EXPLANATORY MEMORANDUM TO

THE CONTRACTS FOR DIFFERENCE (MISCELLANEOUS AMENDMENTS) (NO. 2) REGULATIONS 2025

2025 No. XXXX

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Energy Security and Net Zero and is laid before Parliament by Command of His Majesty.

2. Declaration

2.1 The Rt Hon Ed Miliband MP, Secretary of State at the Department for Energy Security and Net Zero confirms that this Explanatory Memorandum meets the required standard.

2.2 Marc Sherratt, Deputy Director for Renewable Electricity at the Department for Energy Security and Net Zero confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Eleanor Saunders at the Department of Energy Security and Net Zero, email: Biomasselectricitycorrespondence@energysecurity.gov.uk can be contacted with any queries regarding the instrument.

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

4.1 The instrument enables support to be provided to existing biomass generators through a contract for difference ("CFD"). It also allows biomass sustainability obligations in any such CFD to be updated.

4.2 The extent of this instrument (that is, the jurisdictions which the instruments forms part of the law of) is England and Wales, Scotland and Northern Ireland.

4.3 The territorial application of this instrument (that is, where the instrument produces a practical effect) is England and Wales, Scotland and Northern Ireland.

5. Policy Context

What is being done and why?

5.1 To facilitate support for large-scale biomass generators, the amendments made by this instrument make existing biomass generators eligible for CFDs. This will enable the Secretary of State to direct the CFD counterparty to offer a CFD to biomass generators.

5.2 Large-scale biomass generators, converted from coal, can provide reliable and dispatchable power, and currently contribute around 5% of the UK's electricity generation. Existing government support for some large-scale biomass generators under the Renewables Obligation (RO) and CFD schemes ends in 2027, and analysis

shows that they would not have sufficient incentive to continue generating after existing subsidies end. The National Energy System Operator has advised that without large-scale biomass, the UK could face security of supply risks between 2027 and 2031. The alternatives to large-scale biomass generators are limited in the necessary timescales, given their scale and low carbon dispatchability. Therefore, maintaining these plants would increase resilience and support security of supply into the late 2020s to early 2030s.

5.3 Government has confirmed its intention to provide short-term support to large-scale biomass generators through a new low-carbon dispatchable CFD. Under these arrangements, generators would play a much more limited role in the energy system and would be supported to dispatch low-carbon power only when the system, and in turn consumers, really need it. This means they would operate at substantially reduced load factors than historic levels, delivering a secure, value for money power system.

5.4 Unlike the RO, a CFD model enables us to negotiate bespoke terms, for example on contract duration and on strike price, which results in better value for money and alignment with policy objectives. Extending the length of accreditations under the RO would not deliver value for money to the consumer or align with the Government's current objectives and we have no plans to extend the length of accreditations. Since the RO was launched in 2002, the energy landscape has evolved, and the scheme is no longer the option which provides the correct market incentives or value for money.

5.5 The Regulations will also enable the Secretary of State to issue a direction to a CFD counterparty to modify the sustainability obligations in a CFD they had been directed to offer to a biomass generator. This is to enable the government to update a CFD to reflect any significant changes which may arise from wider government sustainability work. The power to update suitability obligations cannot be used to reduce or undermine sustainability obligations.

5.6 Any amendments to the sustainability obligations would be additional to the biomass sustainability criteria the government has committed to include as part of any CFD offered to large-scale biomass generators. These criteria increase the proportion of biomass that must be sustainably sourced from 70% to 100%, reduce the supply chain emission threshold from 55.6 gCO2e/MJ to 36.6 gCO2e/MJ (aligned with the EU Renewable Energy Directive III), and exclude material sourced from primary and old growth forests from receiving support payments. The science underpinning biomass sustainability continues to evolve, and Government will consult separately on developing a strengthened common sustainability framework later this year in 2025.

What was the previous policy, how is this different?

5.7 The previous policy was that biomass generators (other than a combined heat and power generator fuelled by solid biomass) were not eligible for CFDs. This was implemented by the Contracts for Difference (Miscellaneous Amendments) Regulations 2021, which omitted biomass conversion stations from the list of eligible generators. Additionally, under the previous policy, a person was eligible for CFDs only if they intended to establish a generating station, to alter an eligible generating station to increase it's generating capacity by 5 megawatts or more, or to alter an existing generating station to connect to a complete carbon capture and storage system.

5.8 The new policy will allow CFDs to be offered to existing biomass generators that intend to continue to generate electricity. It is consistent with the government's wider strategic approach to the role of biomass set out in the Clean Power 2030 action plan.

Within the action plan, the government recognises the role of biomass in providing low-carbon, firm and flexible power to support the country's clean power ambitions.

5.9 The power to direct a CFD counterparty to update sustainability obligations is similar to the existing power for the Secretary of State to require a CFD counterparty to amend the sustainability obligations in a CFD. However, while the existing power is limited to revisions to the standard terms for CFDs, this amendment creates a similar power, that is not dependent on revisions to the standard terms. This means the Secretary of State can instruct a CFD counterparty to update the sustainability obligations in a previously agreed contract with a biomass generator, without having to revise the standard terms for all CFDs. This would enable Government to reflect any bespoke updates from the Biomass Sustainability Common Framework and to introduce further sustainability measures specific to biomass generators that are aligned with the latest evidence.

6. Legislative and Legal Context

How has the law changed?

6.1 Section 10 of the Energy Act 2013 allows the Secretary of State to direct a CFD Counterparty to offer a CFD to a generator in terms specified in the notice. The Low Carbon Contracts Company, ("LCCC") has been designated as the CFD Counterparty. A CFD can only be offered to an "eligible generator". That is defined in regulation 3 of the Contracts for Difference (Definition of Eligible Generator) Regulations 2014, which defines an eligible generator as a person who intends to carry out a generating activity in relation to an eligible generating station. This instrument expands the scope of who is an eligible generator in two respects. Firstly, the list of eligible generating stations is amended to include a biomass station, meaning a generating station which is fuelled by solid biomass. Secondly, the definition of "carry out a generating activity" is amended so that it includes an existing biomass station continuing to generate electricity.

6.2 CFDs may be entered into on standard terms, following an offer under section 14 of the Energy Act 2013. Those standard terms may be revised under section 11, including any sustainability obligations. Where sustainability obligations in the standard terms are revised, the Secretary of State may by notice require the CFD counterparty to make equivalent amendments to the sustainability obligations in an existing CFD. The power to require the CFD counterparty to do so is in regulation 18 of the Electricity Market Reform (General) Regulations 2014.

6.3 This instrument adds to the Electricity Market Reform (General) Regulations 2014 a similar power to require a CFD counterparty to amend sustainability obligations in existing CFDs entered into by virtue of a direction under section 10 of the Energy Act 2013. The power does not rely on any amendment to the standard terms. The power includes the safeguard that it may not be used where, in the opinion of the Secretary of State, the amendments would reduce or undermine the sustainability obligations in the relevant CFD.

Why was this approach taken to change the law?

6.4 This is the only possible approach to make the necessary changes.

7. Consultation

Summary of consultation outcome and methodology

7.1 Government consulted for six-weeks between 18 January and 29 February 2024 on a potential transitional support mechanism for large-scale biomass generators, ahead of potential contracts under the power BECCS business model.[1] The consultation was published on gov.uk. The consultation sought views on whether a mechanism was warranted and its potential design, including eligibility criteria, such as the 100MW+ threshold, and approach to sustainability criteria. It set out four delivery models: unconstrained CFD, CFD with a generation collar, availability payment, and a regulated margin model. The consultation also sought views on potential areas of legislative amendments to enable the proposed policy intent. The consultation was shared with the devolved administrations as part of this consultation process.

7.2 We received approximately 2150 responses. Approximately 2050 of these appeared to be part of a campaign led by Biofuelwatch, an advocacy group which, as part of its work, raises awareness of the negative impacts they perceive to come from industrial biomass. The consultation asked if the Government should intervene to create a support mechanism to help large-scale biomass generators transition to power BECCS.[2] Most responses rejected the need for such a mechanism, many of those because they disagreed that biomass generation is low carbon. This argument was the central focus of the campaign response, and specific responses from environmental organisations and private individuals. Concerns were also raised about the emissions associated with the transportation of wood pellets. Some respondents questioned the viability of power BECCS.

7.3 Conversely, generators and trade bodies contended that without such support, achieving carbon budgets and net zero targets, protecting jobs and ensuring operational assets remain viable, will be extremely difficult. A few respondents argued that the biomass market predominantly operates on long-term contracts, rather than short-term. They emphasised the necessity of transitional support to sustain supply chains and infrastructure, such as port capacity, ahead of transition to power BECCS. Responses from some small-scale generators (below 100MW) generally supported the concept of a transition mechanism overall but argued that they should be included as their existing Renewables Obligation support is also ending from 2027. The 100MW eligibility threshold is not specified in this instrument, but Government has confirmed its minded-to position to maintain it as part of the eligibility criteria for accessing the proposed support mechanism. This ensures any short-term support targets those low carbon generators best able to provide a significant contribution to security of supply within a constrained timeframe, helping the UK on its decarbonisation pathway through the provision of clean power. This also retains the option of future large-scale power BECCS.

7.4 The consultation also included consideration of proposed legislative amendments which could be necessary to implement the policy. Most respondents opposed the

[1] Consultation on a transitional support mechanism for large-scale biomass electricity generators, January 2024 https://www.gov.uk/government/consultations/transitional-support-mechanism-for-large-scale-biomass-electricity-generators

[2] Power BECCS (bio energy with carbon capture and storage) is the process of generating electricity using sustainable biomass feedstocks, then capturing and permanently storing the CO2 generated in the process. The process removes CO2 from the atmosphere, generating 'negative emissions' which are also known as 'Greenhouse Gas Removals' (GGRs).

changes, based on their wider rejection of biomass as low carbon. Some expressed concern about insufficient monitoring of eligible generators' transition to power BECCS, arguing that there needed to be an obligation to transition. In addition, a smaller group argued against including existing generators within the definition of eligible generators either because this would be preferential treatment or because the eligibility criteria were not yet finalised. A few suggested requiring UK-sourced timber. Some respondents favoured the proposed amendment to the definition of an eligible generator, emphasising cost-effectiveness for existing generators. Others raised broader points outside the scope of the proposed legislative changes, such as pricing carbon certificates appropriately and issuing contracts at site or unit levels for parties with multiple units on one site.

7.5 The Department is setting up an independent review to consider how options for greenhouse gas removal, including large-scale power BECCS and direct air carbon capture and storage, can assist the UK in meeting its Net Zero targets, and ensuring security of supply, out to 2050. Further details of the review will be shared in due course. Furthermore, we note that the majority of biomass imported is a byproduct of the wider US timber industry. Biomass is imported as the UK does not have sufficient forest capacity to meet demand. Sourcing internationally, where there is much greater sustainable biomass supply, is a commercial decision for generators.

7.6 Further detail on the consultation and responses are available in the Government Response published on gov.uk.[3]

8. Applicable Guidance

No guidance is necessary regarding this instrument.

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

9.1 There is no separate Impact Assessment for this instrument.

9.2 However, an impact assessment on the general policy was completed for the policy consultation in 2024.[4] Further updates to the impact assessment will be made ahead of any exercise of the power to direct the CFD counterparty to offer a CFD to a biomass generator.

Impact on businesses, charities and voluntary bodies

9.3 There is no direct, or no direct significant, impact on business, charities or voluntary bodies. The Regulations allow for support through CFDs to be provided to biomass generators, which have impacts on businesses. That is because payments made to generators under CFDs are ultimately funded by electricity consumers, including businesses. This cost would be attributable to any CFD offered to biomass generators rather than this enabling legislation.

[3] Government response to the consultation on a transitional support mechanism for large-scale biomass electricity generators, February 2025. https://www.gov.uk/government/consultations/transitional-support-mechanism-for-large-scale-biomass-electricity-generators/outcome/transitional-support-mechanism-for-large-scale-biomass-generators-government-response-html

[4] Impact assessment for biomass power transitional options, January 2024. https://assets.publishing.service.gov.uk/media/65a8175694c997000daeb995/transitional-support-mechanism-large-scale-biomass-generators-impact-assessment.pdf

9.4 The Regulations do not directly impact small or micro businesses. For the reasons described in the above paragraph, were a CFD provided to a biomass generator, that would have an impact on electricity users including small or micro businesses. The magnitude of these impacts is expected to be smaller for small and micro businesses compared to businesses on average given the current arrangements for funding of electricity consumer-funded subsidy schemes.

9.5 There is no, or no significant, impact on the public sector.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

10.1 This legislation makes minor amendments to the wider existing CFD legislation. We will therefore monitor the impact of this SI as part of wider reviews of the CFD framework. Furthermore, we are considering the recommendations from the National Audit Office report on Monitoring, Reporting and Verification (MRV) and assurance. Work is underway in government, together with Ofgem, to evaluate the current assurance arrangements on biomass sustainability for large-scale generators to ensure it continues to be suitably robust. We will be reviewing the outcome of that work alongside research being undertaken as part of preparations for the Biomass Sustainability Common Framework and will use this to enhance the MRV arrangements in any contracts awarded under the mechanism.

10.2 The instrument does not include a statutory review clause. This instrument makes provision in connection with the provision of financial assistance by or on behalf of a public authority and therefore falls within the exception in section 28(3)(c) of the Small Business, Enterprise and Employment Act 2015.

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

11.1 None.

12. European Convention on Human Rights

12.1 The Secretary of State for Energy Security and Net Zero has made the following statement regarding Human Rights:

"In my view the provisions of the Contracts for Difference (Miscellaneous Amendments) (No. 2) Regulations 2025 are compatible with the Convention rights."

13. The Relevant European Union Acts

13.1 This instrument is not made under the European Union (Withdrawal) Act 2018, the European Union (Future Relationship) Act 2020 or the Retained EU Law (Revocation and Reform) Act 2023 ("relevant European Union Acts").