

STOP PRESS: New tax proposals may have major impact on data centre costs

The Government has recently announced, in its White Paper on Electricity Market Reform (EMR), further green taxes that will have, in their own words, a “significant impact” on energy-intensive industries, such as data centres. New electricity regulations may also bring about radical changes to the way electricity is supplied to multi-let facilities.

Key issues include:

- **Higher electricity costs** through the introduction of a Carbon Floor Price.
- **Loss of control** over operators’ ability to recover costs for electricity supplies from end users.
- **Increased bureaucracy** because of a new right for end users to choose their electricity supplier.

This Legal Alert considers the impact of these latest proposals for the data centre industry.

The Carbon Floor Price

Aiming to drive investment in low carbon generation, the proposals set out in the EMR represent the biggest shake-up in the UK electricity market since privatisation in the 1980s. One of the linchpins of the EMR is the introduction of the world’s first Carbon Floor Price (CFP). This could add £3.2 billion to industry’s annual energy bills by 2016, according to Treasury estimates.

The CFP will be introduced through changes to the Climate Change Levy (CCL). This is a tax on the supply of electricity (amongst other things) to non-domestic consumers. The changes to the CCL will mean that each kWh is to be effectively subject to three carbon taxes: the CCL (on supplies to generators), the CCL on the supplies to businesses (as currently) and the CRC Energy Efficiency Scheme (CRC).

The Government has agreed that the CFP should be subject to exemptions for energy-intensive industries. However, there is currently no evidence to suggest this will extend to the data centre industry. Instead, increased costs will need to be considered by both data centre owners and end users.

Right for end users to choose their electricity supplier

Under new regulations laid before Parliament at the end of July, many end users in data centre sites will have the right to ask their operator to use a different electricity supplier. The Government has not yet confirmed when these changes will take effect, although this could be as early as autumn 2011.

The right to request an alternative supplier is intended to increase competition in the electricity industry and may enable end users to take advantage of cheaper energy supplies. Nevertheless, the changes are likely to create many practical and technical problems for data centre operators who will have only limited rights to turn down a valid end user request.

The requirement to provide third party access only applies where the network in question is a “distribution system” within the terms of the legislation. The Government intends to issue guidance on this key concept in due course.

In the main, the cost of creating access for an alternative supplier should fall on the party making the request (i.e the tenant or end user). However, there are significant administrative requirements for operators (particularly in multi-let facilities) which must be managed within strict time frames. In certain cases, these will include obtaining Ofgem approval for the proposed tariff structure.

In addition, the new right could cause problems for data centre operators with long-term energy supply contracts where payments are made to reserve capacity which may no longer be needed and guaranteed minimum quantities of energy are to be supplied subject to penalties if this energy is not used up.

What steps should you take now?

The Government's reform agenda for the electricity industry is wide-ranging. Steps that data centre businesses can take now to ensure they are well prepared for the future changes include:

- Assessing the practical implications of providing third party access to sites (e.g. are additional cables, meters or other equipment needed and, if so, where will these be accommodated?). Operators may need to factor these points into the design of and documentation for new sites.
- Reviewing the terms on which existing suppliers provide electricity (e.g. are there penalties for not meeting minimum purchase requirements?).
- Collating information on the cost of operating the electricity distribution system in order to present and justify any eventual tariff methodology to Ofgem.

- Considering whether a change of electricity supplier will impact on your strategy for buying allowances under the CRC.
- Considering whether any smaller on-site generation or renewables schemes will be affected; some schemes may only be viable where all end users purchase electricity from the same source.
- Ensuring that lease and other documentation contain provisions to give operators advance notice of a request to change electricity supplier and some control over such requests. Operators will also want to review the extent to which cost recovery/apportionment in respect of electricity prices can continue to be made under contractual documentation.

Please contact our market leading data centre group if you require further assistance.

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