

# UK Capacity Market suspended after landmark European General Court ruling

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On 15 November 2018, the European General Court (“EGC”) delivered a decision regarding the EU Commission’s State Aid clearance of the UK’s Capacity Market Scheme.<sup>1</sup>

The EGC concluded that, given the short length and circumstances of the pre-notification phase and the lack of appropriate investigation of certain aspects of the Scheme by the EU Commission (which in turn resulted in a decision which was incomplete and lacked content), the EU Commission cleared the Capacity Market Scheme despite the existence of doubts as to the Scheme’s compatibility with the internal market – in other words the EU Commission should not have reached the decision it did based on the preliminary investigation undertaken rather the circumstances warranted a full investigation.

The EGC has **not** said that the UK Capacity Market Scheme breaches State Aid rules. Rather its decision relates to the process by which the EU Commission reached its conclusion. Essentially the EU Commission has to go back and start the process again and any new assessment may need to involve a formal investigation.

## EU Commission’s Decision – July 2014

In July 2014 the EU Commission concluded that the UK Capacity Market was in line with EU State Aid rules and so was compatible with the internal market.<sup>2</sup> Importantly this was the first time the EU Commission had assessed a capacity market under the Environmental and Energy State Aid Guidelines 2014 (the “**2014 Guidelines**”). The EU Commission at the time noted that, as required by the 2014 Guidelines, the UK had introduced the Capacity Market Scheme following a thorough investigation of its necessity and the potential for alternative measures to contribute to ensuring the security of supply objective. It was further noted that the Capacity Market Scheme would be open to a range of technologies, including demand side response and interconnection. The use of auctions was seen as a way of ensuring the aid granted would be limited to the minimum necessary in a non-discriminatory fashion.

## Consequences of EGC Decision

National Grid ESO (the delivery body of the Capacity Market Scheme in the UK) has suspended indefinitely the T-4 Auction for delivery years 2022/2023 and the T-1 auction for delivery years 2019/2020. All future capacity market payments under existing contracts are suspended. This will affect suppliers holding contracts from 2018 to 2021/2022.

<sup>1</sup> EGC Case T-793/14

<sup>2</sup> EU Commission Decision C(2014) 5083 final of July 23 2014

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At this point we understand that National Grid is not seeking to recover payments previously made under the Capacity Market Scheme, although this cannot be excluded as a possibility going forward if a future State Aid decision holds that the Capacity Market is not compliant with State Aid rules after all. Private third party actions also cannot be ruled out.

The UK government is discussing the decision and options with the EU Commission. Mention has been made as to the possibility of the UK seeking a special exemption to run a near term auction to deal with imminent capacity issues although this is currently unclear.

The EGC decision has rendered the future of the UK Capacity Market Scheme uncertain. Whilst there is nothing to prevent the EU Commission reaching the same conclusion on the compatibility of the measure, there is of course an element of doubt that this will be the case, particularly given the increased public scrutiny now surrounding the issue. Any decision however will inevitably take time – in the meantime participants in the UK electricity market whether generators, interconnectors, battery or storage operators, lenders or funders will no longer receive the capacity market payments that were often a key revenue flow.

However, not only does the EGC's decision raise issues and uncertainty for the UK Capacity Market Scheme it may also call into question the assessments already undertaken by the EU Commission with respect to Irish, Polish, Belgian, Greek and Italian mechanisms, all of which have capacity market decisions which were also all taken without the formal investigation procedure being initiated. The more wide ranging consequences of this EGC decision should not be under-estimated given the potential implications for past and future assessments concerning all mechanisms with state relevance.

White & Case LLP will continue to monitor developments and provide regular updates.

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