EXPLANATORY MEMORANDUM TO

THE CONTRACTS FOR DIFFERENCE (MISCELLANEOUS AMENDMENTS) (NO. 3) REGULATIONS 2025

2025 No. 903

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

2.2 Lucy Longstaff, Deputy Director for Renewables Delivery, at the Department for Energy Security and Net Zero confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Jessica Reid at the Department for Energy Security and Net Zero email: jessica.reid@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 These Regulations amend two statutory instruments made under the Energy Act 2013 relating to Contracts for Difference (CfD) scheme.

4.2 They amend the Contracts for Difference (Allocation) Regulations 2014 ("Allocation Regulations") and the Contracts for Difference (Electricity Supplier Obligation) Regulations 2014 ("ESO Regulations").

4.3 The purpose of the amendments is to:

i) Amend the Contract Budget Notice publication process: provide for a price and pot notice to be published before the contract allocation process application window opens; remove the requirement for the contract budget notice to be sent to the CfD delivery body, National Energy System Operator ("NESO"), 10 working days ahead of the application window opening, and instead provide for the contract allocation framework[1] to determine when the notice should be sent; ensure the contract budget or contract budget revision is made public at the end of an allocation round.

ii) Amend the information Secretary of State has access to during the allocation round: allowing the Secretary of State to see anonymised bids of strike prices that have been submitted to NESO for that allocation round, and to be able to

[1] The allocation framework sets out the rules governing how CfDs are to be allocated by NESO, and one is produced for each allocation round.

see that and other information related to the bids at any time, i.e. removing the requirement for Secretary of State to wait until the first CfD Notice had been given by NESO to the first successful bidder before he could see any other information; this will be facilitated by an estimated budget that will be sent to NESO to enable NESO to provide the information.

iii) Amend Low Carbon Contracts Company (LCCC) calculations to include Clean Industry Bonus (CIB) payments: includes CIB (referred to in regulations as the 'sustainable industry reward') costs in how the CfD counterparty, LCCC, calculate electricity supplier's contributions to the supplier obligation levy which funds CfD payments. Including CIB costs in LCCC's calculations ensures that they are included in Ofgem's calculation of the energy price cap and that the price cap is accurate.

4.4 These amendments are made in support of policy changes to the CfD, outlined in this document, which are expected to be implemented before the contract application window opens for 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.

4.6 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.

5. Policy Context

What is being done and why?

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. CfDs offer generators of low-carbon electricity a guaranteed price for the sale of the electricity they generate. A price is set per MWh of electricity, known as a 'strike price'. The scheme runs in 'allocation rounds.' In previous allocation rounds applicants have submitted sealed bids of strike prices ("bids of strike prices") ahead of a contract allocation process, with the lowest bidders successfully securing the contract, and unsuccessful bidders being those whose strike prices breach the Secretary of State's contract budget for that allocation round.

5.2 Previously, contract budget notices are set without any certainty on the capacity that could be procured in the allocation round.

Amending the budget publication process and access to information on bids

5.3 The amendments to the contract allocation process enable the contract budget to be set efficiently and to maximise deployment of renewable generation to aid the delivery of Clean Power 2030[2].

5.4 The key changes include:

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[2] Secretary of State's policy ambition is to ensure clean sources produce at least as much power as Great Britain consumes per year, and at least 95% of Great Britain's generation; reducing the carbon intensity of our generation from 171gCO2e/kWh in 2023 to well below 50gCO2e/kWh in 2030. For further information on Clean Power 2030 see the Clean Power 2030 Action Plan published here Clean Power 2030 Action Plan - GOV.UK

a) permitting Secretary of State to direct NESO to provide anonymised information about bids including strike prices, and permitting this at any time in the round;
b) making provision for Secretary of State to provide NESO with an ‘estimated budget’ in order for NESO to answer the direction to provide information on bids before the contract budget has been set;
c) ensuring Secretary of State must still provide and publish the administrative strike prices and any pots (the competitive groupings of applications that will be allocated a portion of budget) before the allocation round opens; and
d) when the contract budget is sent to the delivery body and published.

5.5 These changes will allow Secretary of State to decide to see anonymised bid information earlier, allowing him to make more informed budget decisions which support renewables deployment towards achievement of the Clean Power 2030 goal while balancing cost to consumers.

Amending Counterparty calculations to account for the CIB

5.6 The CIB was introduced as an optional add-on, which the Secretary of State may apply to the seventh, eighth and ninth allocation rounds of the CfD scheme. The CIB allows offshore wind developers applying to a relevant allocation round to compete for ‘bonus’ payments in return for committing to invest in the development and sustainability of supply chains.

5.7 The previous government laid The Contracts for Difference (Sustainable Industry Rewards) Regulations 2024 before the House on 21 March 2024. The Regulation passed the parliamentary process in the House of Commons and the House of Lords and came into force in June 2024. These regulations amended the Allocation Regulations, the Electricity Market Reform (General) Regulations 2014, the Contracts for Difference (Definition of Eligible Generator) Regulations 2014 and the Standard Terms Regulations to make provision for the CIB scheme within CfD legislation.

5.8 The CIB was launched on 12th November 2024.

5.9 Like CfD payments, funding for ‘bonus’ payments made under the CIB scheme is raised through the supplier obligation levy, as set out in the ESO Regulations. This requires electricity suppliers to make payments to the CfD counterparty (Low Carbon Contracts Company, LCCC) to enable LCCC to meet their costs, including obligations to make payments under CfDs.

5.10 LCCC performs all calculations to determine the level of contribution which electricity suppliers must make to the supplier obligation levy. An amendment to the ESO Regulations is being made to expressly include the cost of CIB ‘bonus’ payments in LCCC’s calculations. This will ensure that these costs are included the energy price cap set by Ofgem. The energy price cap is the maximum amount energy suppliers can charge consumers for each unit of energy and standard charge for consumers on a standard variable tariff. The price cap is calculated based on various factors, including the amount which electricity suppliers are required to contribute to government schemes.

What was the previous policy, how is this different?

<u>Access to information on bids</u>

5.11 The Allocation Regulations provided a broad power to allow the Secretary of State to direct NESO to provide information. However, those regulations previously restricted

Secretary of State from requesting NESO to provide the strike prices. They also restricted Secretary of State from seeing any information not listed in regulation 54(2)(a)-(d) until the end of the contract allocation process, i.e. after NESO has sent the first "CfD notification" to the first successful bidder (under regulation 42).

5.12 Keeping those two previous restrictions could prevent the contract budget, particularly for offshore wind in the seventh allocation round, from being set efficiently. The sixth allocation round saw budget underspend for offshore wind. With limited allocation rounds before the ambition of Clean Power 2030, it is important to have greater certainty over the capacity that can be procured in an allocation round.

5.13 This amendment will allow the Secretary of State the flexibility to decide if it would be beneficial to see anonymised bids of strike prices much earlier in the contract allocation process, including before setting the contract budget. This power is broad enough to account for future round that might require a different range of information for different technologies.

5.14 Importantly, the amendments have retained the requirement for the Secretary of State to only direct NESO to provide anonymised information. This ensures participants in the contract allocation process have confidence their commercial information is being treated securely. In addition, in order for NESO to provide information on bids of strike prices before a budget has been set, Secretary of State will first have to provide an estimated budget for NESO, who will use this information to feed into their auction system, which will then generate the data requested. To account for this, these Regulations provide an obligation for Secretary of State to send an estimated budget when he is requesting certain information and NESO cannot respond without an estimated budget.

5.15 In order to allow the most potentially useful range of information, the estimated budget notice includes options for Secretary of State to provide NESO with minima and maxima for different technologies, or to provide an estimate for the whole allocation round, or just one pot. It also allows for any of those constraints to be applied as a 'soft' constraint (when they are expressed in terms of capacity). If applied as a 'soft' constraint rather than a 'hard' constraint, the application that breaches the relevant constraint would be accepted, subject to conditions to be specified in the relevant allocation framework.

5.16 The amended Allocation Regulations also require NESO to ensure that the calculations and information they are directed to provide will first go through an appropriate audit process.

Timing of the Contract Budget Notice

5.17 The Allocation Regulations previously required Secretary of State to send to NESO and publish a 'Contract Budget Notice' at least 10 days before the contract allocation application window opened. However, sending a contract budget notice early on in the contract allocation process timeline meant the initial budget was set without certainty on the capacity or strike prices that can be procured, which risked potentially significant underspend, even with the Secretary of State's ability to revise the budget

5.18 Taking this into account, the Allocation Regulations now provide greater flexibility in the timing of the contract budget notice; now it will be the contract allocation framework that sets the point at which the contract budget notice will be provided to the delivery body. The contract allocation framework sets the process for how NESO will allocate the CfDs; it follows that this framework is the appropriate place to determine the most suitable time for the budget to be set.

5.19 As a result, the Allocation Regulations now only require the administrative strike prices and pot structure to be published ahead of the application window. This is so generators have enough information for their bidding strategy formation, whilst also allowing the Secretary of State, for each allocation round, to determine the best time to give the contract budget notice and striking a balance that promotes competition and value for money. It is also designed to work in tandem with the power for Secretary of State to see anonymised bids of strike prices.

Calculations for the Supplier Obligation Levy

5.20 Currently, the ESO Regulations do not expressly take into account CIB costs in calculations for electricity suppliers' daily and interim contributions to the supplier obligation levy. The amendment to the ESO Regulations alters the calculations to include those costs, ensuring their inclusion in the Ofgem's calculation of the energy price cap.

6. Legislative and Legal Context

How has the law changed?

Amending the budget publication process and access to information on bids

6.1 Amendments have been made to regulations 2, 10, 11, 12, 36, 37 and 54 of the Allocation Regulations, The Regulations have also inserted new regulations 10A, 10B and 13B.

6.2 The amendment to regulation 10 removes the overarching requirement for the notices in this Part of the Regulations to be made public as soon as practicable after being given to NESO. New regulation 13B provides for the publication of four of the notices in the contract allocation process. The price notice, pot notice and sustainable industry reward budget notice must be made public as soon as practicable after they have been sent to NESO. The contract budget notice (or the contract budget revision notice if there is one) must, at the latest, be made public as soon as practicable after NESO give the notice of completion of the contract allocation process.

6.3 New regulation 10A introduces two notices:

- **Price Notice**: this preserves the requirement for the Secretary of State to specify the administrative strike prices for a contract allocation process in a notice.
- **Pot Notice**: this preserves the power to specify groups of applications in a notice, which form 'pots' that will receive a division of the contract budget in the contract budget notice.

6.4 New regulation 10B requires the Secretary of State to provide NESO with an estimated budget notice when he directs NESO to provide information under regulation 54(2)(e) but NESO cannot comply with that request without an estimated budget. The notice is designed to contain the necessary information for NESO to run calculations in order to provide the requested information.

6.5 The amendment to regulation 11(5) allows the contract allocation framework to set the timing for sending the contract budget notice to NESO.

6.6 Regulation 12(2) is updated to allow contract budget revisions after a contract budget notice and before the first CfD notification is given. Regulations 12(3) and (4) are omitted as the contract budget notice is not required more than 10 working days before the opening of the contract allocation application window, so the previous broader possible revisions that can apply more than 10 working days before the application window are no longer required.

6.7 The amendment to regulation 36 requires NESO to conduct an additional audit of any calculations they have done following an estimated budget. This must be conducted as soon as reasonably practicable after NESO has been given an estimated budget.

6.8 Regulation 54(3) is amended to remove the prohibition on requesting information on bids of strike prices and the restriction that information on ‘other matters’ could only be provided at the end of the contract allocation process i.e. after the first CFD notification.

6.9 Decisions on when to create the contract budget and which strike price information to see will be taken for each round in a manner which balances the effect on competition, value for money for consumer, and, in the relevant rounds, ensuring the round is effective in securing capacity for Clean Power 2030. The Secretary of State will only make requests for information that do not allow him to know which applicants have submitted which bids; this is reinforced by maintaining the requirement for anonymity and providing for the independent delivery body to make the necessary calculations which are then audited.

Calculations for the Supplier Obligation Levy

6.10 Amendments have been made to regulations 2, 4 and 7 of the ESO Regulations. The amendment to regulation 2 brings the definition of “Sustainable Industry Reward” (the legislative name for the CIB) into the ESO regulations. The amendment to regulation 4 adds the costs of payments made under the CIB into the calculation of the daily contribution electricity suppliers must make to the supplier obligation levy. The amendment to regulation 7 adds the cost of CIB payments to the matters taken into account when LCCC calculates the interim levy rate which electricity suppliers must pay in respect of any given quarterly obligation period to the supplier obligation levy.

Why was this approach taken to change the law?

Amending the budget publication process and access to information on bids

6.11 The amendments to the Allocation Regulations are needed to optimise the CfD’s ability to deliver Clean Power by 2030. The previous process left a great degree of uncertainty as to how much capacity could be procured and at what cost in a given CfD round. This approach has been taken as it is the fairest and most straightforward way to maximise the amount of energy procured in future allocation rounds whilst retaining value for money for consumers.

Calculations for the Supplier Obligation Levy

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

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 21 February 2025 and closed on 21 March 2025. The formal consultation period was under six weeks, as the key proposals had already been published in December 2024 in the Clean Power Action Plan and stakeholders were engaged in informal consultation on the proposals from this point.

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 May 2025. https://assets.publishing.service.gov.uk/media/6814b6ff359707ba3d446767/cfd-scheme-proprosals-ar7-government-response-legislative-amendments.pdf

7.4 There was a range of 60 to 70 responses across the questions on the below sections.

Amending the budget publication process

7.5 Questions for this topic area sought views from respondents regarding receiving the monetary budget in advance of the sealed bid window, as opposed to later in the contract allocation process. It also asked whether replacing the monetary budget with a capacity ambition would have an impact on competition and bidding behaviour; boards / developer decision making timelines / processes; and whether this could impose any unintended consequences / additional costs on developers.

7.6 Respondents were split in their views, with c.40% stating it was important to receive a monetary budget and c.40% stating it wasn't important, with the remainder unsure.

7.7 Many respondents (c.40%) stated this change would not impact their participation, however an additional c.40% were unsure. Only a minority of respondents said it would have an impact on participation.

7.8 As to impacts on competition/bidder behaviour or developer decision making, nearly half of respondents stated it would have a negative impact, whereas c.40% stated it would not.

7.9 However, c.60% of respondents stated it would not have a negative impact on non-delivery or withdrawal from auction.

Amending access to information Secretary of State receives on bids

7.10 Questions for this topic area sought views on whether respondents were in favour of the Secretary of State having the power to see anonymised bids of strike prices prior to the first CfD notification and whether this would have any negative impacts on bidder behaviour, investor confidence in the CfD scheme and consumers. Other questions asked whether respondents agreed with the rationale to only apply the new power to fixed-bottom offshore wind.

7.11 Many respondents (c.50%) were in favour of Secretary of State having the power to see anonymised bids of strike prices prior to the first CfD notification. Only c.30% of respondents were not in favour. However, several respondents proposed alternative methods to use the new power.

7.12 There was a mixture of themes in the responses as to the impact of this change on developers. Some believe that concerns about handling data and the perception of bias in budget setting could have a negative impact on bid prices, whilst some believe that this change could provide more transparency to the budget setting process, lead to a more efficient allocation of contracts and incentivise developers to bid their minimum viable price.

7.13 Respondents were split in their views, with c.40% stating they agreed with the rationale to apply the new power to fixed-bottom offshore wind only. With c.40% stating this power should be applied to other technologies.

7.14 The Government is proceeding with both amendments to the Allocation Regulations, as they are needed to optimise the CfD's ability to deliver Clean Power by 2030. This approach has been taken as it is the fairest and most straightforward way to potentially maximise the amount of capacity procured in future allocation rounds whilst meeting the statutory obligation of the CfD scheme to consider the cost to consumers of an allocation round.

Calculations for the Supplier Obligation Levy

7.15 The question for this topic area asked whether there were any unintended consequences to the change which the government might need to consider.

7.16 There were 28 responses to this question. The majority agreed that the changes to introduce CIB costs into the price cap did not seem to introduce any unintended consequences.

7.17 Those who disagreed or were neutral did not focus specifically on the price cap issue, but more on the speed at which the CIB gets repaid compared to when minimum standard liabilities may be raised, or on the absence of the CIB for tidal or solar technologies.

7.18 This amendment is proceeding as it is the only possible approach to make the necessary changes.

Consultation with Devolved Administrations

7.19 The Devolved Administrations were consulted on these proposals, as stipulated by the Energy Act 2013. No comments were received on these proposals.

8. Applicable Guidance

8.1 The contract allocation framework sets out the rules for the contract allocation process for each allocation round; including the eligibility requirements applicants must satisfy. The contract allocation framework for Allocation Round 7 will be published closer to the opening of the application window.

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

9.1 A full Impact Assessment is submitted with this memorandum and published alongside the Explanatory Memorandum on the legislation.gov.uk website

Impact on businesses, charities and voluntary bodies

9.2 The impact on business, charities or voluntary bodies is likely to be positive. The proposal seeks to address the current barriers faced by developers securing a CfD. The purpose of the CfD scheme is to support investment into new build renewable projects by protecting against the risk of high upfront capital costs and the sustained price risk across the asset's operating life.

9.3 The legislation does not 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

What is the approach to monitoring and reviewing this legislation?

10.1 The approach to monitoring this legislation will entail a review of the effectiveness of legislative changes after every allocation round. This will include reviewing the allocation round results to determine if our objective of maximising renewable capacity at good value for consumers has been achieved.

10.2 The instrument does not include a statutory review clause and, the requirement under section 28(2) of the Small Business, Enterprise and Employment Act 2015 to make provision for review does not apply to this instrument as it falls within an exception in section 28(3) of that Act.

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 Energy Minister has made the following statement regarding Human Rights:

"In my view the provisions of the Contracts for Difference (Miscellaneous Amendments) (No. 3) 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").