required.
- c. **It is impossible to say how long it will take the Commission to conclude their formal investigation into the case**, however, BEIS will work closely with the Commission to ensure that state aid for the Capacity Market can be approved as soon as possible.

Will the Next Round of Capacity Market Auctions Go Ahead?

Despite the Secretary of State's instruction to National Grid to postpone indefinitely the upcoming T-4 and T-1 Capacity Market Auctions for Delivery Years 2022/23 and 2019/20, the government is intending to seek separate state aid approval from the Commission to run a one-off "replacement" T-1 Capacity Market Auction. The **postponed T-4 Capacity Market Auction is intended to be run as a T-3 Capacity Market Auction in next year's auction round, subject to the Commission completing its formal investigation and providing state aid approval** for the main Capacity Market scheme.

What Happens if a Capacity Provider Does Not Comply With Their Agreement During the Standstill Period? Will They Still Be Subject to Penalty Payments or Termination Fees?

BEIS is reviewing the judgment, including its implications for capacity providers, and will provide guidance to the Delivery Body as soon as possible.

Further Information for Capacity Agreement Holders

What Applicant Credit Cover for the Postponed T-1 and/or T-4 Capacity Market Auctions and/or for Future Delivery Years Continue to Be Held?

The Delivery Body has confirmed in its communication to Capacity Market agreement holders and Capacity Market applicants that:

- a. All credit cover that is currently being held in relation to the proposed auctions will be returned
- b. Agreement holders may also request the return of credit cover for Capacity Market Agreements arising from past auctions

Will the UK Government Recover Capacity Market Payments Already Made?

The UK government is taking no steps to recover payments at this stage, and hopes that this can be avoided. BEIS will discuss with the Commission the extent to which aid already paid may need to be recovered, as part of the Commission's formal investigation. The final position will need to await the results of the Commission's investigation.

What is the Position for New Build Projects Expecting to Participate in the Upcoming T-4 Capacity Market Auction?

Subject to the Commission completing its formal investigation and providing State Aid approval for the main capacity market scheme, the postponed T-4 Capacity Market Auction will be run as a T-3 Capacity Market Auction in next year's auction round. BEIS appreciates this has the potential to be problematic for certain construction lead times.

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