

# UPDATE:

# ELECTRICITY GENERATOR LEVY ON LOW CARBON GENERATORS

We reported in November 2022 on the UK Government's plans to introduce a tax on low-carbon power generators from 1 January 2023. We now have more detail on how the tax will work, as the Government has published draft legislation and updated its technical guidance.

## KEY POINTS TO NOTE

- The Benchmark Price of £75/MWh is now indexed to CPI
- The threshold for in-scope generation output is halved from 100GWh to 50GWh per year. It has been changed from the 100GWh proposed in the original Technical Note to reduce the risk that generators exceed the £10m allowance on 100GWh of generation, which could create disincentives to generate around the threshold
- The tax is on revenues actually received by generators for the electricity they generate
- We now have a definition of corporate group: a parent company and its 75% subsidiaries and their 75% subsidiaries
- They are still clarifying the rules on joint ventures and welcome responses to the suggestions made

For background, see our original update, UK Government to introduce the Electricity Generator Levy on low carbon generators

## UPDATE: 20 DECEMBER 2022

The UK Government published further information and draft legislation as promised, on 20 December 2022. All the relevant documents are here <https://www.gov.uk/government/publications/electricity-generator-levy> including draft legislation (which will form part of the next Finance Bill) and an updated Technical Note, which is very useful and explains what the legislation is trying to do.

## GENERATORS COVERED

The levy applies to corporate groups, or standalone companies, that operate assets generating electricity in the UK which are connected to the national transmission network or local distribution networks.

- So not electricity generated and used under a private wire arrangement or "behind the meter" generation that is not exported.
- Electricity imports are not caught, but exports are, if generated by a relevant generating station.

The actual definition of a "relevant" generating station is:

- a. if it generates electricity at a relevant place [the UK, territorial sea of UK or a Renewable Energy Zone] and is not a generating station that mainly generates electricity—
  - i. as a result of the burning of oil, coal or natural gas, or
  - ii. as a result of the use of plant driven by water, where the power is mainly a result
- b. to the extent that is not subject to—
  - i. a contract for difference within the meaning of Chapter 2 of Part 2 of the Energy Act 2013 (contracts for difference),
  - ii. an investment contract within the meaning of Schedule 2 to that Act (investment contracts), or
  - iii. feed-in tariff export payments.

so it is a bit of a negative definition but covers everything except fossil fuel and pumped hydro. So it includes nuclear, biomass and energy from waste plants as well as solar and wind farms.

## WHAT ABOUT CO-LOCATION?

A hybrid site using renewable generation and battery storage will need to:

- Determine the amount of metered output that relates to generation as compared to output that relates to power imported, stored and exported
- Separately determine the amount of receipts of the group that are attributable to that generated output

There will be further detail in HMRC's forthcoming guidance.

## CALCULATING THE LEVY

The levy is applied on 'Extraordinary returns', which are the aggregate revenue that generators make in a qualifying period from in-scope generation on a measure of 'Exceptional Generation Receipts' exceeding £75.00 per MWh and will only then apply to returns over £10 million per group.

Exceptional Generation Receipts are calculated as follows:

### GENERATION RECEIPTS – ELECTRICITY GENERATION X BENCHMARK PRICE - ALLOWABLE COSTS - ALLOWANCE

- **Generation Receipts** = total receipts of a group from in scope UK electricity generation; grid to replace contracted output that is not generated; and
  - **Electricity Generation** = electricity generated in the UK from in scope generation in Megawatt-hours (MWh);
  - **Benchmark Price** = £75.00 per MWh\*;
  - **Allowable costs** = a limited set of exceptional costs such as increased costs of generation fuels, revenue sharing and the costs of buying back electricity from the grid to replace contracted output that is not generated; and
  - **Allowance** = £10m per annum per group.
- \*The Benchmark Price represents the average price above which generator returns are considered to be exceptional so any portion of generators' earnings below this level will not be subject to the EGL. Note that the Benchmark Price is now indexed so will rise/fall in line with the CPI from April 2024.

## HOW TO CALCULATE GENERATION RECEIPTS

The basic approach is that generation receipts are the amounts that a group realises for its relevant generation output from wholesale purchases of that output.

The Technical Note goes into more detail, including on adjustments for things like gains or losses on hedging arrangements.

These are not classed as generation receipts:

- Revenue from or payments for accepted balancing market bids, under which a generator agrees to reduce its output. opted to export on commercial terms will have such export revenue included.
- Renewables Obligation Certificates or Renewable Energy Guarantees of Origin.
- Ofgem-regulated Feed-in Tariff generation and export tariff payments. Note that Feed-in Tariff sites that have opted to export on commercial terms will have such export revenue included.
- Payments not in connection with power provided to the grid, such as ancillary services.
- Capacity Market Payments in the few cases where renewable generators are eligible.

But Balancing System use of services charges will not be available for deduction from generation receipts for the limited time generators are still liable for these during the first quarter of 2023.

### ALLOWABLE COSTS THAT CAN BE DEDUCTED: EXCEPTIONAL FUEL COSTS

Where fuel is used to generate electricity, generators will be able to reduce exceptional generation receipts by a measure of the amount by which generation fuel costs exceed historic levels. This reflects that, for these generators, the benefit of higher electricity prices might be substantially offset by higher generation fuel acquisition costs.

To claim this relief, generators will be required to calculate a baseline fuel cost. This will be the lower of:

- A measure of the generator's fuel costs per MWh calculated over a period of at least twelve months between 1 January 2017 and 1 March 2020. (This will have to be estimated where this is not possible)
- A specified rate of £65 per MWh.

## REVENUE SHARING

For example, paying a third party for access to a source of generation fuel such as landfill waste based on the value of the revenues the generator earns or calculated in proportion to electricity prices.

Generators are not taxed for payments that are based on revenues earned/market electricity prices above the benchmark price.

## WHAT IS A "GROUP"?

The draft legislation defines a group as a principal member (parent company), its 75% subsidiaries and their 75% subsidiaries (and so on).

The Lead Member of the group pays the levy. The lead member is normally the group company that is nominated to pay corporation tax on the group's behalf. Otherwise it is the principal member. The other group companies are jointly and severally liable for the levy.

## JOINT VENTURES – SPECIAL RULES

There are special rules for calculating the EGL liability of a **corporate** JV. Where joint ventures are conducted without a corporate entity in place, the rules for joint ventures set out here will not apply and the participating investors will be treated separately. This includes cases where the joint venture is established as a partnership or a limited liability partnership (LLP).

A corporate JV qualifying for EGL purposes is similar to a JV for corporation tax purposes: five or fewer persons must together have a 75% interest. Members of a group are treated as if they were a single company.

A qualifying JV cannot be a member of a group, unless it is the principal company of its own group. So, if you have a 75% interest in a corporate JV, it is classed as part of your group and taxed for EGL on that basis, not on the basis of the JV rules.

## APPLYING THE SPECIAL RULES

### STEP 1 – TAXATION OF JV

On the same basis as other companies or groups: if the annual output is above 50GWh the JV will be subject to the EGL on exceptional generation receipts above the £10m annual allowance.

### STEP 2 – TAXATION OF JV MEMBERS

Members of at least 10% shareholding are attributed their proportionate share of exceptional generation receipts **within** the £10m allowance.

These attributed amounts will be treated as an addition to exceptional generation receipts of those JV members and will be subject to the EGL insofar as those members' exceptional generation receipts exceed £10m at group-level.

For example, if two investor groups participated in a JV with each owning a 50% share, and the JV earned £25m in exceptional returns, its EGL liability would be £15m after taking into account the £10m allowance. Each investor group would then need to add £5m onto its generation receipts to reflect use of the allowance.

This step is to ensure that each group only benefits from a single £10m allowance in respect of exceptional generation receipts that it receives directly from its own generation activity or indirectly through relevant JV interests.

### STEP 3 – TAXATION OF JV MEMBERS ON RETURNS FROM SELLING OR HEDGING JV OUTPUT

When material JV members (those with a 10% interest or more) realise amounts from selling output of the JV or hedging output of the JV, those amounts will be treated as additions or reductions to the member's exceptional generation receipts.

The Government is discussing whether a JV member can surrender a negative amount to the JV itself. This is not dealt with in the draft legislation. See the updated Technical Note paras 1.86-1.91 (Relief for negative amounts) for more detail.

## NEXT STEPS

The government intends to introduce the draft legislation as part of the next Finance Bill. The draft may be subject to further revision to ensure it will work as intended.

HMRC will issue draft guidance for taxpayers early in 2023. If you have questions about HMRC's expectations of taxpayers, or want to share observations about the draft legislation, you can email them at [egl@hmrc.gov.uk](mailto:egl@hmrc.gov.uk).

The updated Technical Note also requests views on how the policy is delivered in a small number of identified areas such as the special rules for qualifying JVs. These can be shared using the same address [egl@hmrc.gov.uk](mailto:egl@hmrc.gov.uk)

## FOR MORE INFORMATION

Please contact one of us listed below or your usual AG contact.

### RICHARD GOODFELLOW

Head of Infrastructure and Energy  
+44 (0)7775 586409  
[Richard.Goodfellow@addleshawgoddard.com](mailto:Richard.Goodfellow@addleshawgoddard.com)



### STEWART GORDON

Managing Associate  
+44 (0)7919627879  
[Stewart.Gordon@addleshawgoddard.com](mailto:Stewart.Gordon@addleshawgoddard.com)



### ANNA SWEENEY

Principal Knowledge Lawyer  
+44 (0)7590 003081  
[Anna.Sweeney@addleshawgoddard.com](mailto:Anna.Sweeney@addleshawgoddard.com)



 **ADDLESHAW  
GODDARD**

**MORE IMAGINATION MORE IMPACT**