



Department for  
Energy Security  
& Net Zero

# Contracts for Difference for Low Carbon Electricity Generation

Government Response to the Call for  
Evidence on introducing non-price factors  
into the Contracts for Difference Scheme.

September 2023



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## Context

Government is looking at ways of amending the Contracts for Difference (CfD) scheme to address specific challenges facing the renewable energy industry, including recommendations stemming from the Offshore Wind Acceleration Taskforce report. As a result, the Department for Energy Security and Net Zero [launched a Call for Evidence](#) on the 17<sup>th</sup> of April 2023 to consider the ways in which the scheme could capture the wider value of renewable projects, specifically by introducing non-price factors. This is part of our work to continue to evolve the CfD scheme, as we consider long-term market arrangements through the Review of Electricity Market Arrangements (REMA). This document is the government response to the Call for Evidence.

Industry challenges that have been identified by stakeholders include: renewable energy supply chains struggling to cope with upward pressure on costs; increased supply chain disruption; surging global demand for renewable energy; and limited manufacturing capacity for key components. While current government policy addresses some of these challenges (for instance, the Offshore Wind Manufacturing Investment Scheme), government is looking at ways in which Contracts for Difference policy could be developed to better address current issues.

We are also considering some of the challenges identified in the REMA case for change and how Contracts for Difference policy can help address those issues. As part of this work, government is looking closely at what other major renewable energy markets are doing in similar policy areas.

## The Contracts for Difference scheme

Contracts for Difference are a 15-year private law contract between low-carbon electricity generators and the Low Carbon Contracts Company, a government-owned company that is operationally independent and manages CfDs at arm's length from government. Contracts are awarded in a series of competitive auctions; the lowest price bids are successful, which drives efficiency and cost reduction and is a low-cost way to secure clean electricity. Generators receive revenue from selling their electricity into the wholesale market. However, when the market reference price is below the strike price, generators receive a top-up payment for the additional amount. Conversely, if the reference price is above the strike price, the generator must pay back the difference.

## Non-price Factors

CfDs have been hugely successful in driving down renewable energy deployment costs. This downward pressure combined with price pressure in the wider market has quickly passed through to the supply chain, especially in offshore wind, where low margins and a tough

economic environment are making it more challenging for some renewable industries to support longer term investments, for example in capacity, skills, innovation, or wider system flexibility and operability. In the near-term, there is a risk of deployment challenges and bottlenecks arising from these global pressures, compounding existing issues.

The Call for Evidence on CfD non-price factors sought to test whether and how to introduce mechanisms to value criteria other than just cost through CfD auctions, in response to market conditions faced by renewable energy projects. Non-price factors should therefore help encourage sustainable renewable electricity generation by helping to address supply chain issues that are affecting deployment, therefore contributing to our overall Net Zero ambitions, while having regard to consumer costs.

## Next steps

Government will take into account the points outlined below and use them to decide next steps on this policy. The government response should not be read as an indication of final policy decisions on any issue, nor that the policy will go ahead. Final decisions will be taken as part of the wider fiscal and policy context.

# Responses to the call for evidence

The Call for Evidence closed on the 22<sup>nd</sup> of May 2023. Responses were submitted through the online response tool Citizen Space and by email.

There were 92 responses to the Call for Evidence and 45 responses were from developers, 17 from the supply chain, 18 from various trade and representative bodies, 3 from public bodies, 3 investors and 6 individuals.

This government response outlines the summary of the 92 responses to the 17 questions in the Call for Evidence. The government is grateful to each and every respondent to the Call for Evidence for taking the time to submit their views on the proposals.

In reporting the overall response to each question, the ‘majority’ indicates the clear view of more than 50% of respondents in response to that question, and ‘minority’ indicates fewer than 50%. The following terms have been used in summarising additional points raised in the responses: ‘most respondents’ indicates more than 70% of those answering the particular question, ‘a few respondents’ means fewer than 30%, and ‘some respondents’ refers to the range in between 30% and 70%. This is consistent with the approach of other government responses.

## Question one

Question one sought views on the top-up model, which is one out of the three proposed models government could consider as a mechanism to introduce non-price factors into the CfD scheme.

This model would introduce a “top-up” to the CfD strike price. Auctions would be run exactly as they are now, with no change to the bidding process. After the auction has been run, projects that made it through the auction, and that submit and implement high-scoring non-price factors, could receive a top-up to their CfD.

Respondents were asked the extent to which they supported the top-up model as a mechanism for implementing non-price factors and whether there were any unintended consequences that come from this model.

## Responses to the call for evidence

There was a total of 78 responses to this question and 44 supported the model, 18 disagreed with the model and the remainder were neutral or did not respond to the question.

## Views on the proposal and government response

The majority of respondents preferred the top-up model, citing its simplicity and lack of disruption to the existing CfD process. Many respondents were nonetheless concerned that

under the top-up model, the CfD auction itself is still run on price-only and top-ups applied only to the winners, therefore not fully integrating non-price factors into the auction, running the risk that non-price factors become an optional “nice to have”.

Many respondents also noted that for the model to work, appropriate information would need to be released ahead of time, including top-up budgets, the non-price factors themselves, and the penalties associated, as well as potentially the need to release an applicant's score before the CfD auction begins, to enter the auction with full transparency.

**Policy response:**

- Taking into account the responses received, the government agrees with the benefits and drawbacks of the model identified by respondents and will further explore options to mitigate its limitations.

## Question two

Question two sought views on the extent to which respondents supported the bid re-ranking model as a mechanism for implementing non-price factors and whether there were any unintended consequences that come from this model.

In this model, non-price factor scores would have a direct impact upon the bid stack ranking methodology, making it possible for a project scoring sufficiently highly on non-price factors to win a CfD ahead of another project bidding into the auction at a lower price but scoring poorly on non-price factors.

### Responses to the call for evidence

There was a total of 74 responses to the question with 20 respondents supporting the bid re-ranking model, 39 disagreeing with the model and the remainder were neutral or did not respond to the question.

### Views on the proposal and government response

The majority of respondents disagreed with the bid re-ranking model due to its perceived complexity, and potential unintended consequences, however many flagged that it could be better than top-up at integrating non-price factors into bidding strategies.

Respondents also noted that for the bid re-ranking model to work, technologies to which non-price factors do or do not apply would likely need to be considered in separate CfD auction ‘pots’ so as to prevent the different requirements from having a distortive effect on their pricing strategies and overall competitiveness.

Many respondents noted it would be challenging to assign an appropriate weight to non-price factors into the auction, so that they do not significantly increase clearing prices, yet remain sufficiently important to distinguish bids.

**Policy response:**

- Taking into account the responses received, government agrees that the bid re-ranking model may result in unintended consequences, especially due to the current pot structure of CfD auctions, and these may be harder to mitigate than in the top-up model without fundamentally overhauling the design of the CfD.

## Question three

Question three sought views on whether respondents supported the model of amending the valuation formula as a mechanism for implementing non-price factors and whether there were any unintended consequences that come from this model.

This model involves amending the valuation formula used to estimate the annual budget impact of a project bidding into a CfD Allocation Round. This formula determines when the assigned budget of an auction has been exhausted and therefore which of the projects in that auction will be successful in winning a CfD. The proposal was that non-price factors would modify a project's budget impact in the valuation formula, increasing or decreasing its chances of coming in under budget.

### Responses to the call for evidence

There was a total of 66 responses to the question with 55 respondents disagreeing with the amending the valuation formula model, 3 agreed and the remainder were neutral.

### Views on the proposal and government response

The majority of respondents disagreed with the model of amending the valuation formula as a mechanism for implementing non-price factors due to its significant complexity which could impact investor confidence.

The majority of respondents highlighted further issues with the model that include the potential risk of increasing the opacity of the CfD decision-making process and the difficulty in predicting bid outcomes and therefore impacting the ability to plan for the budget accordingly. Respondents also noted that if this model is chosen, certainty and transparency would be key and the valuation formula and non-price factors need to be published well in advance of an allocation round.

**Policy response:**

- Taking into account the responses received, the government agrees that amending the valuation formula would significantly increase the complexity of the CfD because of its potential lack of transparency and resulting in greater difficulty for government in planning and setting CfD budgets.

## Question four

Question four sought views on whether there are any additional risks of unintended consequences (e.g. for renewable energy deployment, auction design / competition and consumers) that respondents have identified with certain non-price factor models and think should be considered.

### Responses to the call for evidence

There was a total of 61 responses and 59 responses agreed that there were additional risks of unintended consequences with some or all of the models that should be considered, 1 disagreed and 1 response was neutral.

### Views on the proposal and government response

An overwhelming majority of respondents agreed that there are unintended risks which include potentially adding complexity to the auction process, and applicants overpromising / overbidding on non-price factors without appropriate controls/penalties.

A few respondents noted that under the top-up model, the financial uplift provided would need to be higher than the cost of delivery otherwise there would be limited incentive to deliver on the non-price factors. There was also concern that a punitive penalty system may deter investors.

#### **Policy response:**

- Taking into account responses received, the government agrees that all models could carry the risk of unintended consequences, and it will review and assess those as it considers next steps.
- Further analysis on the potential size of top-ups could be undertaken - any top-up should be designed to be proportionate to the extra cost of undertaking a particular action, balancing incentives to invest with limiting costs to consumers and avoiding overpayment.

## Question five

Question five sought views on the ways in which the models for a mechanism for non-price factor implementation could be improved.

### Responses to the call for evidence

There was a total of 46 responses. 41 out of 46 agreed that the mechanisms proposed could be improved and 5 disagreed.

## Views on the proposal and government response

Most respondents listed the various ways the mechanisms outlined could be improved. For the top-up model, some respondents suggested that projects should be ring-fenced within a pot to recognise the impact on their competitive position vis-à-vis other technologies, with a dedicated budget to secure the necessary levels of deployment.

Suggestions also included setting a minimum level of non-price factor score that all participants must attain before they can be considered for a contract for the bid re-ranking model.

In terms of delivery, respondents suggested that non-price factors for offshore wind could be stated, submitted and scored as a submission during leasing stage or well before the price auction. Some respondents also state that the non-price factors are trying to solve industry scale problems at project level.

### **Policy response:**

- Taking into account responses received, government will consider each of the proposals for improvement, noting in particular the suggestions on minimum-standards and pot structure, though noting that pot structure is determined by a range of factors, not least competitive tension. See question 17 for proposals on the timing of non-price factors.

## Question six

Question six focused on whether there were alternative mechanisms that government should be considering (including models outside of the CfD mechanism).

### Responses to the call for evidence

There was a total of 61 responses to the question that outlined alternative mechanisms.

## Views on the proposal and government response

Respondents largely used this question to set out wider thoughts on how the current CfD model could be improved more generally. This included a proposal to move to a “hurdle CfD” model (a non-competitive allocation process whereby projects become entitled to a CfD upon a certain milestone being met). Other suggestions included proposals for an alternative strike price indexation method and reforms to the setting of Administrative Strike Prices (ASPs) and/or budget parameters.

### **Policy response:**

- Wider reforms to the CfD scheme will be considered in the normal course of policy development for future allocation rounds, including longer-term considerations associated with REMA. Where appropriate, wider changes to the scheme would be consulted on.

## Question seven

Question seven focused on outlining which projects (in terms of size) and technologies respondents thought should be eligible for non-price factors.

### Responses to the call for evidence

There was a total of 76 responses that outlined which projects respondents thought should be eligible.

### Views on the proposal and government response

The majority of the respondents were supportive of all projects and technologies being eligible for non-price factors (but subject to a bespoke design for each). Some respondents also stated that technologies that are subject to any specific non-price factor should compete only within a defined pot and budget framework; non-price factors may provide an advantage to larger developers, or specific technologies, who have the economies of scale to develop projects with wider benefits.

#### **Policy response:**

- Government will need to consider if non-price factors are the appropriate policy tool to respond to specific issues and market failures for other technologies in ways that are similar to offshore and floating wind – the nature of the market volatility and supply chain bottlenecks are different for each technology, and therefore different policy interventions for different technologies might be more suitable.
- Government recognises the challenge of having numerous technologies competing in a single auction pot with different non-price factors applying. Pot structure is reviewed ahead of each allocation round and is based on a range of factors including the need to maintain competitive tension in auctions.

## Question eight

Question eight invited views on the family of non-price factors focused on addressing supply chain sustainability, capacity building, skills and innovation, and whether these family of factors are appropriate to strengthen renewable energy supply chains.

### Responses to the call for evidence

There was a total of 74 responses and 33 agreed that the family of non-price factors outlined were appropriate, 21 respondents disagreed, 17 were neutral and 3 were unclear.

### Views on the proposal and government response

The majority of the respondents were supportive of the factors proposed. However, the majority emphasised that non-price factors need to be clear and transparent. On supply chain

capacity building (i.e. investment more in manufacturing capacity and infrastructure), the majority of respondents felt this was too late in the development cycle of the supply chain process for capacity building to be addressed as a CfD non-price factor, and that this issue requires a strategic industry approach. Those who disagreed either disagreed with the concept of non-price factors or considered that there was a danger this family of factors could be subjective and lack transparency in its application.

**Policy response:**

- Taking into account the responses received, government will continue exploring potential non-price factors based on this family, potentially fitting them in wider groups around supply chain sustainability (economic, social, environmental), aligning with existing sustainability frameworks. The government recognises issues around subjectivity and transparency and considers that non-price factors should be objectively measurable (see question 13).
- Government recognises the challenge around when the timing of significant investments are made and will consider how to address this appropriately if the policy goes ahead (see also question 17).

## Question nine

Question nine invited views on whether there were alternative non-price factors that should be considered other than those listed under question eight.

### Responses to the call for evidence

There was a total of 62 responses. 44 respondents agreed there should be additional non-price factors whilst 15 disagreed, 2 were neutral and 1 unclear.

### Views on the proposal and government response

A majority of respondents provided additional non-price factors for consideration. Some respondents outlined that biodiversity and nature impacts should be assessed, along with community impacts. A few expressed concerns however that these should not duplicate requirements in the planning stage. A few respondents also felt that innovation criteria should include innovation in finance and project ownership, and a few considered that speed of implementation should be considered given the push for Net Zero. Standardisation of components was proposed as a non-price factor by a few respondents in order to increase supply chain capacity.

A minority of respondents did not provide any additional non-price factors for consideration, while a majority of respondents expressed the view that the number of non-price factors should be limited to increase their effectiveness, with a few stating that some non-price factors could be combined or listed at the pre-qualification stage.

**Policy response:**

- Taking into account the responses received, government agrees that the number of non-price factors should be limited to maintain simplicity of the process. The focus should be on high-impact issues or concerns for the supply chain, targeting support where it would have the most impact rather than diluting it across too many issues.
- Government considers that biodiversity, community and planning-related questions in non-price factors may be best dealt with at earlier stages of the development and consent cycles of a project. Government will consider proposals around innovation.

## Question ten

Question ten invited views on whether valuing non-price factors is the right approach to address the specific issues identified related to system flexibility, operability and locational signals, and whether there could be any unintended consequences or better ways to address these issues through the CfD scheme or other policy instruments.

### Responses to the call for evidence

There was a total of 56 responses. 45 respondents disagreed that non-price factors are the right approach to addressing the issues related to system flexibility, operability and locational signals. 5 respondents agreed and 6 were neutral or unclear.

### Views on the proposal and government response

Most respondents disagreed with addressing issues relating to system flexibility, operability and locational signals through non-price factors in the CfD.

Many respondents felt these issues should be addressed holistically through REMA and cited alternative market mechanisms that would be more appropriate or effective in addressing these issues at a system level. A few respondents raised concerns about the difficulty of designing consistent and transparent factors for these issues.

Regarding system flexibility and operability, respondents raised concerns about the unintended consequences of seeking to address these issues through the CfD, such as over-incentivising co-located storage relative to other forms of flexibility, and the difficulty of assessing the value of flexible assets to the system, which depends on their location and can vary over time.

On location, many respondents stated that CfD projects would not be able to respond to a locational non-price factor, as decisions take place years ahead of CfD allocation rounds and are largely driven by other factors, including leasing, planning and grid accessibility, so this could lead to an increase in costs and termination of projects rather than them moving to a different location.

**Policy response:**

- Taking into consideration the responses received, government agrees that these issues may not be best addressed through non-price factors mechanisms at this time.
- Government may return to consider whether this could be an appropriate approach for some issues, depending on the outcome of the REMA process and pending further analysis.

## Question eleven

Question eleven invited views on whether there are any other issues identified in the REMA case for change that could be addressed through non-price factors.

### Responses to the call or evidence

There was a total of 40 respondents. Out of 40 respondents, 30 disagreed, 10 provided other suggestions or were neutral.

### Views on the proposal and government response

Most respondents did not think that any other issues identified in the REMA case for change could be addressed through non-price factors in the CfD, with many citing that this was not the right mechanism to address system-level issues raised by REMA.

**Policy response:**

- Taking into account the responses received, government agrees that using non-price factors to address other issues identified in the REMA case for change should not be pursued further at this time.

## Question twelve

Question twelve is focused on what financial value would need to be attributed to the potential factors outlined above to incentivise ambitious behaviour for each topic.

### Responses to the call for evidence

There was a total of 52 responses outlining the type of financial values attributed to the potential factors.

### Views on the proposal and government response

Respondents noted that assigning financial value to non-price factors will require a lot of analysis and modelling, though no specific ranges were put forward. They also stated that

value of extra revenue support should be substantial to ensure developers can recoup their investments and generate profits.

**Policy response:**

- Government intends to undertake further analysis to develop the evidence base on cost of delivering non-price factors, in line with the views of respondents.
- As flagged under question four, any revenue support model set up by government needs to meet value for money requirements and be subsidy control compliant, meaning that they would need to be proportionate to the cost of any additional actions delivered under non-price factors, in particular having regard for the cost to consumers as per the Energy Act 2013.

## Question thirteen

Question thirteen asked for views on whether there are alternative ways of measuring and monitoring the non-price factors other than the examples outlined in this Call for Evidence (in terms of quantifying and valuing). The government was also interested in views on whether there are any factors where a more qualitative method of assessment would be more appropriate.

### Responses to the call for evidence

There was a total of 45 responses that discussed alternative ways of measuring and monitoring the non-price factors.

### Views on the proposal and government response

Over 70% of respondents felt qualitative assessments should be kept to a minimum, with over 50% of those wanting qualitative assessments ruled out altogether.

The majority of respondents expressed the view that qualitative assessments for non-price factors introduced increased complexity and administrative challenges onto developers and government, and that qualitative criteria were more susceptible to ambiguity and legal challenge.

A few respondents felt qualitative criteria should be used to assess sustainability and environmental criteria as this is challenging to access quantifiably.

**Policy response:**

- Taking into account the responses received, government agrees that qualitative approaches could be inappropriate in some cases because of ambiguity they may present and will therefore explore wherever possible, quantitative, objective and measurable methodologies for measuring non-price factors.

## Question fourteen

Question fourteen invited views on how we could measure non-price factors to value system flexibility, operability, and location.

### Responses to the call for evidence

There was a total of 42 responses. 6 responses provided suggestions on how to measure system non-price factors.

### Views on the proposal and government response

Most respondents did not provide suggestions for how to measure non-price factors to value system flexibility, operability, and location, with many stating that it would be very difficult to design a consistent, objective and transparent set of factors to measure the value of these system benefits.

A few respondents gave suggestions for measuring the system benefits of CfD projects as non-price factors, such as measuring the capacity of energy storage or other flexibility services they could provide, their ability to reduce grid congestion or constraints, their proximity to demand centres, and the estimated impact of their location on constraint charges.

#### **Policy response:**

- Taking into account the responses received, government notes the challenges identified in how to design factors that measure these system benefits. As set out in the response to question ten, government agrees that these issues may not be best addressed through non-price factors mechanisms at this time. Government may return to consider whether this could be an appropriate approach for some issues, depending on the outcome of the REMA process and pending further analysis.

## Question fifteen

Question fifteen asked for views on whether any of the models for implementing non-price factors (top-up, bid re-ranking or valuation formula), were more likely to be more effective for certain non-price factors than others.

### Responses to the call for evidence

There was a total of 47 responses that provided views on whether some models were more likely to be more effective when matched with certain non-price factors than others.

### Views on the proposal and government response

This question was not directly answered by the majority of respondents. In the majority of answers, respondents either repeated their rationale for their favoured model or took the opportunity to emphasise that non-price factors need to be transparent and fairly applied.

**Policy response:**

- Taking into account the responses received, government will explore the interaction between models likely to be viable, and the choice of non-price factors in greater detail.

## Question sixteen

Question sixteen was focused on compliance (i.e. enforcement, penalties and monitoring compliance). Views were invited on whether the compliance and penalty options proposed for non-delivery were appropriate and proportional, and whether other alternatives could be considered.

### Responses to the call for evidence

There was a total of 53 responses. 29 respondents agreed that one or more of the options presented were proportionate and appropriate. 11 respondents were neutral, and 13 respondents disagreed with the options set out.

### Views on the proposal and government response

Most respondents to this question provided advice on high-level principles for any compliance regime that should be adhered to, rather than directly engaging with the specific options set out in the Call for Evidence.

Some respondents were supportive of top-up withdrawal as a penalty, stating that it would be proportionate as the penalty would match the original incentive. However, some respondents were concerned that withdrawal of only the original top-up amount would encourage developers to commit to NPFs without any intention of delivering them in order to win a CfD.

Some respondents suggested an additional financial penalty or charge to act as further deterrent or cover public costs. Relatedly, some respondents noted the importance of penalties to minimise gaming of the system.

Many respondents stated that more granularity on the proposed non-delivery penalties and overall non-price factor mechanism, in particular quantification of the uplift to the revenue support itself and associated penalties, was required to reach a definitive view.

**Policy response:**

- Taking into account the responses received, government will consider developing more detailed compliance mechanisms, taking into account the principles outlined in the responses.

## Question seventeen

Question seventeen asked for views on when would be the best point to introduce non-price factors in the CfD process and whether the government's initial suggestion (up to 2 years in advance) was appropriate.

### Responses to the call for evidence

There was a total of 68 respondents. 30 respondents agreed and 14 disagreed. The remaining 24 respondents were neutral or unclear.

### Views on the proposal and government response

Some respondents have cited that they are comfortable with the introduction of non-price factors at any stage, but most involved in offshore and floating offshore wind would prefer non-price factors introduced at the seabed leasing stage when schemes are being developed, to support the alignment of CfD and leasing processes.

#### **Policy response:**

- Taking into account the responses received, government agrees that there may be benefits to generalising non-price factors at leasing stage for offshore wind in the long term, however significant offshore and floating offshore wind capacity is already leased, and government therefore believes that a policy mechanism covering this capacity may be desirable.
- Should the policy be pursued, in so far as it concerns offshore and floating offshore leasing processes, the government could work with both Crown Estates to align the development of non-price factors.
- The government recognises that investment lead-in times are critical for non-price factors to be effective and will consider ways of giving as much notice as possible to drive that investment in a predictable and stable way.

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