



# **CFD Independent Auditor**

## Report on CFD Allocation Round 4

29 June 2022

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# 1 Assurance Report

## **ISAE 3000 Independent Assurance Report on Compliance of National Grid Electricity System Operator Limited (NGESO) (as Electricity Market Reform Delivery Body) with selected requirements of the Contracts for Difference (CFD) Allocation Framework for CFD Allocation Round 4.**

To: The Board of Directors of NGESO

### **1.1 Scope**

We have performed assurance work over the extent to which the Delivery Body (DB) has complied with the requirements of the CFD Allocation Framework insofar as they relate to the calculations made by the DB in the allocation process. In particular we have considered the sections of the CFD Allocation Framework listed in Appendix A. The detailed CFD Allocation Framework is available here: [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/1035899/cfd-allocation-round-4-allocation-framework.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1035899/cfd-allocation-round-4-allocation-framework.pdf)

In the context of this Report the calculations of the DB in performing CFD Allocation Round 4 are the "Subject Matter" and the above sections of the CFD Allocation Framework form the "Criteria" against which the Subject Matter has been evaluated.

### **1.2 Respective Responsibilities**

The DB as the Responsible Party is responsible for executing the CFD Allocation Round in accordance with the requirements of the CFD Allocation Framework, including designing and executing such processes and controls required to reduce the likelihood that errors or irregularities will occur and remain undetected.

Our responsibility, as agreed with the DB, is to assess the calculations performed by the DB in executing the CFD Allocation Round against the requirements of the CFD Allocation Framework and to independently express a conclusion as to whether the calculations comply with the requirements of the CFD Allocation Framework. Other than as defined in our assurance procedures, we did not audit or otherwise test or verify the information given to us in the course of our work.

### **1.3 Work Performed**

We conducted our work in accordance with the International Standard on Assurance Engagements 3000 (Revised) "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information". That standard requires that we plan and perform our work to obtain appropriate evidence about the subject matter of the engagement sufficient to support an opinion providing reasonable assurance.

An outline of the work we performed is included in Appendix B. Except to the extent expressly stated, we did not subject the information contained in our Report or given to us by the DB to checking or verification procedures. The procedures we performed were not designed to and are not likely to reveal fraud.

## **1.4 Basis of Opinion**

We believe that our work performed and evidence obtained provides a reasonable basis for our opinion. Our assurance report has been produced under our call-off contract with the Responsible Party dated 1 September 2021.

## **1.5 Opinion**

**In our opinion the calculations performed by NGESO, in its role as the CFD Delivery Body for Electricity Market Reform, have, in all material respects, complied with the relevant sections of the CFD Allocation Framework as referenced in Section 1.1 above in respect of CFD Allocation Round 4.**

## **1.6 Other Matter**

When holding an auction in relation to the Pot Budget following holding one or more Minimum Auctions in relation to the same Pot, the DB determines the budget impact of Qualifying Applications that were successful in the Minima Auction at the higher of the Clearing Price from the Minimum Auction and the overall Pot auction. Whilst this is consistent with the principle that those Qualifying Applications subject to Minimum have first access to the specified part of the budget, paragraph 17.4(b) states that when "assess[ing] the impact on the Monetary Pot ... the Delivery Body must use the Strike Price of the bid under consideration as the provisional clearing price for ...any relevant Qualifying Application(s) already determined to be Successful Application(s) (**including in any relevant Minimum auction(s)**)".

In performing our work we considered whether the DB should have altered the clearing price for those bids that were successful in the Minimum auction. We reviewed correspondence that showed that, during the period of framework drafting and subsequent system development, the DB had sought clarification from BEIS on the purpose of this paragraph and received clarification that this was intended to capture that should a Qualifying Application subject to Minimum be cleared at a *higher* price during the general Pot Auction that the Qualifying Applications from the Minimum Auction should also be cleared at this price. We considered that the DB had sought and received this clarification and that the approach to the calculations adopted by the DB was consistent with this clarification, accordingly our opinion is not qualified with regards to this matter. We would however recommend that the drafting of the Allocation Framework for future rounds be updated to make the intended calculation clear.

## **1.7 Independence**

In conducting our engagement, we have complied with the independence and other ethical requirements of the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants, which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

## **1.8 Quality Control**

Deloitte applies International Standard on Quality Control 1 and accordingly maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

## **1.9 Use of Report**

Our Report has been prepared for the exclusive use of NGESO in accordance with the scope agreed within our call-off contract dated 1 September 2021. Our work has been undertaken solely for the purpose of assessing the DB's compliance with the relevant section of the CFD Allocation Agreement outlined in Section 1.1 above. Our work was not planned or conducted with any other objective in mind and so cannot be relied upon for any other purposes. Save that a copy of our report may be provided to the Secretary of State for Business, Energy and Industrial Strategy (BEIS) and may be published on the BEIS or NGESO website in order to meet the requirement to make publicly available within the CFD Allocation Framework, our Report is not to be used for any other purpose, recited or referred to in any document, copied or made available (in whole or in part) to any other person without our prior written express consent. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than NGESO for this report or for the conclusions we have formed.

A handwritten signature in black ink that reads "Deloitte LLP". The signature is fluid and cursive, with "Deloitte" on the first line and "LLP" on the second line.

Deloitte LLP  
Edinburgh, United Kingdom  
30 June 2022

# 2 Background and Context

## 2.1 Background

The Energy Market Reform (EMR) Programme is intended, *inter alia*, to promote investment in low-carbon electricity generation through a number of mechanisms including Contracts for Difference (CFD) to provide long-term price stabilisation to low carbon plant. EMR has been implemented through the Energy Act 2013 and supporting secondary legislation in particular the Contracts for Difference (Allocation) Regulations 2014 and subsequent amendments.

A CFD is a private law contract between a low-carbon electricity generator and the Low Carbon Contract Company (LCCC), a Government-owned limited liability company. The CFD pays the generator the difference between the 'strike price' – a price for electricity reflecting the cost of investing in a particular low carbon technology – and the 'reference price' – a measure of the average market price for electricity in the GB market. It gives greater certainty and stability of revenues to generators by reducing their exposure to volatile wholesale prices, whilst protecting consumers from paying for support when electricity prices are high. CFDs seek to provide efficient long term support for all forms of low-carbon generation .

In its role as CFD Delivery Body (DB) for Electricity Market Reform, National Grid Electricity System Operator Limited (NGESO) is required to administer a series of allocations of CFD for low-carbon electricity generation, potentially including running one or more auctions if applications for CFDs exceed the budget for the allocation round as set by the Department for Business, Energy and Industrial Strategy (BEIS). The process for performing the Allocation Round, including any necessary auctions, is set out in an Allocation Framework as required by the CFD (Allocation) Regulations.

## 2.2 Requirement for Independent Audit

Regulation 36 of the CFD (Allocation) Regulations requires the DB to obtain an audit of the calculations made by the DB in the allocation process. Under this regulation the Independent Auditor is required to produce a report to the DB which:

- i. sets out whether or not the auditor considers that calculations have been made correctly and accurately; and
- ii. where applicable, identifies any calculations which the auditor considers were not correctly or accurately made and identifies the consequences of those calculations.

Following receipt of the report the DB is required to provide the report to the Secretary of State along with the DB's intention to either proceed or re-run the allocation process and in addition make the report publicly available.

Deloitte has been engaged by NGESO to perform an independent audit by providing a reasonable assurance opinion under the International Standard on Assurance Engagements (ISAE) 3000 in respect of the calculations performed by NGESO, in its role as Delivery Body for EMR, in relation to the CFD Allocation Round 4 in order to

meet the requirements for an audit of the calculations made by it in the allocation process ("a process audit") as set out in the CFD Allocation Regulations Section 36.

Our independent opinion has been prepared under the International Standard on Assurance Engagements (ISAE) 3000, which provides the structure and internationally recognised framework for undertaking the engagement, leading to a formal assurance opinion which is provided in Section 1 of this report.

# Appendix A – In-scope CFD Allocation Framework Sections

The following sections of the CFD Allocation Framework were considered in performing the assurance work:

- 6 Valuation of Applications
- 9 Allocation Process
- 10 Notice of Auction
- 11 Submission of Sealed Bids
- 13 Withdrawal of Applications and sealed bids
- 14 Soft Constraints
- 15 Order of Auctions
- 16 Minimum Auctions
- 17 Auction in relation to Pots or the Overall Budget
- 18 Maxima only auction
- 19 Tiebreaker Rules

# Appendix B – Outline of Work Performed

Table 1: Outline of Work Performed by in-scope Allocation Framework Section

Allocation Framework Section	Testing Approach
<b>6 Valuation of Applications</b>	<p>Test, on a sample basis, the key controls in place in respect of:</p> <ul style="list-style-type: none"> <li>• Testing and approval of software utilised.</li> <li>• Access to the portal used to capture and store applicant data.</li> <li>• Validation of data submitted by applicants.</li> </ul>
<b>6 Valuation of Applications &amp; 9 Allocation Process</b>	<ul style="list-style-type: none"> <li>• Obtain a list of qualifying applications from the DB.</li> <li>• Obtain the inputs to the valuation formulae from the Allocation Framework applicable to the Allocation Round.</li> <li>• Obtain the Allocation Round budget as published by BEIS.</li> <li>• Reapply the valuation formula and confirm that the DB has correctly identified each pot as constrained or unconstrained.</li> </ul>
<b>9 Allocation Process</b>	<p>In the event one or more pots is unconstrained confirm that all Applications for the pot(s) are reported as successful and that the appropriate strike price is associated with each application as required under the applicable Allocation Framework.</p>
<b>10 Notice of Auction</b>	<p>In the event a Budget Revision Notice is issued, confirm any changes to the qualification status of applicants and, as required, reapply the valuation formula. Compare the current valuation to the revised budget and confirm that the DB has correctly identified each pot as constrained or unconstrained.</p> <p>Confirm a notice for auction was issued per the required timetable.</p>
<b>11 Submission of Sealed Bids &amp; 13 Withdrawal of Applications and sealed bids</b>	<p>In the event one or more auctions is required, test, on a sample basis, the controls in place in respect of:</p> <ul style="list-style-type: none"> <li>• Testing and approval of software utilised.</li> <li>• Access to the portal used to capture and store applicant data.</li> <li>• Validation of data submitted by applicants.</li> </ul>

Allocation Framework Section	Testing Approach
<b>14 Soft Constraints, 15 Order of Auctions, 16 Minimum Auctions, 17 Auction in relation to Pots or the Overall Budget, 18 Maxima only auction</b>	<p>In the event one or more auctions is required:</p> <ul style="list-style-type: none"> <li>• Obtain details of sealed bids from the DB, including any flexible bids.</li> <li>• Independently reapply the auction rules, as detailed within the Allocation Framework, and compare the results to the results calculated by the DB. If differences are identified review with the DB and obtain explanations for these differences.</li> <li>• Following completion of any necessary auctions, including any tie-break situations, agree the list of successful qualified applications to the results of the independent recalculation, including capacity, strike price and target delivery year per application.</li> </ul>
<b>19 Tiebreaker Rules</b>	<p>In the event a tie-break occurs within the Auction calculation and there is a requirement to apply a random selection to determine successful qualified applications:</p> <ul style="list-style-type: none"> <li>• Confirm that the population of applications considered was limited to those that should have been considered according to the Allocation Framework;</li> <li>• Confirm the successful qualified application or combination of applications had the lowest randomly assigned number.</li> </ul>

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