

Annex B

GOVERNMENT SUPPORT PACKAGE FOR T&SCO Draft Commercial Principles

Note: these draft commercial principles are subject to the "Disclaimer" section at the front of the update document to which they are annexed.

1. INTRODUCTION

1.1 Background

- (a) These commercial principles set out the basis upon which HM Government ("**HMG**") would consider providing a contingent Government Support Package ("**GSP**") to a company licensed to provide transport and storage services ("**T&SCo**") as part of HMG's CCUS Programme (the "**Programme**").
- (b) It is assumed for this purpose that T&SCo will be licensed under a licence ("**Licence**") issued by an economic regulator ("**Regulator**") under an Economic Regulatory Regime ("**ERR**").
- (c) The contents of these commercial principles are indicative only and do not constitute an offer by HMG and do not create a basis for any form of expectation or reliance. Any GSP arrangements that are developed in the future will be subject to approval by Ministers, in consultation with the Regulator, and the development and completion of necessary contractual documentation.

1.2 Rationale

- (a) The GSP has been structured to cover certain high impact, but low probability, risks beyond those which are manageable by operation of the ERR, which the investors and/or supply chain, including insurers, of T&SCo cannot take, or cannot price at an efficient level which is good value for money for UK taxpayers or consumers.
- (b) The risks to be covered by the GSP and the detailed terms of coverage remain under consideration, but these commercial principles set out current HMG thinking on the support which could be provided by the GSP. This will depend upon the terms of the ERR and the target risk profile and credit rating for T&SCo required by the ERR.

1.3 Description

- (a) This document sets out high level commercial principles for the GSP using the following structure:
 - (i) general terms and conditions (Section 2);
 - (ii) defined risks to which the GSP will apply (Section 3);
 - (iii) description of support (Section 4); and
 - (iv) glossary of terms (Section 5).
- (b) The scope of the areas of specific protection remains subject to review, in particular in the context of the detail of the ERR.

1.4 **Initial assumptions**

- (a) These proposed commercial principles are based on the following assumptions in respect of the transport and storage ("**T&S**") network:
 - (i) ownership of the T&S network: the onshore and offshore T&S network will be owned by T&SCo. In particular, T&SCo will hold any Crown Estate lease and licence/permit issued by the OGA (or licensing authority of a devolved administration);
 - (ii) development and operation of the T&S network: T&SCo will be responsible for the development, construction, operation and maintenance of the T&S network, including obtaining all necessary permits and approvals;
 - (iii) expansion of the T&S network: in the future T&SCo will likely need to expand the T&S network under the terms of the ERR and will provide access to new T&S users under the Storage of Carbon Dioxide (Access to Infrastructure) Regulations 2011 (as may be amended or supplemented);
 - (iv) decommissioning: T&SCo will be responsible for the decommissioning and monitoring of:
 - (A) the offshore T&S network in accordance with the Energy Act 2008 (as may be amended or supplemented); and
 - (B) the onshore T&S network in accordance with the relevant decommissioning conditions of any development/planning consent;
 - (v) T&S fees: users of the T&S network will pay T&SCo fees for provision of T&S services which will be regulated under the ERR. The ERR may allow recourse to taxpayers/consumers in limited circumstances; and
 - (vi) CO₂ ownership and sale: T&SCo will certify delivery of CO₂ onto the T&S network and will take title to and own the CO₂ and any revenue from sale of CO₂ will be accounted for under the ERR.

1.5 **Glossary of terms**

Defined terms used in this document have the meaning given to them in the glossary of terms at Section 5.

2. GENERAL TERMS AND CONDITIONS

There are set out below some proposed general terms and conditions applicable to the GSP.

No.	Item	Commercial Terms
2.1	Conditions precedent	It is proposed that the GSP will be conditional on certain conditions precedent including: a) award of a Licence to T&SCo under the ERR; and b) award to T&SCo of any other licences, permits or approvals which are required.
2.2	Mandated requirements	The GSP will set out certain mandated requirements for T&SCo, including tax residency in the UK. HMG is considering any other policy considerations.
2.3	Reporting and liaison	HMG is considering its requirements in relation to: a) reporting and information to be provided by T&SCo; and b) the setting up of a liaison committee for consideration and management of interfaces with other elements of the CCUS chain and T&SCo's interaction with other regulators.
2.4	Management and mitigation of risk	HMG is considering its requirements in relation to: a) monitoring of Defined Risks by T&SCo; and b) incentives for T&SCo to mitigate Defined Risks.
2.5	Full documentation	Details of contractual terms will need to be developed in conjunction with the development of the ERR.

3. DEFINED RISKS

There are set out below the proposals relating to the limited areas to which the GSP will apply.

No.	Defined Risk	Description
3.1	Significant leakage from storage facility	<p>There is a risk that there is a significant CO₂ leakage from the T&S storage facilities into the atmosphere or water column or into neighbouring subsurface formations.</p> <p>Leakage during the development, construction, operations, maintenance and decommissioning phases of the storage facilities, and in the period following the decommissioning stages of each store (including wells) before handback the site to HMG, will sit with T&SCo (and its contractors), save for the occurrence of leakage in respect of a store (i.e. the geology and wells) which is above a remote threshold where commercial insurances are not available ("Leakage Risk").</p> <p>The GSP will include requirements on T&SCo to mitigate the risk:</p> <ul style="list-style-type: none"> • through detailed store characterisation and injection scheme design, that will be assessed by HMG through due diligence prior to any GSP protection being granted; • by application of appropriate standards to construction and operation of the T&SCo network; and • by being required to procure commercial insurances where available at an efficient cost, as HMG expects a commercial insurance market to develop.
3.2	Stranded Asset	<p>Stranded asset risk is the risk that there is a complete and permanent loss of demand for the T&S network for reasons outside the control of T&SCo, such as change in regulation or HMG policy such that the T&S network becomes economically redundant ("Stranded Asset Risk").</p> <p>Stranded Asset Risk could result in:</p> <ul style="list-style-type: none"> • uncompensated capital investment: up to a maximum of 1 x the regulatory asset value (RAV) of the T&S network; • impact on Opex: costs of suspending the T&S network so that it is preserved for future use or to limit costs of decommissioning (may be offset by a reduction in operating costs); • early decommissioning: shortfall in decommissioning cost provision as a result of entering decommissioning sooner than expected; and • leakage liability: subject to the measures to address Leakage Risk set out in Section 3.1 above, there will be a CO₂ liability consideration should Leakage Risk materialise following the occurrence of a stranded asset risk.

4. DESCRIPTION OF SUPPORT

There are set out below an outline of the proposed support for providing T&SCo with relief against a Defined Risk.

4.1 Supplemental Compensation Agreement

No.	Heading	Description
4.1.1	Parties	Department for Business, Energy and Industrial Strategy (" Secretary of State ") and T&SCo.
4.1.2	Term	The GSP will expire on revocation of the Licence or earlier Discontinuation, subject to provisions that expressly survive Discontinuation.
4.1.3	Compensation trigger events	<p>T&SCo will be required to seek commercial insurance in respect of each of the Defined Risks.</p> <p>If insurance is commercially viable, then the GSP will only respond as "insurance of last resort":</p> <ul style="list-style-type: none">• to the risk of unavailability of such insurances; and• where the relevant insurances cease to respond because the limit of indemnity to cover revenues has been reached, to the risk of loss of revenue above such limit of indemnity. <p>If insurance is not commercially viable, then the GSP will respond to the occurrence of the relevant Defined Risk.</p>
4.1.4	Compensation	<p>There will be provision for recovery of compensation in respect of specified costs associated with each Defined Risk.</p> <p>Any compensation will be paid out on a periodic basis against evidence of the specified costs, subject to any adjustment resulting from failure by T&SCo to mitigate (see Section 2.4 above) and subject to HMG's right of Discontinuation.</p>
4.1.5	Fees	HMG is considering the fees payable by T&SCo in return for provision of the Supplemental Compensation Agreement.

4.2 Discontinuation Agreement

No.	Heading	Description
4.2.1	Parties	Secretary of State and T&SCo
4.2.2	Term	The GSP will expire on revocation of the Licence or earlier Discontinuation, subject to provisions that expressly survive Discontinuation.
4.2.3	Discontinuation trigger events	<p>The events which trigger a right for HMG to provide notice of discontinuation ("Discontinuation") will include a call for compensation in respect of one of the Defined Risks.</p> <p>HMG is considering whether there should be any other triggers.</p>

4.2.4	Consequences of Discontinuation	<p>Upon exercise by HMG of its right of Discontinuation:</p> <ul style="list-style-type: none"> a) there will be a calculation of compensation payable in respect of debt/equity investors in T&SCo - see below Section 4.2.5; b) the Regulator will be entitled to revoke T&SCo's licence; and c) the Regulator will be entitled to institute a statutory transfer scheme in respect of the T&S network.
4.2.5	Calculation of Discontinuation compensation	<p>The compensation will be calculated in accordance with the following principles:</p> <ul style="list-style-type: none"> a) the compensation will be capped (see below) and adjusted to take account of mitigation measures required to be undertaken by T&SCo (see Section 2.4 above); and b) the compensation will reflect senior debt liabilities and base case equity return up to Discontinuation, subject as noted at Section 4.2.5(a) above. <p>The maximum compensation liability cap of HMG under the Discontinuation Agreement will be the regulatory asset value (RAV) of the relevant T&S network.</p> <p>HMG is considering the basis of calculation in the context of T&SCo insolvency.</p>

5. GLOSSARY OF TERMS

In this document capitalised terms not otherwise defined shall have the following meaning:

Term	Definition
CCUS	means carbon capture, usage and storage, which is the process of capturing carbon dioxide emissions from large-point sources (such as industrial facilities and power stations), and either transporting it in pipelines or via ships to very deep subsurface rock formations, where it can be safely and permanently stored; or using it, for example in the food and drink sector as a carbonating agent, or in the pharmaceutical industry, as a respiratory stimulant, or in the cement industry;
Crown Estate	means the statutory corporation established by the Crown Estate Commissions under the Crown Estate Act 1961;
Defined Risks	means the risks outlined in Section 3 (Defined Risks) of this Annex;
Discontinuation	has the meaning given to it in Section 4.2.3 of this Annex;
ERR	has the meaning given to it in Section 1.1(b) of this Annex;
GSP	has the meaning given to it in Section 1.1(a) of this Annex;
HMG	has the meaning given to it in Section 1.1(a) of this Annex;
Leakage Risk	has the meaning given to it in Section 3.1 of this Annex;
Licence	has the meaning given to it in Section 1.1(b) of this Annex;
OGA	means the Oil and Gas Authority;
Opex	means operating expenditure incurred by T&SCo;
Programme	has the meaning given to it in Section 1.1(a) of this Annex;
Regulator	has the meaning given to it in Section 1.1(b) of this Annex;
Secretary of State	has the meaning given to it in Section 4.1.1 of this Annex;
Stranded Asset Risk	has the meaning given to it in Section 3.2 of this Annex;
T&S	has the meaning given to it in Section 1.4 of this Annex; and
T&SCo	has the meaning given to it in Section 1.1(a) of this Annex.