EXPLANATORY MEMORANDUM TO

THE CONTRACTS FOR DIFFERENCE (MISCELLANEOUS AMENDMENTS) REGULATIONS 2024

2024 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 Minister Michael Shanks, Parliamentary Under Secretary of State at the Department for Energy Security and Net Zero (Minister for Energy) confirms that this Explanatory Memorandum meets the required standard.

2.2 Sarah Redwood, Director for Renewable Electricity, at the Department of Energy Security and Net Zero confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Naomi Potter at Department of Energy Security and Net Zero (contractsfordifference@energysecurity.gov.uk; +44 20 7215 4018) can be contacted with any queries regarding the instrument

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

4.1 These Regulations amend two statutory instruments made under the Energy Act 2013 relating to Contracts for Difference (CfDs).

4.2 They amend the Contracts for Difference (Allocation) Regulations 2014 (referred to as the "Allocation Regulations") and the Contracts for Difference (Definition of Eligible Generator) Regulations 2014 (referred to as the "Eligible Generator Regulations").

4.3 The purpose of the amendments are to:

(i) Extend the existing phased CfD policy to floating offshore wind projects to allow the option for floating offshore wind projects within the same Crown Estate seabed lease area can be built in up to three phases, with each phase being party to its own CfD agreement.

(ii) Permit repowering renewable electricity projects to apply for a CfD. Repowering involves the decommissioning of existing electricity generation assets, and then replacing some or all of them· This amendment will enable repowering to be eligible for a CfD, subject to further eligibility criteria.

4.4 These amendments are made in support of policy changes to the CfD, outlined in this document, which are expected to be implemented at the opening of Allocation Round 7 in 2025.

Where does the legislation extend to, and apply?

4.5 The territorial extent of each amendment made by this instrument (that is, the jurisdiction(s) which the instrument forms part of the law of) is the same as that of the provision amended. The territorial application of each amendment made by this instrument (that is, where the instrument produces a practical effect) is the same as that of the provision amended.

4.6 The territorial extent of amendments to the Allocation Regulations made by this instrument is England and Wales and Scotland. The territorial application of amendments to the Allocation Regulations made by this instrument is England and Wales and Scotland.

4.7 The territorial extent of amendments to the Eligible Generator Regulations made by this instrument is the United Kingdom. The territorial application of amendments to the Eligible Generator Regulations is the United Kingdom.

5. Policy Context

5.1 The CfD scheme is the government's main mechanism for supporting new low-carbon electricity generation projects in Great Britain. It guarantees a set price per MWh of electricity for 15 years, indexed to inflation. CfDs are currently awarded on an annual basis via allocation rounds.

5.2 The income stabilisation that it provides for the generator, makes projects that have high up-front costs but long lifetimes and low running costs attractive to investors and lenders, reducing cost of capital and overall project cost. It also protects consumers when electricity prices are high.

5.3 Secretary of State, Ed Miliband, has agreed to implementing two legislative changes for the next allocation round to improve the operation of the CfD scheme and facilitate the achievement of the rapid scale-up of renewable electricity capacity targeted by the government.

Extending phasing for floating offshore wind

5.4 The Government has committed to radically increasing the UK's offshore wind capacity, including floating offshore wind.

5.5 As an emerging technology with only c.200 megawatts (MW) of capacity deployed worldwide to date[1], the floating offshore wind construction process is yet to be industrialised. Several factors are likely to result in a slower buildout rate for the technology, compared to established fixed-bottom offshore wind, including limitations on suitable port capacity and increased sensitivity to adverse weather conditions.

5.6 CfD phasing policy, allowing projects to be built in multiple stages, was designed to provide support for early fixed-bottom offshore wind projects by mirroring as closely as possible the commercial realities of constructing those projects. Extending this policy to floating offshore wind projects will allow more realistic timelines for developers and ensure more certainty and confidence in the wider supply chains. In turn, this will reduce investment risk as investors will have more confidence in projects completing.

5.7 Our amendments will expand the existing phasing policy to floating offshore wind projects. To do this we will delete limb (a) in regulation 27ZA (4) of the Allocation

[1] Source: RenewableUK EnergyPulse - https://www.renewableuk.com/energypulse/about/

Regulations which states that "Floating Offshore Wind is not a phased offshore wind CFD unit".

5.8 There are specific rules in the Allocation Regulations which are deliberately designed to prevent applicants submitting one bid to develop several different projects. This approach avoids developers receiving the same strike price for a single, very large project which would usually apply as multiple projects across different years. The rules are:

(i) That the unit generates electricity using wind; is (or is to be) situated wholly in offshore waters;

(ii) That it is to be established or altered by two or three phases of construction;

(iii) That each phase of construction is to provide new generating capacity;

(iv) That each phase of construction provides a generating capacity of more than 500 MW.

5.9 There are also requirements in the Allocation Framework which must be satisfied for a CfD unit to qualify for phasing. These include:

(i) The completed unit will have capacity of no more than 1500 MW;

(ii) 25% of construction will be completed in the first phase;

(iii) The first phase is targeted to complete by 31 March in the last applicable delivery year (i.e. the year when a project can start receiving payments under its CfD contract);

(iv) The date by which the project is aiming to commence operation of the final phase is no later than 2 years after the first phase commences operation.

5.10 We plan to extend the same phasing rules as outlined in 5.8 and 5.9 to floating offshore wind. However, to ensure we stay sensitive to market and technology developments, we will review the combined requirements and the upper capacity limit for future allocations.

Better enable repowering under the CfD

5.11 The United Kingdom (UK) has ambitious net zero targets, including a mission to achieve clean power by 2030. Our analysis2 suggests that there is approximately 2 GW total renewable capacity coming to the end of its operating life between 2027 and 2030. Breaking this down further, the Government estimates that 75% of this capacity (c.1.3 GW) will be onshore wind, with a further c.400 MW being from landfill gas, and c.300 MW from other technologies.

5.12 Generation assets have a fixed operating lifespan (usually 25 - 35 years). At the end of this lifespan, asset owners have several routes. They could, a) terminate/decommission the asset, b) carry out a short-term life extension of the asset by upgrading some components, or c) fully repower the asset. This policy change relates to the latter option, which involves significant decommissioning of the existing site in order to commission new generating assets on site.

5.13 CfD support for repowering assists with the ambition to achieve clean power by 2030 as repowering can help ensure renewable generation capacity is not lost from older projects. In most scenarios, repowering is likely to be preferable to the counter-factual of losing capacity. Repowering also provides an opportunity to increase the renewable

[2] Internal DESNZ data on Renewables Obligation projects. Does not include potential merchant projects approaching end of operating lifetime. End of life estimates based on known project start dates and Generation Cost report assumptions on technology operating lifetimes.

generation capacities of existing sites through improvements in technology and more efficient use of the site.

5.14 Although repowered projects may have more learnings and reusable infrastructure than a completely new project, there is often still very high upfront capital costs for most technology types. Given this, the CfD remains a crucial mechanism for repowered projects. Importantly, these projects also enhance the efficiency of existing sites/assets, thereby playing a pivotal role in the UK efforts to meet its net-zero emissions target by 2050 using its current renewable energy assets.

5.15 However, intervention via the CfD must, alongside other considerations, ensure a balance between decarbonisation, consumer value for money and security of supply. It is possible that there may be technologies able to repower on a merchant basis without need for CfD support due to their lower upfront costs. There is also a risk that repowering support could incentivise existing generating stations to decommission early to obtain CfD support rather than to continue operating a station sustainably. Repowering support via the CfD therefore needs to incentivise projects to prioritise innovation and site optimisation with restrictions in place to help avoid suboptimal, inefficient policy outcomes, potentially leading to additional and avoidable costs to consumers.

5.16 To ensure that repowering applications meet the business case for CfD intervention, and to prevent perverse incentives, the Government has therefore taken a least regrets approach to supporting repowering, having regard to the following criteria:

(i) Technologies must already be eligible for the CfD scheme;

(ii) There is an available pipeline to repower in the applicable Allocation Round.

(iii) Projects must have at least reached the end of their operating life by/before the Delivery Years3 in the applicable Allocation Round.

(iv) Projects must satisfy the fundamental case for market intervention via the CfD, including high upfront capital costs.

5.17 These criteria will help enable us to protect the consumer, ensure we are intervening only when and where needed and will help provide greater assurance as to the cost-effectiveness of the repowering policy.

5.18 Following careful evaluation and public consultation (see section 7), DESNZ considers that only onshore wind assets satisfy all the above criteria for the next allocation round. Our proposed approach is to keep the eligibility of other technologies for repowering under review for future contract allocations.

5.19 Specific eligibility requirements will be set out in the CfD scheme's Allocation Framework for each Allocation Round where appropriate. However, secondary legislation is necessary to clearly establish that certain repowered projects (which involve partial decommissioning of the eligible generating station) are eligible, in principle, to apply for the CfD (subject to further eligibility criteria set out in the Allocation Framework).

5.20 To enable full repowering we will amend the scope of regulation 14 in the Allocation Regulations (which outlines excluded applications to the CfD) through the insertion of regulation 14ZA (see paragraph 6.7). This amendment ensures that repowering applications, are not in principle excluded from a CfD due to the prior project having received subsidy.

[3] Each Allocation Round sets out delivery years for when projects must begin generating. For example, the delivery years for AR6 were 2026/2027 and 2027/2028 for Pot 1.

5.21 We have also updated the Eligible Generator Regulations by amending regulation 3 (definition of eligible generator). This amendment allows a developer whose repowering activities involve partial decommissioning, rather than fully decommissioning and establishing a new "eligible generating station" (defined in regulation 3(5) of the Eligible Generator Regulations), to fall within the definition of "an eligible generator" and therefore able to be party to a CfD.

5.22 Further, the amendments aim to enable forward bidding of the CfD for repowering projects. Forward bidding refers to the ability of a repowering project to apply for a CfD on the same site as a pre-existing project, without requiring that pre-existing project to have first decommissioned. Forward bidding also ensures parity between repowering projects and new build projects by ensuring that repowering projects can have the commercial certainty of a CfD and can therefore begin construction without having to wait for the prior project to have decommissioned. This reduces development time and the duration in which the site is not generating.

6. Legislative and Legal Context

Justification for approach to changing the law

6.1 The Allocation Regulations only allow fixed-base offshore wind projects to be established/altered in phases of construction. To extend the phasing option to floating offshore wind (where the definition of floating offshore wind specifically states it cannot be a phased project), the only possible approach was to make the proposed regulatory changes.

6.2 The current CfD regulatory framework is not designed with the intention of enabling support of repowered assets. While the detail of the eligibility criteria for repowering applications can be outlined in the Allocation Framework, secondary legislation was necessary to clearly establish that certain repowered assets are eligible for the CfD. This approach was also required to remove regulatory restrictions on applications to repower, and to outline the obligations to be imposed on the delivery body, LCCC and Ofgem in terms of assessing eligibility.

Extending phasing for floating offshore wind

6.3 Under regulation 2(1) of the Allocation Regulations, fixed-bottom offshore wind CfD units can be built in multiple stages. This regulation outlines the definition and requirements of a 'phased offshore wind CfD unit', including that it should be completed in a maximum of three phases of construction and that each phase of construction must provide new generating capacity.

6.4 Regulation 27ZA of the Allocation Regulations specifically excludes floating offshore wind assets from being 'phased offshore wind CfD units'. These regulations amend regulation 27ZA to remove this exclusion, allowing floating offshore wind CfD units to be constructed in accordance with phasing rules.

Better enable repowering under the CfD

6.5 The CfD scheme did not previously have a formal policy in relation to repowering applications. As such, the eligibility of repowering applications was unclear in the legislation. In particular, some repowering activities were not within the scope of regulation 3 of the Eligible Generator Regulations which defines an 'eligible generator', and so would not be eligible to apply for a CfD. For example, there are scenarios where an existing site is partially decommissioned, and it is not clear that a repowered generator is a separately established generating asset.

6.6 In addition, the CfD regulatory framework had potential barriers to repowering applications and forward bidding. Regulation 14 of the Allocation Regulations, specifically regulations 14(5), 14(9), 14(10) and 14(13), could have excluded repowering applications where there was a continuity between the previous generating station on the site and the repowered generating station.

6.7 The amendments contained in these regulations ensure that a generator who repowers an eligible generating station can, in principle, and subject to further requirements, be an eligible generator and so party to a CfD. The amendments also ensure that the exclusions contained in regulation 14 of the Allocation Regulations no longer block the possibility of repowering applications and that forward bidding is possible: allowing repowered projects to apply for a CfD prior to the pre-existing project on the site being decommissioned.

6.8 The risk of gaming resulting from these amendments has also been considered. Eligibility requirements set out in the CfD's Allocation Framework, associated application checks set out in Schedule 5 of the Allocation Framework, and contractual checks in the CfD Standard Terms and Conditions will help ensure that CfD support will only be awarded for projects that can evidence that they will repower and generate renewable electricity. Further, Regulation 14(12) of the Allocation Regulations, continues to apply to all cases to ensure that the CfD unit will be metered separately from other electricity generation.

7. Consultation

Summary of consultation outcome and methodology

7.1 The consultation for these policy and legislative changes sought views and supporting evidence on a range of specific changes proposed for Allocation Round 7. It opened on 11 January 2024 and closed on 7 March 2024.

7.2 The Government welcomed responses from anyone with an interest in the policy area. We noted that the consultation would be of particular interest to: those considering the development of new renewable energy projects in Great Britain, electricity traders and suppliers, businesses operating in the offshore wind sector, and consumer and environmental groups with an interest in the electricity sector.

7.3 The government response to the consultation, detailing all findings and outcomes, was published in October 2024.

Extending phasing for floating offshore wind

7.4 Questions for this topic area sought views on whether respondents felt that phasing policy should be extended to floating offshore wind. It also asked for views on the potential impact of this extension as well as on the existing rules for fixed-bottom offshore wind and whether these should be changed for floating offshore wind.

7.5 36 of 37 responses which addressed floating offshore wind agreed with the proposal to extend phasing to the technology in Allocation Round 7. Key themes in the responses included the need to de-risk projects, shorter weather windows for the construction of FLOW, the success of the phasing policy for fixed-bottom offshore wind and the critical stage of development for FLOW.

7.6 The one respondent who disagreed, said phasing should be introduced from Allocation Round 9 to allow the opportunity for test and demonstration sites – which are planning to participate in Allocation Round 7 and Allocation Round 8 – to participate.

7.7 Regarding the carrying over of rules from fixed bottom offshore wind to, 17 out of 37 responses explicitly supported the 1500 MW capacity limit for floating offshore wind. A majority of those who supported this also encouraged a review of the cap in later rounds.

7.8 One respondent supported reducing the cap to 1000 MW. Two respondents supported no fixed cap. A further 16 out of 37 responses explicitly supported a cap higher than 1500 MW.

7.9 Most respondents either explicitly expressed a preference that the other phasing rules *not* be changed or did not comment on the rules. A minority requested that the 25% completion requirement be changed and/or the Target Commissioning Date be extended.

Better enable repowering under the CfD

7.10 The questions posed to respondents regarding repowering included assessments of the proposed eligibility criteria, the proposed rules and requirements for projects which want to apply for repowering and the impact of forward bidding for repowered projects.

7.11 A majority of respondents agreed with enabling full repowering applications for the CfD scheme in Allocation Round 7.

7.12 All who responded to the relevant question agreed that onshore wind repowering satisfied the eligibility criteria set out in the consultation proposal.

7.13 A majority respondents also agreed that all other technologies did not meet the repowering criteria for Allocation Round 7.

7.14 All respondents that addressed the question of forward bidding, agreed that forward bidding would better enable repowering via the CfD as it would reduce periods of no generation and reduce repowering timelines.

8. Applicable Guidance

8.1 The Allocation Framework sets out the rules for each Contracts for Difference Allocation Round and the eligibility requirements applicants must satisfy. The Allocation Framework for the next Allocation Round will be published closer to the commencement of the round.

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

9.1 A full Impact Assessment will be published and will be found on gov.uk. This will present an assessment of the impact of the policy on business and wider society.

Impact on businesses, charities and voluntary bodies

9.2 There is no significant impact on charities or voluntary bodies.

9.3 The legislation does not significantly impact small or micro businesses.

9.4 There is no, or no significant, impact on the public sector because the CfD will be open only to companies involved in the renewable electricity industry.

10. Monitoring and review

10.1 The approach to monitoring this legislation will entail a review of the effectiveness of legislative changes during every Allocation Round. In the case of phasing for floating offshore wind, this will specifically include ensuring that the requirements and rules for phased assets remains relevant to floating offshore wind technology/market. In the case of repowering, this will specifically include reviewing the eligibility criteria and the extent to which CfD asset types satisfy/do not satisfy them.

10.2 The instrument does not include a statutory review clause and, in line with the requirements of the Small Business, Enterprise and Employment Act 2015, Minister Shanks has made the following statement:

"In my view, a review provision is not appropriate because it would not be proportionate taking into account the economic impact of the regulatory provision on business activity, as set out in 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 Minister for Energy, Minister Michael Shanks, has made the following statement regarding Human Rights:

"In my view the provisions of the Contracts for Difference (Miscellaneous Amendments) (No. 2) Regulations 2024 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").