Department for
Energy Security
& Net Zero

Contracts for Difference for Low Carbon Electricity Generation

Government Response to the Consultation on Introducing a CfD Sustainable Industry Reward

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Context

The Contracts for Difference (CfD) scheme is the government's main mechanism for supporting new low-carbon electricity generation projects in Great Britain. As part of the government's Net Zero agenda, the government has committed to a fully decarbonised electricity system by 2035, subject to security of supply considerations, with an ambition to deploy up to 50GW of offshore wind by 2030, including up to 5GW of floating offshore wind. Delivering this will require rapid and sustained scale-up of renewable electricity deployment. The Contracts for Difference (CfD) scheme is fundamental to achieving this goal, supporting investment in low cost, low carbon electricity generation.

Recent macroeconomic, geopolitical and social trends have made the supply chain for offshore wind and floating offshore wind increasingly challenging from an economic, social and environmental perspective. Component costs have increased, and many supply chain companies have struggled as a result, deployment targets have increased faster than manufacturing capacity, the carbon footprint of the industry remains substantial, and consumers rightly expect to see more benefits from greater renewables deployment in terms of economic and environmental gains. In short, there are challenges for the economic, environmental and social sustainability of these supply chains. We need an industry which can weather economic and global challenges and deliver sustainable deployment now and in future.

The government is looking at ways of amending the Contracts for Difference (CfD) scheme to address the challenges facing the offshore wind and floating offshore wind industry described above, including recommendations stemming from the Offshore Wind Acceleration Taskforce report. As a result, the Department for Energy Security and Net Zero (DESNZ) launched a Call for Evidence on 17th April 2023 to consider the ways in which the scheme could capture the wider value of renewable projects, specifically by introducing non-price factors. The government response was published in September 2023[1]. The government now refers to these non-price factors as CfD Sustainable Industry Rewards (SIRs), as a more accurate description of how the policy could work.

After further consideration following the Call for Evidence, the government decided to put forward more refined ideas for consultation in November 2023, detailing a full proposal on how the CfD Sustainable Industry Rewards could work and help address the issues outlined above by driving investment in a more environmentally, socially and economically sustainable offshore wind and floating offshore wind supply chain.

[1] https://www.gov.uk/government/calls-for-evidence/introducing-non-price-factors-into-the-contracts-for-difference-scheme-call-for-evidence

Overview of consultation proposals

On 16th November 2023, the government published a consultation on Introducing a CfD Sustainable Industry Reward from Allocation Round 7 onwards.

The aim of CfD SIRs is to help accelerate the deployment of low carbon electricity generation, specifically offshore wind and floating offshore wind, by addressing some of the challenges that have been identified by the industry, in particular providing more revenue support through the CfD for investments that a “price only” approach might otherwise undervalue, despite their overarching benefit for healthier, more sustainable means of production and deployment.

The consultation sought views on a number of proposals, including the government’s preferred option of introducing an industry-led reward mechanism for both allocating and valuing SIRs as well as the proposed SIR criteria to be used that aim at increasing the economic, environmental or social sustainability of supply chains.

The consultation closed on 11th January 2024.

Engagement with the consultation proposals

The consultation was published online and ran from 16th November 2023 to 11th January 2024. Responses were submitted through an online response tool Citizen Space and by email. The consultation received 74 responses, out of which 30 were from developers of renewable generating stations, 23 were from trade associations and public bodies, 21 supply companies and Ports.

Next steps

Alongside this government response, the government has published a draft CfD SIR allocation framework, which has been published on GOV.UK, for further consideration by the offshore wind and floating offshore wind industry. An Impact Assessment will also be released on GOV.UK when the regulations for CfD SIRs are laid before parliament.

The Sustainable Industry Reward policy has been designed to be sufficiently flexible to align and complement wider strategies such as the Industrial Growth Plan being developed by the offshore wind industry, and the Scottish Strategic Investment Model.

Where the government’s recently announced Green Industry Growth Accelerator (GIGA) fund will provide grant funding support to help with the upfront costs of setting up new offshore wind manufacturing capacity, SIRs can support the long term sustainability of that industrial capacity by incentivising CfD applicant investment in more sustainable facilities.

Responses to the consultation

This Government response outlines the summary of the 74 responses to the 17 questions in the consultation, and the policy responses.

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 UK Government responses to consultations.

Sustainable Industry Rewards

Summary of Key Changes to the Sustainable Industry Rewards

The government wishes to thank all those who responded to the consultation for their feedback. The government has decided to introduce SIRs into the CfD from Allocation Round 7 to further support the sustainability of the renewable energy supply chain, building on the recommendations of Tim Pick (the UK's recent Offshore Wind Champion). The introduction of Sustainable Industry Rewards into the CfD is just one part of a wider picture and complements the £1.1billion Green Industries Growth Accelerator (GIGA) to support clean energy manufacturing capacity including for offshore wind and floating offshore wind.

The SIR criteria for AR7 will be "lighter-touch" with fewer criteria than consulted on, and likely fewer than in AR8 and AR9 to reflect the fact that developers will have less time to prepare their bids for the first SIR auction round. There will be different benchmarks for floating offshore wind projects compared to fixed bottom offshore wind projects, to reflect their relative size and the maturity of the technology.

In addressing many of the concerns raised in the consultation, the government has decided to amend some of the key aspects to the proposed Sustainable Industry Rewards for AR7 and simplify the process by reducing the number of criteria down to two, and the number of questions down to three.

The government is keen to simplify how SIRs can support supply chain economic, social and environmental sustainability, and proposes that the new SIR framework laid out in the draft SIR Allocation Framework appended to this government response sets out two pathways to obtaining Sustainable Industry Rewards, reflecting stakeholder feedback on how to best make the SIR criteria work. The first path is to invest in shorter supply chains to the benefit of disadvantaged communities. The second path is to invest in firms that that are actively reducing their carbon footprint.

In practice, this means that the government proposes that the criteria for Sustainable Industry Rewards will be:

- (a) Investment in shortening supply chains, in deprived areas in the UK; or
- (b) Investment in more sustainable means of production, anywhere in the world;
- (c) or combining both approaches, by investing in shorter supply chains in UK deprived areas and ensuring such investment goes to more sustainable means of production.

Shorter supply chains means that CfD applicants are taking action, where reasonably possible, to reduce the footprint of their supply chains by investing in Ports and Tier 1 supply chain capacity closer to deployment zones. The government takes the view that where investments are made closer to deployment zones, such investments should be concentrated where they are needed most from a socio-economic perspective. More sustainable means of production means that CfD applicants are using Tier 1 suppliers that have proven credential in terms of reducing their overall greenhouse gas emissions, evidenced by having set, communicated and validated Science Based Targets for the reduction of such emissions.

All proposals must relate to investment in either ports, and / or the key components listed in the SIR Allocation Framework. These are aligned with the strategic priorities identified in the forthcoming Industrial Growth Plan. Proposals are also required to meet an overall minimum standard, under the method of a minimum level of expenditure on sustainable supply chains. The minimum standard value will be set at a value equivalent to £X per GW of project capacity to ensure fairness for smaller and larger projects. The government will propose this value during the development of the draft SIR Allocation Framework. Values will be set for both fixed bottom and floating offshore wind projects and will be set before each Allocation Round to ensure they remain fit for purpose. Such a minimum standard would be required to enter the CfD auction. When setting these thresholds, the government will take on board feedback received in the consultation and agrees that it would be counterproductive to impose too high a bar on minimum standards that could inadvertently affect the amount of pipeline bidding into a CfD auction.

The government continues to propose that applicants compete against each other for CfD SIRs in a competitive auction where the highest value for money proposals win, taking on board the feedback that a competitive auction where applicants set the price of their proposals is a practical way of controlling the risk of over-compensation. Avoiding over-compensation is crucial to protect bill payers and to ensure the dynamics of the CfD auction are not impacted by the receipt or lack of an SIR award. The government is mindful of the risk of under-compensation flagged in consultation responses and has throughout the government response set out ways in which this risk can be mitigated.

The government rejects calls to move the timing of the CfD SIR process so that it takes place after CfD award, as it considers that a substantial portion of major supply chain development choices and sustainability design considerations will have been made or will be well advanced before CfD bids are submitted, as an accurate CfD bid would depend on these very factors. The government believes that moving the CfD SIR process to after the CfD auction process would not therefore result in net benefits for the supply chain, as CfD bids will have been designed primarily on a “cost-only” basis, reducing the chances and prospects of substantive engagement with more sustainable supply chain players.

The government has dropped the requirement for new facilities backed by SIRs to be created within the preceding 5 years before an allocation round, or to be set up in the future as this would too tightly constrain options for supporting a sustainable supply chain. All facilities as listed in the draft allocation framework will become eligible.

Overall, the government proposes a process that has a similar or lesser administrative burden than current CfD Supply Chain Plans. Further details and rationale for changes are provided in the government response to the consultation below.

As set out in the original consultation document, the main CfD auction will continue to run as normal, once the CfD SIR competition has been run.

The government is proposing SIRs for only three CfD allocation rounds, on the basis that it expects the fixed bottom and floating offshore wind industry to have re-established itself on a more sustainable footing after such time – baring any economic shocks – considering the proposed government support in the form of this policy, or the Green Industries Growth Accelerator.

Mechanism for Allocating Funding

Proposal

Question 1 sought views on whether the government's preferred model for allocating and valuing SIR proposals is an appropriate delivery model to avoid overcompensation, while giving applicants flexibility on how they deliver their proposals. We asked that responses include information on unintended consequences and value for money concerns, if any.

Responses to the consultation

There were 62 responses to this question with the majority of respondents agreeing that the industry-led model for delivering SIRs was the most appropriate. They agreed that a model whereby government would set the "price" of SIRs, was not preferable as government was unlikely to be able to set an accurate value on the costs of SIR interventions and therefore it was unlikely to achieve value for money. A minority preferred a model whereby government would set the "price" for each SIR intervention, arguing that the 'industry led' model introduces significant uncertainty, and it is unclear how suitable mechanisms could be put in place to effectively regulate the system and reduce the potential for gaming. Some respondents noted that "under-compensation" was likely to be a greater risk in the government's preferred SIR model (compared to overcompensation), that is the scheme could accidentally provide less revenue support than required to deliver the actions. This was because, depending on the minimum standards and "penalties" the government would set for non-delivery, and depending on how developers and supply chain were held accountable for actions under their control, bidders may make conservative bids to minimise risks. Few respondents thought that over-compensation was a risk given the competitive nature of the model.

A majority of respondents sought further details on the draft allocation framework including rules on minimum standards, penalties, scoring, before commenting further. Some respondents also preferred a "soft" introduction of SIR policy in AR7, or a delay altogether, to give more time for consultation and modelling.

Many respondents raised concerns on various issues such as the overall complexity of the proposed delivery model would advantage larger projects over smaller ones, and that the timing of SIRs could be difficult for some projects depending on their stages in the development cycle.

Though not directly related to the question, most respondents called on the government to set out more clearly how SIRs would work with the forthcoming offshore wind Industry Growth Plan, and the government's Green Industries Growth Accelerator fund.

Policy response:

Based on the feedback received, the government has decided that the CfD SIR will be implemented through an industry-led, competitive auction model as outlined in the consultation document subject to the modifications outlined in this government response. This is on the basis that the model is best suited to prevent over-compensation of applicants and deliver value for money for the consumer. In this model:

- Before a CfD round opens, offshore wind developers will be required to submit proposals to DESNZ on how they could deliver the sustainability criteria the Government is offering support for, along with their estimated cost of delivery. Developers must price their own proposal and compete against each other for funding.

- Proposals will be scored on a combination of the quality and the cost of delivering them, and the proposals will then be ranked.

- The government will publish a draft SIR budget before an SIR round opens. The government also proposes that the Secretary of State has powers to issue a final SIR budget once all applications are received, to react to the quality of the applications received, ensuring value for money for the consumer and wider energy security considerations are taken account of, and set a final budget accordingly.

- The highest scoring proposals could draw down from the available CfD SIR budget first. Funding would be assigned to each of the proposals in the order that they are ranked until the budget is exhausted.

- This industry-led, competitive auction will drive developers to deliver the highest quality proposals for their supply chains at the lowest possible cost, to secure their chance of getting funding. Which ensures the Government will see the greatest ‘return’ on its investment.

- The government believes this model has the lowest risk of gaming because of the competitive nature of funding bids, with each applicant incentivised to bid at their lowest viable cost.

It is our intention to introduce this in Allocation Round 7. We recognise industry’s calls for more details and that it why we have published a draft Allocation Framework alongside this Government response. We are keen to work with industry to refine this ahead of publishing the final auction parameters later in the year and to make sure it works well for larger and smaller projects alike. In addition, the requirements for AR7 will be more light touch compared to those of AR8 and AR9 to reflect the fact that developers will have less time to prepare their bids for the first auction round. There will also be different requirements for floating offshore wind projects compared to fixed bottom offshore wind projects, to reflect their relative size.

We continue to work closely with the Offshore Wind Industry Council in order to ensure that there are synergies between SIRs and the forthcoming offshore wind Industry Growth Plan which aims to deliver a long-term strategy to address supply chain constraints and opportunities and will be published shortly. In addition, we are making £1.1billion available for a Green Industries Growth Accelerator (GIGA) to support clean energy manufacturing capacity including for offshore wind (including floating offshore wind) and networks. This builds on previous support provided by the Offshore Wind Manufacturing Investment Scheme and the Floating Offshore Wind Manufacturing Investment scheme. These will remain complementary interventions.

Backstop

Proposal

Question 2 sought views on what kind of backstop or mitigation would you suggest the government introduces to prevent a small number of large projects capturing the vast majority of the SIR budget.

Responses to the consultation

34 out of the total 74 respondents did not answer this question. Out of the 40 respondents who did answer this question, the majority answered neutrally by providing suggestions of backstops or mitigations that the government should introduce to prevent a small number of large projects capturing the vast majority of the SIR budget. For example, a few respondents suggested that there should be a limit on the reward that a single project could receive, that there should be a cap on the size of SIR proposals made by developers, or that there should be separate pots for fixed-bottom and floating offshore wind technologies. There was no broad consensus on any of the options put forward. Among the minority of respondents who could be considered to disagree with the policy intent, there was a clear theme that the minimum standard requiring applicants to win at least one SIR to be able to take part in the main CfD auction should not be considered and, therefore, accompanying backstop and mitigation options should not be considered either.

Policy response:

As the government has chosen to pursue option 2 on minimum standards (to make it mandatory for all applicants to submit proposals for investing at least the minimum standard under given criteria, see Government Response to Question 6 below), the government considers that a “backstop” is now unnecessary, as all projects will have an equal chance of entering a CfD auction, making protections for smaller players unnecessary. Bigger or smaller applicants may still score differently depending on the size of the investments they make, but by pursuing option 2 on minimum standards, there should be no risk that bigger applicants use up all the SIR budget and prevent or make it more difficult for smaller applicants from winning at least an SIR and entering the CfD Allocation Round.

Multiple Bids

Proposal

Question 3 sought views on whether it would it be of value to applicants to allow multiple SIR bids and what the limit should be on multiple bids per criteria.

Responses to the consultation

36 out of 74 respondents answered this question. The majority of respondents are supportive of multiple bids, arguing that it would increase an applicant's chances of success. Most respondents agreed that three bids per SIR criteria would be the right balance between competition complexity and application flexibility. Most concerns focused on burdensome assessment processes and how this could negatively impact project timelines. A few respondents are concerned that multiple bids could be cumbersome for developers who have already begun procurement processes for AR7 & 8 projects. A few respondents also believe that multiple bids could favour larger players and increase book uncertainty for suppliers.

Policy response:

Taking into account the responses received, the government has decided to allow multiple variants of a proposals to support flexibility in the bidding process. The number of multiple variants will be kept at a maximum of three in line with most respondents' views. Multiple variants will be optional for applicants as we recognise that this could be more burdensome for developers. It will therefore be a choice for developers as to whether they want to submit 1-3 bids. We note the concerns around order book uncertainty. This is one of the reasons why we have decided to run the SIRs auction ahead of the main CfD auction, so that developers are aware of the outcomes before they pull together their CfD bids and can provide more certainty to suppliers as soon as possible.

Each proposal and each variant will be scored in accordance with the method set out in the SIR Allocation Framework and each proposal and each variant will be ranked alongside all other submitted proposals, in accordance with the SIR Allocation Framework.

Only one variant of an SIR proposal will be supported if successful in the SIR allocation round. Applicants will designate their order of preference for each variant, and funding will be awarded to the "most preferred", based on the method used to rank proposals and the available budget.

Full details of the multiple variants process will be set out in the draft Allocation Framework.

Timing of Awards

Proposal

Question 4 sought views on whether 6 months in advance of the opening of a CfD Allocation Round was the optimal time to hold the SIR award and valuation process, assuming a 35 working days process to assess each application and notify applicants of the results.

Responses to the consultation

There were 38 responses to the questions on the "Timing of Award". The majority of those who gave an opinion largely agreed that 6 months in advance of a CfD round opening was appropriate, provided the 35-day working process is adhered to and the proposed dispute resolution process is included and completed within the available timeframes. A few respondents disagreed, highlighting the complexity of having to prepare SIR bids for AR7 well before the results of AR6 are known in mid to late summer 2024 to ensure they are ready for submission in September. A few respondents considered a post CfD SIR allocation more appropriate as it would enable more certainty and collaboration, while a few other respondents stated that the SIRs should aligned with the seabed lease rather than the CfD auction.

Policy response:

In light of the consultation responses, the government has decided to hold the SIR auction 6-months before the opening of the main CfD Allocation Round. This will allow offshore wind and floating offshore wind developers to enter a normal CfD round knowing how much funding they have secured for more expensive, but more desirable, interventions on their supply chain.

The government acknowledges the issues around awarding SIR prior to a CfD Allocation Round. The government has therefore decided to introduce a second part to the SIR Allocation Round after the CfD auction has run. This will not be for new bids but will allow the government to recycle any SIR funding previously awarded to projects that ended up being unsuccessful in the CfD auction, to those projects that did obtain a CfD, provided their bid was of sufficient quality. This will allow viable bids that did not receive support first time around a second chance, so that the process can maximise the chances of an applicant's investment being rewarded.

Only eligible SIR proposals submitted in the initial SIR Allocation Round will be eligible for consideration in the second part of the round, subject to being of sufficient quality (as specified in the draft allocation framework). Applicants will have the choice as to whether they wish to take up the offer of re-entering the proposals for allocation on the leftover SIR budget. The process will not be compulsory.

No new funding will be allocated to the second part of the SIR Allocation Round. However, any remaining budget from the first round will be added to the total being recycled. The overall budget for the SIR Allocation Round will stay the same and will not be exceeded.

The government has concluded that SIRs should not be held too early on the basis that costs would be so imprecise and speculative as to make it hard to assign a correct financial value to the revenue support needed.

Weighting

Proposal

Question 5 sought views on what the right weighting between marks awarded for quality and marks for the price of delivery when determining the overall combined score of a proposal.

Responses to the consultation

40 out of the 74 respondents answered this question and 19 were in favour of the 60/40 split. The reasons given included that it encouraged a focus on sustainable investments and outcomes, that the split was similar to that in other jurisdictions and that it provided the best chance of driving high quality investments. Four respondents disagreed with the 60/40 split, one suggested a 70/30 to ensure the focus on high quality investments and the other three thought it should be 50/50 in order to ensure value for money. Of the 15 that answered but were classified 'neutral' the following points were made: the weighting might need to vary between different SIRs; more detail was needed on the parameters and scoring mechanisms to make a decision; they were more concerned that the criteria was objective and transparent; and that the weighting should be kept under review.

Policy response:

The government acknowledges that different approaches to weighting will attract different pros and cons. The government now proposes to remove any weighting in favour of quality or price, and have both elements scored equally to obtain a straightforward value for money assessment of a given proposal. The government tested various forms of weighting and found that increasing the weight assigned to any of the scoring metrics led to disproportionate outcomes from a value for money perspective (e.g. either favouring disproportionately more expensive bids or restricting the potential ambition of a bid). However, to ensure that proposals made to government are of sufficient quality, the government has proposed in the draft SIR allocation framework that applicants need to provide assurances as to the quality of their proposals under the form of evidence of likely impacts and proof of intentions, while keeping the administrative burden considerably lighter than existing Supply Chain Plans.

Minimum Standards (eligibility)

Proposal

Question 6 sought views on whether the government should bar applicants who have not obtained at least one SIR reward award from the CfD auction, or whether it should apply minimum standards to each SIR criteria as a contractual obligation instead.

Responses to the consultation

The majority of respondents preferred Option 2 (to apply minimum standards to the SIR criteria), as a prerequisite for participation in the CfD round, reasoning that it is more appropriate to require bidders to meet pre-defined and achievable minimum standards. The majority were strongly opposed to Option 1 (to bar applicants who have not obtained at least one SIR reward from entering the CfD) as it would be very disproportionate, and the adverse impacts of reduced competition will be much higher than the potential benefits. Some respondents thought Option 1 could be open to gaming and would require a "backstop" to protect smaller projects. Some respondents stated that more detail was required on what the minimum standards in Option 2 would be. Some respondents suggested these minimum standards should be aligned with current CfD Supply Chain Plans (SCPs), to give some continuity to the sector. Some respondents linked this to the proposed implementation timeline of Allocation Round 7 (AR7), highlighting that projects aiming for AR7 will have been conducting their procurement based on SCP requirements and so will not have time to adapt to SIRs if the minimum standards are substantially different from SCPs. Some respondents also stated that the minimum standards should be based on current industry precedent, rather than future ambition, so that in the early years of implementation of SIRs, the minimum standards are not unrealistically and unattainably high. A few respondents said the minimum standards could subsequently be kept under review and increased once SIRs are established. A few respondents highlighted the need for different minimum standards between fixed bottom and floating offshore wind, for example on environmental impact where floating wind may necessarily use more steel or concrete.

Policy response:

Taking into account the responses received, the government has decided to proceed with Option 2 and apply a minimum SIR standard to the given SIR criteria, that all applicants need to meet as a condition of entry to the main CfD auction. This option will maintain a level playing field for all projects regardless of project size or technology and removes the need for a "backstop" to protect smaller projects.

The minimum standard will be set as a cumulative total for investment made under the criteria the government proposes to introduce in the draft Allocation Framework (see further below for the amended criteria). The minimum standard value will be set at a value equivalent to £X per GW of project capacity to ensure fairness for smaller and larger projects.

The government will propose this value during the development of the draft SIR Allocation Framework. Applicants for SIRs can either meet the minimum standard with a single investment above the total minimum standard threshold or through the cumulative total of several eligible investments.

Values will be set for both fixed bottom and floating offshore wind projects. The minimum standard values will be set before each Allocation Round to ensure they remain fit for purpose. The overall minimum standard process should be simpler and less administratively burdensome to ascertain than the equivalent requirement in current CfD Supply Chain Plans.

Performance related adjustments

Proposal

Question 7 sought views on whether the government's proposals on performance related adjustments (i.e. to address non-delivery) are proportionate and enforceable. In relation to:

a. Performance related adjustments for non-delivery or partial delivery of SIR commitments.

b. Performance related adjustments for non-delivery of minimum standards.

Responses to the consultation

There were 45 responses to the question. The majority of respondents agreed that a performance related adjustment is required, but with some caveats: performance standards should be clear and objective, leaving no room for interpretation as it will increase the risk of disputes, and penalties for partial or non-delivery must be proportionate. Most respondents outlined the importance of a force majeure provision (i.e. protecting applicants against events outside their control) and suggested a sliding scale or tiered penalty structure (i.e. predictable performance adjustments based on levels of non-delivery).

A few disagreed completely with the proposal of performance related adjustments, considering the penalisation a risk to developers that might result in a risk to revenue and associated impact on achieving financing and FID. A few respondents noted that linking adjustments to bid prices may result in adverse bidding strategies and potentially gaming.

Most of the respondents strongly disagreed with the option to ban applicants from future CfD rounds for non-delivery of SIRs. This was on the grounds that this could impact future deployment rates as it will affect the pipeline of projects set out, and disproportionately harm developers with a more planned pipeline than others.

Minimum Standards (link to SIR delivery cost)

Proposal

Question 8 sought views on how much to vary an applicant's CfD payments in the event that an applicant fails to deliver the minimum standards required, whether it is appropriate to link the performance-related adjustment of CfD payments to the original SIR delivery cost the applicant put forward.

Responses to the consultation

There were 36 responses to this question, The majority disagreed with linking performance-related adjustments of the CfD payments to the original SIR delivery costs put forward by applicants. Reasons included the risk of gaming, potentially incentivising lower bids, and challenges with project financing for developers. Some suggested a performance-adjustment level set high above the original proposal value in order to mitigate gaming risk and also a tiered, set performance related-adjustment structure published in advance.

A few respondents support the link between the performance adjustment and an applicant's original SIR bid because it would act as cap on such adjustments.

Policy response to questions 7 & 8:

Taking into account the responses received, the government has decided to introduce Performance Related Adjustments to deal with both partial and non-delivery of an SIR commitment and partial or non-delivery of the minimum standard.

Partial or non-delivery of an SIR commitment

Any generator that partially delivers an SIR commitment will receive a partial SIR payment, proportionate to the level of delivery, as long as the generator has exceeded the minimum standards set out in the contract.

The formula for calculating partial delivery payments on any given criteria will be:

Total payment = Total proposed spend – Total actual spend

Any generator that does not deliver an SIR commitment (but does still meet the minimum standard) will have their whole SIR payment removed.

Non delivery of the minimum standard

Any generator that does not deliver on the minimum standard, as set out in the contract, will have the performance related adjustments applied to their quarterly CfD payments, until the full value of the performance related adjustment has been recouped.

These adjustments will be equal to the difference between the total minimum standard required, and the actual spend of the generator against that minimum standard.

Performance related adjustment

= Minimum standards – actual spend on Minimum Standards

Where “minimum standards” means the minimum standard expenditure required as part of the CfD contract.

The mechanics of how the Performance Related Adjustments will operate and the value of an SIR minimum Standard are set out in the draft Allocation Framework.

A decision was taken not to apply a ban on applicants entering a future CfD round. In this instance it was considered that a system of financial penalties would be more proportionate and could be applied fairly across both larger and smaller projects.

Dispute Resolution Mechanisms

Proposal

Question 9 sought views on dispute resolution mechanisms (at both application and payment stage) and what sort of independent panel body, or independent members, would be appropriate for DESNZ to appoint.

Responses to the consultation

There were 36 responses to this question and most respondents support the introduction of a dispute resolution process. Respondents outlined the importance of an independent and impartial panel that has industry expertise. A few respondents emphasised the importance of selecting panel members without vested interests and biases. Most respondents outlined the importance of timing as to ensure the process occurs ahead of the CfD round. A few respondents suggested a dispute process for the post-award stage only, not the application stage due to the concerns over impacts on the timing of the CfD round.

Views on proposals and government response

Policy response:

In line with the consultation responses, the government has decided to set up an external independent dispute resolution panel to deal with disputes during the SIR application stage. The aim is to deal with disputes fairly and quickly. The dispute should be settled within the overall time allotted for SIR applications if at all possible, so as to not delay the SIR and CfD process. Government has decided to not proceed with an independent panel for the post-award stage, owing to the different skill sets required to manage contractual disputes. Any disputes post award stage will be settled through contractual mechanisms or ultimately recourse to judicial review.

The government will consult with industry on the makeup of the expert panel. Further details of the dispute resolution process are set out in the draft SIR allocation framework and any associated guidance. The SIR dispute resolution panel will be separate to the CfD appeals process.

Sustainable Industry Rewards Criteria

SIR Criteria

Proposal

Question 10 sought views on whether the proposed SIR criteria are appropriate considering the government's policy objectives, and should others be considered?

Responses to the consultation

The majority of respondents agreed that the SIRs are 'appropriate', but voiced concerns as to the lack of clarity on proposed criteria and the ambiguity surrounding how the proposed criteria were to be scored, and highlighted problems regarding the location and definition of 'deprived areas'.

A few respondents disagreed that the proposed criteria were appropriate as they were not sufficient to stimulate supply chain growth and lacked funding for innovation. A few other respondents thought expenditure throughout the operational phase, rather than just the capital expenditure phase, should also be accounted for considering the major potential for supply chain sustainability. Respondents also questioned if there was a synergy between the SIR criteria proposals and other government initiatives like the Scottish Strategic Investment Model or the UK Industrial Growth Plan.

Deprived Areas

Proposal

Question 11 sought views on whether the deprived areas SIR criteria reward applicants effectively so that they are incentivised to invest in manufacturing facilities, deployment infrastructure (such as ports), skills and R&D within deprived areas.

Responses to the consultation

48 respondents answered this question. The majority did not agree that the deprived areas SIR criterion would reward applicants effectively so that they are incentivised to invest in manufacturing facilities, deployment infrastructure (such as ports), skills and R&D within deprived areas. Among the reasons for this, a few respondents indicated that greater clarity on the precise areas considered to be deprived was needed, while others thought investments in manufacturing facilities or ports should not be limited to deprived areas. Some argued that the definition of new manufacturing capacity should be changed to reward investments in more existing infrastructure, some thought the definition of deprived areas should not include deprived areas outside of the UK, and a few made the point that there should be greater clarity

on how CfD SIRs will integrate with collaborative investment programmes and wider industry initiatives.

A few respondents agreed that the deprived areas SIR criterion would be beneficial for the offshore wind industry and bring a range of wider economic and social benefits to deprived areas.

Policy response to question 10 & 11:

After careful consideration of responses and taking into account the complexity of some of the proposed criteria, the speed of introduction and calls for a "softer" launch the government has decided to reduce the number of criteria down to two, spread across three questions. The original question on deprived areas, considering feedback received, has been remodelled partially. The new criteria will be as follows:

Investment in shorter supply chains, in UK deprived areas.

The purpose of this metric is to reward investment in shorter supply chains that have a smaller global environmental footprint because they are closer to the deployment zones, while ensuring that investment supports more deprived communities in the UK. Investments would continue to be in Ports and in Tier 1 supply chain companies for fixed/floating offshore wind. The methodology for UK deprived areas would remain the same as consulted on, with some adjustments made to more sparsely populated areas in Scotland, referenced in the draft allocation framework. NSEC data on deprived areas were not sufficiently comparable with existing UK data to make the metric fair and transparent, and therefore had to be discounted.

The government is retaining the focus on deprived areas, however, as it is important that any form of revenue support has the biggest possible impact – expenditure in deprived areas has a bigger impact on the local economy and communities compared to the equivalent expenditure in more affluent areas.

Investment in more sustainable means of production.

This metric rewards investment in Tier 1 fixed/floating offshore wind manufacturing firms that have set and validated Science Based Targets (for the reduction in greenhouse gas emissions in production in line with the Paris Agreement). These firms can be anywhere in the world, including the UK. This criterion will carry equal weighting to the first criteria.

Investment in shorter, more sustainable means of production, in UK deprived areas.

This metric will combine Criteria 1 and 2, meaning that an applicant will be rewarded for investing in a Port or a Tier 1 manufacturing facility in a UK deprived area, if that facility is also signed-up to Science Based Targets. This metric effectively rewards investment that have the biggest sustainability impacts: shorter supply chains, cleaner companies, socio-

economic benefits for deprived communities. *More detail is provided in the draft allocation framework.*

The government is committed to promoting a sustainable offshore wind supply chain either through more sustainable means of production or shorter supply chains. The government is also conscious that it needs to maintain the social acceptance of the communities that host these large infrastructure projects on their doorstep. Focusing an SIR criterion on "deprived areas" will help drive investment into many of these communities. Creating a "win-win" both for local communities, who will see tangible benefits to host projects, and for the offshore wind industry who will benefit from shorter and more resilient supply chains.

The "5 year" rule on new and upgraded facilities will no longer apply, considering feedback and recognising the benefits of making existing as well as new supply chains more sustainable.

Note that the government has decided to maintain the focus on capital expenditure phase, rather than operational expenditure – most of the supply chain constraints are currently concentrated in the former.

SMEs

Proposal

Question 12 sought views on whether rewarding applicants with projects spending a greater percentage of total DevEx and CapEx on SMEs would lead to an increase in the amount of project spend that goes to SMEs.

Responses to the consultation

41 out of the 74 responders answered this question. Of these 29 opposed the introduction of a criterion on setting a percentage of total DevEx and CapEx spending on SMEs. 11 were in favour, with 1 saying it was difficult to state with any certainty.

The reasons given for disagreeing with the proposal included:

- That it favours smaller projects, as larger projects would need to contract with a larger number of SMEs.
- Developers generally have limited direct contracting with SMEs.
- Developers may be able to pass incentives for use of SMEs to Tier 1 suppliers, but developers will then not be responsible for this spend, adding to complication and risk.
- Likely to lead to highly complex discussions/negotiations with Tier 1 suppliers and to equally complex interactions between Tier 1 contractors and their sub-contractor supply-chain.

- Risk of large suppliers being able to set up subsidiary SMEs as a method of taking advantage of this criterion.
- Additional management and contingency costs on top of potentially higher direct costs.

Those that supported the criteria as having the potential to increase SME spending, still had some concerns that need addressing. Such as:

- The minimum % spending going to SMEs should ensure the right balance of supporting emerging and scaling businesses, whilst continuing to ensure projects are financially viable.
- A mechanism to prevent larger developers ‘buying up’ all relevant capability/capacity.

Proposal

Question 13 sought views on what extent would it be burdensome for developers and Tier 1 suppliers to collect the requested information project DevEx and CapEx spend that goes to SMEs?

Responses to the consultation

36 out of the 74 responders answered this question. Of these, 20 considered the introduction of a criteria on setting a percentage of total DevEx and CapEx spending on SMEs to be burdensome. 13 considered collecting the data straightforward, while 2 thought clear definitions on key terms would be required to fully understand the extent to which this would be burdensome.

The reasons given for considering the proposal burdensome included,

- Data will be difficult to collect both administratively and on a commercial/legal basis, and the quality of data may be difficult to validate via third parties without significant cost.
- Challenging to put the requisite monitoring and information gathering systems and legal processes in place especially at short notice.
- Generally, developers contract directly with Tier 1 suppliers. Whilst this data could be requested as part of Tier 1 contracts, typically a developer will not know exactly how much is spent with SMEs in monetary terms and this is often commercially sensitive data.
- Tier 1 suppliers may wish to retain flexibility and confidentiality on their contracting decisions, which would limit developers’ ability to adjust to the use of the SMEs SIR criterion.
- Additional delivery and interface risks, with higher management and contingency costs likely.

Those that supported the SME spend criteria thought that this mechanism provides incentive to enable non-UK based Tier 1 contractors to improve the stimulation and investment in the UK supply chain. That the data collection itself should not be excessively burdensome as suppliers are already supplying vast amounts of information to developers. The addition of this metric would seem small. Although some recognised that influencing the choice of suppliers is likely to be challenging as many Tier 1's will prefer to retain flexibility and confidentiality about the detail and breakdown in spend.

Proposal

Question 14 sought views on what would be an appropriate minimum, medium and maximum thresholds by which to score applicants against the SME SIR criteria and why? For example, a minimum threshold might be that at least 5% of a project's DevEx and CapEx spend goes to SMEs.

Responses to the consultation

28 out of the 74 respondents answered this question. Most of those who are opposed to the introduction of a SME spend criteria, reiterated their opposition. Adding that some lower tier supplies are not themselves SMEs but the sector still needs their components to ensure offshore wind is a success.

A few respondents suggested some research was needed before setting thresholds to score applicants against.

A few respondents who supported the introduction of a SME spend criteria considered a target of 5% was too low and a more stretching target should be used.

One respondent considered 5% a reasonable threshold but questioned whether the SIR is the most appropriate vehicle for stimulating SME growth / contribution to the sector.

Policy response to Questions 12 - 14:

After consideration of the responses to questions 12, 13 and 14, the government has decided not to include the SMEs SIR criterion as one of the SIR criteria, at least in the initial allocation round.

The government accepts that it would be too burdensome for developers and their Tier 1 suppliers to accurately collect the requested information currently in terms of additional costs, the complexities of gathering the information and having it validated, the commercial sensitivities of the information as well as additional delivery and interface risks to a developer. The government also acknowledges that the SMEs SIR criterion as currently drafted could be open to gaming.

The government is willing to consider, for CfD Allocations rounds post AR7, evidence from the sector as to how a criterion on SMEs could be made to work that address the problems identified in the consultation. Government would need to be convinced that there are ways of approaching this question that are administratively simple and methodologically robust before considering this criterion any further in future.

Joint Industry Programme methodology

Proposal

Question 15 sought views on whether the Carbon Trust's Joint Industry Programme methodology is an appropriate, and effective, means by which to measure the CO2 emissions of fixed and floating offshore wind projects.

Responses to the consultation

36 respondents answered the question, the majority of respondents agreed that the Carbon Trust's Joint Industry Programme methodology could be an appropriate, and an effective, means by which to measure the CO2 emissions as it offers a standardised and collaborative approach. However, it was noted that its implementation can be complex and resource intensive, posing challenges for smaller projects or developers. A few neutral respondents highlighted that the Carbon Trust methodology has yet to be published making it difficult to comment on.

Of those that disagreed, a few respondents highlighted cost as an issue and noted that requirements under a carbon focused SIR need to be proportional and not burdensome to projects, which otherwise could render unintended consequences. Other reasons for disagreement included the possibility that some projects with specific features could be unduly discriminated against, such as those projects further out to sea. An alternative methodology, PAS 2080, was suggested for consideration, given it is recognised as best practice for managing carbon in infrastructure.

Policy response:

The government acknowledges that the Carbon Trust's Joint Industry Programme methodology has not yet been finalised and is still under ongoing consultation with the industry. Therefore, it would be premature to introduce the decarbonisation outputs SIR criterion in Allocation Round 7. The government has decided to delay the introduction of the SIR criterion linked to the Joint Industry Programme, at least until the methodology has been finalised and agreed. Consequently, this criterion may be introduced in Allocation Round 8 at the earliest and will be subject to further conversations between the government and industry.

Science-Based Targets

Proposal

Question 16 sought views on whether science-based targets are an appropriate standard by which to determine the sustainability of suppliers' manufacturing and procurement practices and whether there are alternative measures the government should be considering that are easily measurable and verifiable.

Responses to the consultation

38 respondents answered the question. The majority of respondents agreed that science-based targets are an appropriate standard by which to determine the sustainability of suppliers' manufacturing and procurement practices. The reasons given included that science-based targets are an objective standard, comparable between projects and are a good indicator of a business's commitment to operating sustainably. A few respondents disagreed and were concerned that the validation process for science-based targets may be too lengthy and that developers should not be penalised were their SIR proposals not delivered due to delays in verification.

A few respondents suggested alternative measures which they considered more easily measurable and verifiable, including CDP, Environmental Product Declarations, GHG protocol and life cycle assessments.

SBTi (minimum thresholds)

Proposal

Question 17 sought views on what would be deemed to be appropriate minimum thresholds by which to score applicants against the SBTi criteria. For example, a minimum threshold might be that at least 20% of a project's Tier 1 suppliers have set, and are pursuing, science-based targets that have been submitted for validation and communicated.

Responses to the consultation

30 out of the 74 responders answered this question. Some respondents did not state a preference on the threshold limit but instead highlighted the difficulty in identifying an appropriate minimum threshold due to the current lack of information on what percentage of the supply chain already have, or are due to have, SBTs in place.

A few respondents advocated for significantly higher ambition than the 20% threshold set out, stating the importance of an ambitious threshold based on the long-term level of sustainability required rather than minimum acceptable level.

A few respondents proposed that this SIR has an initial 'soft launch' – e.g. is optional or qualitatively assessed - as part of a data gathering exercise before potential adoption in future.

A few respondents suggested that the proposed SIR focus on the percentage of project value allocated to suppliers with SBTs in place or designate a minimum percentage of supply chain spend on those that do, rather than focusing on the number of individual suppliers. Other respondents noted that SBTs may not be suitable for all of the supply chain, including Tier 1 marine contractors, or conversely advocated for the inclusion of the supply chain beyond Tier 1.

Policy response to question 16 & 17:

After careful consideration of the consultation responses and wider feedback, the government has decided to change and refocus the criteria on Science Based Targets.

The government proposes to reward applicants for investments made in Tier 1 manufacturers that have set and validated Science Based Targets (rather than initially rewarding total uptake of such suppliers in a developer’s supply chain). The government will propose in the draft allocation framework an appropriate minimum standard of investment against this, and the other criteria flagged in responses to question 10 & 11, based on analysis of likely costs linked to such investments.

The government is keen to clarify that it wishes to support more sustainable forms of production, but that these need to be rigorously validated and demonstrated as such, and that other targets proposed by respondents lack the same form of robust external verification that Science Based Targets offer, as the majority of relevant off-the-shelf sustainability metrics tend to rely on reporting without sufficiently robust external verification.

Further details of how the Science Based Target will work is set out in the government response to question 10 &11.

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