EXPLANATORY MEMORANDUM TO

THE CONTRACTS FOR DIFFERENCE (MISCELLANEOUS AMENDMENTS) REGULATIONS 2022

2022 No. [XXXX]

1. Introduction

1.1 This explanatory memorandum has been prepared by Department for Business, Energy and Industrial Strategy and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 These Regulations amend the Contracts for Difference (Definition of Eligible Generator) Regulations 2014 (S.I. 2014/2010) ("Eligible Generator Regulations") and the Contracts for Difference (Allocation) Regulations 2014 (S.I. 2014/2011) ("Allocation Regulations").

2.2 Part 2 amends the Eligible Generator Regulations by adding words to the definition of a "complete CCS system" to contemplate non-pipeline transport methods. Part 2 also widens the criteria for carrying out a generating activity to include altering an existing generating station into a generating station connected to a complete CCS system.

2.3 Part 3 amends the Allocation Regulations so that contracts which do not specify a strike price and a reference price can be contemplated. The references to a "strike price" and a "reference price" are retained, however by amending the language to state that a "strike price" and "reference price" may be included, an alternative payment mechanism which does not use these terms can be used.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None

4. Extent and Territorial Application

4.1 The extent of this instrument, apart from regulation 3(2) is to the United Kingdom. The extent of regulation 3(2) is to England and Wales and Scotland only.

4.2 The territorial application of this instrument is to the United Kingdom other than regulation 3(2) which applies only to England and Wales and Scotland.

5. European Convention on Human Rights

5.1 Greg Hands MP has made the following statement regarding Human Rights:

"In my view the provisions of the Contracts for Difference (Miscellaneous Amendments) Regulations 2022 are compatible with the Convention rights."

6. Legislative Context

6.1 The Act set out that the Secretary of State may for the purpose of encouraging low carbon electricity generation make regulations about contracts for difference between a CFD Counterparty and an eligible generator.

6.2 This instrument needs to be read alongside the Eligible Generator Regulations and Allocation Regulations which it amends.

7. Policy background

What is being done and why?

7.1 In November 2020, the Prime Minister's Ten Point Plan set out government's ambition to have a Carbon Capture and Storage (CCS) sector with an operational capability of capturing 10 $MtCO_2$ per year by 2030. In the Energy White Paper 2020, government committed to use consumer subsidies to support construction of at least one Power CCS plant to be operational by 2030. The Dispatchable Power Agreement (DPA), which is in the process of being finalised, is a Power CCS business model intended to implement this commitment.

7.2 Power CCS, including both new build and retrofit projects, is intended to be brought forward as part of Phase-2 of a wider Cluster Sequencing Process which is intended to establish CCUS Clusters made up of a Transport and Storage (T&S) Network and connected CCS projects such as Power CCS, Industrial CCS and Hydrogen CCS. Power CCS projects selected as part of this process are intended to enter into a DPA.

7.3 The deadline for applications under Phase-2 of the Cluster Sequencing Process was 21 January 2022, and government is currently in the process of assessing the applications it received. This instrument has been laid in preparation for the outcome of Phase-2, to ensure that the DPA can be entered into with any successful Power CCS applicants.

7.4 The Act set out that the Secretary of State may for the purpose of encouraging low carbon electricity generation make regulations about contracts for difference between a CFD Counterparty and an eligible generator. Following the 2020 Energy White Paper, a business model for Power CCS has been designed to encourage low carbon electricity generation.

7.5 The DPA is intended to be entered into under section 10 the Act. Section 10 permits the Secretary of State to direct a CFD counterparty to offer to contract with a person specified in the direction, on terms specified in the direction. A person may be specified in such a direction only if that person is an "eligible generator".

7.6 The Eligible Generator Regulations set out what is meant by an "eligible generator" for the purposes of this direction, and this definition includes a person who intends to establish an eligible generating station, such as a generating station connected to a complete CCS system.

7.7 Part 2 of this instrument intends to amend the Eligible Generator Regulations in order to ensure that a person can be an "eligible generator" if they are altering an existing generating station into a generating station connected to a complete CCS system. This is necessary to enable the Secretary of State to direct a CFD counterparty to enter into a DPA with a person who intends to retrofit an existing natural gas fuelled power station to fit CCUS technology onto it and connect it to a complete CCS system.

7.8 Part 2 of this instrument also adds words to the definition of a "complete CCS system" to contemplate non-pipeline transport methods. Non-pipeline transport involves transporting carbon dioxide from a CCS project to a T&S Network by a means other than a pipeline directly connecting the project to the network, this could include transport by road, rail or ship, and the language in the instrument has been left open to allow for different possible configurations. Non-pipeline transport is essential to ensure that CCS is an option to decarbonise projects which are not located directly within a CCUS cluster and cannot connect to the CCS cluster's CO2 pipeline.

7.9 The Contracts for Difference which have previously been entered into under the Act have involved a difference payment between the wholesale electricity price and an agreed strike price. Following responses to a government consultation on CCS business models in 2019, the DPA has been designed with a different payment mechanism. The proposed DPA will consist of two payments: an availability payment for low carbon generation capacity and a variable payment to adjust the position of the Power CCS plant in the merit order relative to an unabated reference plant. The combination of these payments will incentivise availability and enable a plant to operate flexibly, dispatching low carbon electricity to meet the energy market's needs.

7.10 Part 3 of this instrument amends the Allocation Regulations so that contracts which do not specify a strike price and a reference price can be contemplated. In these amendments references to a "strike price" and a "reference price" are retained and the provision will continue to apply as before to contracts which contain these terms, however the language has been amended to accommodate situations in which a contract does not include a strike price and a reference price.

Explanations

What did any law do before the changes to be made by this instrument?

7.11 Before any changes to be made by this instrument, the Eligible Generator Regulations did not explicitly refer to non-pipeline transport in the definition of a complete CCS system.

7.12 The Eligible Generator Regulations also did not explicitly consider a person to be carrying out a generating activity if they were retrofitting a generating station with carbon capture equipment (i.e. altering a generating station to become a generating station connected to a complete CCS system).

7.13 Before any changes to be made by this instrument the Allocation Regulations presumed that a strike price and a reference price would always be included in direct award contract for difference..

Why is it being changed?

7.14 The Eligible Generator Regulations are being changed to explicitly include non-pipeline transport in the definition of a complete CCS system to allow for the decarbonisation of generating stations which require non-pipeline transport to utilise CCS. Although the Eligible Generator Regulations did not previously explicitly require that carbon dioxide was transported a pipeline, the addition language explicitly referring to non-pipeline transport is perceived as helpful by stakeholders. This offers greater opportunities to utilise power CCUS to decarbonise the electricity system.

7.15 The Eligible Generator Regulations are also being changed to explicitly allow a person to be an eligible generator if they are retrofitting a generating station into a

generating station connected to a complete CCS system. This is to ensure that existing generating stations on the electricity system have a route to decarbonisation through CCUS, which offers greater opportunities to utilise Power CCUS to decarbonise the electricity system.

7.16 The Allocation Regulations are being changed to ensure that there is no presumption of a strike price and a reference price in direct award contracts for difference. This allows for the DPA payment mechanism and future proofs this regulation for other potential future revenue support contracts which do not include these payment and terms, and so allows the government to design business models more suited to the strategic aims of Power CCUS.

What will it now do?

7.17 The Eligible Generator Regulations will explicitly include non-pipeline transport in the definition of a complete CCS system.

7.18 The Eligible Generator Regulations will explicitly allow a person to be an eligible generator if they are retrofitting a generating station into a generating station connected to a complete CCS system.

7.19 The Allocation Regulations are being changed to ensure that contracts which do not include a strike price and a reference price are contemplated in the Allocation Regulations.

8. European Union Withdrawal and Future Relationship

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act

9. Consolidation

9.1 The government does not intend to consolidate this instrument with existing legislation at this time.

10. Consultation outcome

10.1 The policy set out in this instrument was subject to a 7-week consultation. Carbon capture, usage and storage: amendments to Contracts for Difference regulations was published in July 2021 for stakeholders to provide feedback. This built on extensive, earlier publications on the DPA business model and principles of power CCUS.

10.2 16 responses were received to the July consultation. Over half of these responses were from businesses and organisations, including large multinationals and SMEs, directly involved in Power CCS. The remainder came from trade associations, non-governmental organisations and other interested parties.

10.3 Most respondents were supportive of the proposed amendment to the definition to include retrofit Power CCS projects alongside new build Power CCS projects.

10.4 Most respondents were supportive of the proposed wording change to allow for the payment mechanism under the DPA.

10.5 Many of the respondents were content that the current definition of a complete CCS system was inclusive enough of non-pipeline transport but were not opposed to an expansion of the definition to provide clarification if BEIS felt this was warranted.

10.6 A more detailed analysis of the consultation responses and outcome can be found in the Government Response to the consultation.

11. Guidance

11.1 The Government Response to the consultation informing this has been published. The Government Response sets out the views of stakeholders in response to the previously proposed policy positions and an explanation of the final policy decisions taken.

12. Impact

12.1 This legislation has little to no impact on business. The legislation applies to businesses seeking to apply for a DPA in respect of an eligible generating station. Applying for a DPA will be voluntary. There is no impact on charities or voluntary bodies.

12.2 There is no substantial impact on the public sector. The impact on the public sector is any change to the cost borne by Government in delivering their functions associated with the Dispatchable Power Agreement.

12.3 An Impact Assessment has not been prepared for this instrument because there is no, or no significant, impact on the public sector. The impact on the public sector is any change to the cost borne by Government in delivering their functions associated with the Dispatchable Power Agreement.

13. Regulating small business

13.1 The legislation does not apply to activities that are undertaken by small businesses.

14. Monitoring and review

14.1 Section 5(4) of the Energy Act 2013 requires the Secretary of State to, before 31st December each year, prepare and lay before Parliament a report setting out how he has carried out his functions under Part 2 of that Act (which includes the powers intended to be used to establish the DPA scheme).

15. Contact

15.1 Natasha Beedell at the Department for Business, Energy and Industrial Strategy Telephone: 07342085167 or email: natasha.beedell2@beis.gov.uk can be contacted with any queries regarding the instrument.

15.2 Chris Thackeray, Deputy Director for Power Carbon Capture, Usage & Storage, at the Department for Business, Energy and Industrial Strategy] can confirm that this Explanatory Memorandum meets the required standard.

15.3 Greg Hands MP at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.