Department for Energy Security & Net Zero

Second Hydrogen Allocation Round (HAR2)

Due Diligence and Cost Assurance Guidance

April 2025

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HAR2@energysecurity.gov.uk

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Section 1: Process Overview

1.1. Background and Introduction

In the Autumn Budget 2024, we confirmed support for 11 green hydrogen projects from the First Hydrogen Allocation Round (HAR1), comprised £90 million in capital grant support through the Net Zero Hydrogen Fund, and over £2bn revenue support through the Hydrogen Production Business Model. We have now signed Low Carbon Hydrogen Agreements with 5 of the 11 projects, with a combined capacity of 65.6 MW. We expect to sign contracts with the remaining projects shortly. The new projects, stretching from the Southwest of England to the Highlands of Scotland, are expected to deliver 124 MW[1] of low carbon production capacity, and will invest over £400 million up front over the next three years, in a major boost to the UK's green economy. We expect all of these projects to be operational by the end of 2026.

Building on the success of HAR1, we launched Hydrogen Allocation Round 2 (HAR2) in December 2023 and received project applications for HAR2 on 19 April 2024.

On 7 April 2025, we announced that 27 projects have been shortlisted for HAR2, located across England, Scotland and Wales. These projects are now invited to take part in the next stage of the allocation process of Hydrogen Production Business Model (HPBM) revenue support. This document sets out guidance for projects participating in the due diligence and cost assurance process. A project's inclusion on the shortlist does not guarantee Government support and it is unlikely that, similar to the First Hydrogen Allocation Round (HAR1), all projects will be successful. As such being on the shortlist does not imply availability of funding for any of the shortlisted projects.

Growth is the number one mission of this Government, and our new Industrial Strategy will be central to that growth mission. The Modern Industrial Strategy, which is expected later this year, will focus on the sectors which offer the highest growth opportunity for the UK economy and business, which includes clean energy industries. HAR2 will be part of upcoming growth opportunities for the UK economy and businesses.

We are looking at improving the visibility of the supply chains for developers and suppliers including through, for example, a Meet the Specifier event, where developers would meet with potential suppliers prior to procurement. We are also separately exploring options where we could invest further into shorter and more sustainable supply chains through Hydrogen Allocation Round 3 and beyond.

This guidance is published in addition to the HAR2 application guidance[2] which contains information and caveats about this allocation round and its process and unless expressly superseded by this guidance document, remains relevant.

[1] MW H2 HHV - When considering hydrogen production capacity, we care about the maximum MW of hydrogen output of the facility in high heating value terms before load factor or plant availability are taken into account.
[2] HAR2 Application Guidance (2023) https://www.gov.uk/government/publications/hydrogen-allocation-round-2

1.2. Objective and structure of Due Diligence and Cost Assurance

Shortlisted projects who confirm their intention to participate in the next stage of HAR2 will take part in due diligence and cost assurance. Information on negotiations and the 'Agreeing an Offer' stage of HAR2 will be shared with Projects in due course.

1.2.1. Timelines

Shortlisted projects must follow the process set out below. For further information on each of the stages, please see the relevant section within this guidance document. Please note that the HAR2 timeline has been updated, however, dates are indicative, and government reserves the right to alter these timelines at any stage in the process.

HAR2 stage	Description	Date
HAR2 shortlist announcement	DESNZ announced a shortlist of projects who are invited to the next stage of the allocation process.	7 April 2025
Request for Information (RFI)	Projects will be required to complete and submit Request for Information (RFI) documentation (See Section 2.1).	6 weeks
Broadcast meeting	DESNZ intends to carry out a session to support projects with the next stage of the process.	During the RFI period
RFI project engagement	DESNZ intends to meet bilaterally with shortlisted projects to provide an overview of the process and understand project progression since application stage.	During the RFI period
Due diligence and cost assurance	DESNZ will undertake further investigation and scrutiny of shortlisted projects using RFI returns (See Section 2.2). DESNZ will carry out a detailed review of the submitted cost data (See Section 3).	10 weeks

1.2.2. The Hydrogen Production Business Model (HPBM) and Low Carbon Hydrogen Agreement (LCHA)

The Low Carbon Hydrogen Agreement (LCHA) is the private law contract underpinning the Hydrogen Production Business Model (HPBM). Applicants are encouraged to engage legal advisors at their earliest convenience, since good familiarity with the Standard Terms and Conditions of the LCHA is vital to the HAR2 process.

The LCHA Standard Terms and Conditions (i.e. LCHA V-HAR1) and the Front End Agreement template, both December 2024 versions, were published on gov.uk in February 2025[3].

Shortlisted applicants will be informed of updates or revisions for LCHA V-HAR2 (i.e. the version of the LCHA to be used for HAR2) in the near future, and we plan to engage with stakeholders in advance of the draft LCHA V-HAR2 being circulated later in 2025. As such, any references to the LCHA within this document should be read accordingly – i.e. as provisional pending finalisation of LCHA V-HAR2.

Project-specific variables (for instance, those relating to the target commissioning date and strike price) will be set out in the LCHA Front-End Agreement for each successful project.

The email address to direct LCHA queries to is hydrogen.businessmodels@energysecurity.gov.uk.

Risk-Taking Intermediaries (RTIs)

The sale of hydrogen volumes to Risk-Taking Intermediaries (RTIs) is currently ineligible for subsidy under the HPBM. By RTI, broadly we mean a person that purchases hydrogen for the purpose of resale. This reflects the need to enforce HPBM conditions regarding the end use of hydrogen (including that volumes exported for use outside the UK are not eligible for HPBM subsidy and that volumes used for feedstock pii?urposes attract a different level of HPBM subsidy). It also reflects government's view that, at this early stage of the hydrogen economy, subsidising sales to RTIs would not provide value for money. This is specified in the LCHA Standard Terms and Conditions.

Through this position, Government is seeking to allow non-RTIs to play a role in the market. Such parties may charge a fee to a hydrogen producer (or end user) for a service (e.g. brokerage or hydrogen storage) but do not take ownership of the hydrogen sold by a hydrogen producer. In addition, volumes of hydrogen not supported under the HPBM may be sold to an RTI or may be claimed under the Renewable Transport Fuel Obligation (RTFO).

The Department is aware there may be situations where a Producer would like to enter into an arrangement with an affiliate entity to supply hydrogen on the Producer's behalf. This may be a result of the other entity having experience in sales and marketing. We invite projects to notify HAR2@energysecurity.gov.uk if they intend to implement this type of arrangement.

[3] Low Carbon Hydrogen Agreement DESNZ (2025)

1.2.3. General considerations and ways of working

A significant amount of collaboration and coordination is expected during this period from all applicants. In particular, the shortlisted Projects would be expected, amongst other things, to be:

- At an advanced stage with their project development;
- Able to demonstrate high confidence in the engineering and commercial proposal, for example, minimising contingencies, be at an advanced stage with their FEED, have agreements in place with main contractors and suppliers appropriate to the stage of project development and that they are committed to optimising the design of their Project;
- Committed to optimising the design of their Project in a cost efficient manner[4];
- Able to move forward with all the regulatory processes and consents needed to realise their Project; and
- Able to agree a programme of work ahead of a potential contract award, taking account of government processes.

Without prejudice to any other rights reserved in this document or in the application guidance, Government reserves the right to discontinue a project's application at any point.

Shortlisted Projects will need to ensure they continue to meet the eligibility criteria for HAR2. If at any point during this process Projects have any reason to believe they may no longer meet the HAR2 eligibility criteria, Projects will be expected to contact DESNZ as soon as possible[5].

Ways of working

Government will be supported by its financial, commercial and technical external advisors during the due diligence phase, with DESNZ staff continuing to lead and oversee the progression of work. These external advisors may interact with projects and participate in discussions at meetings, subject to DESNZ direction and/or supervision.

Projects are expected to provide information in a prompt manner and attend any meetings scheduled. Information provided should be complete and accurate to inform and support decision making. Delays or refusals to provide necessary information requested could lead to engagement with projects through the due diligence process being discontinued.

Government is aware that shortlisted projects remain under development and recognises that a degree of uncertainty remains in relation to some aspects, including costs, timelines and design. DESNZ will endeavour to take these uncertainties into account. However, it is

[4] See HAR2 Cost Challenge document for more information on cost-reduction: https://www.gov.uk/government/publications/hydrogen-allocation-round-2-har2-due-diligence-and-cost-assurance
[5] HAR2 eligibility criteria page 28 HAR2 Application Guidance (DESNZ 2023): https://assets.publishing.service.gov.uk/media/6604269ee8c442001a220374/hydrogen-application-round-2-application-guidance.pdf

important that projects provide DESNZ with the best available information to enable robust decision-making. Wherever possible DESNZ will endeavour to undertake this process in an efficient manner to reduce cost burden on projects while balancing considerations to ensure taxpayer money is spent in an appropriate manner. Effort will be made to avoid duplication of requests for information and engagement.

Government may also share information provided by Projects (including information within the Submissions or EOIs) with other parts of government for the purposes of policy development and facilitating coordination in certain areas if relevant. In addition, this information may be aggregated and anonymised for the purposes of engagement with external audiences.

We will also maintain a database of project cost and will use the latest available information to benchmark project cost submissions.

Section 2: Due diligence

The due diligence phase is an opportunity for government to confirm and verify any aspect of the application and to seek updated information from projects. Due diligence is anticipated to cover, but not limited to:

- Technical deliverability;
- Financial deliverability, and commercial compliance matters;
- A further Low Carbon Hydrogen Standard (LCHS)[6] compliance check, a key eligibility criterion for HAR2 projects; and
- KYC checks and media screening;

2.1. Request for Information (RFI)

Shortlisted Projects have been sent a request for information and will be expected to return this information to DESNZ.

This information will be used to conduct the due diligence assessment outlined below. If the completed returns are not received by this date, Government reserves the right to discontinue a project's application. Government reserves the right to amend this timeline at its absolute discretion and request any further information it requires from projects and other parties involved in the project such as delivery partners and offtakers.

RFI returns

Projects must provide completed copies of the relevant RFI documents found on the HAR2 landing page[7] and return the following information. The documents required for RFI returns are:

- RFI template – The aim of this document is to check the progress made since the original submission and gather more information about any areas of concern identified during the assessment. This includes:
    - Evidence – New or updated evidence should be submitted to provide assurances that key arrangements are in place or are on track to be in place by FID and COD milestones, for all aspects critical to delivery. Evidence that needs to be submitted is listed against each question in the RFI template. All submitted evidence must be referenced in the evidence register tab which is part of the RFI template.

[6] UK Low Carbon Hydrogen Standard, Version 3, December 2023: guidance on greenhouse gas emissions and sustainability criteria.
[7] https://www.gov.uk/government/publications/hydrogen-allocation-round-2-har2-due-diligence-and-cost-assurance

    - Project-specific questions – where potential risks have been flagged during HAR2 deliverability assessments, some projects may be asked project-specific questions to gather further information on specific issues not covered by the RFI questions. These should be supported by submitting evidence, where relevant.

- Financial Statement Form – Projects will be required to input financial information into this form which will be used alongside information in the RFI template to understand the financial health of the entity/(ies) being assessed.
- Project Datasheet – This document requires Projects to input and reference key information regarding their project, including estimated production costs, offtaker information and hydrogen production volumes. See Strike Price section (Section 3.3) below for further information on eligible costs.
- Hydrogen Emissions Calculator (HEC) - The Low Carbon Hydrogen Standard (LCHS) sets a maximum threshold for greenhouse gas emissions allowed in the production process for hydrogen to be considered 'low carbon hydrogen'. This calculator is focused on calculating GHG emissions from one consignment of hydrogen, according to the methodology set out in the standard. This also includes the additional Biomass Requirements for biomass and waste feedstocks. This calculator will be used to confirm whether a project is likely to be compliant with the LCHS. This includes submission of any additional supporting documentation, if required. Please note, there are two versions of the calculator: a streamlined version for electrolytic pathways, and the full version for all other production routes. Electrolytic projects using biogenic inputs to generate power should use the full version.
- Fugitive Hydrogen Emission Risk Reduction Plan – This will demonstrate how fugitive hydrogen emissions at the production plant will be minimised. Projects will have to detail the sources of emissions and their expected rate of fugitive hydrogen losses in kgH/year with justifications of estimates, measurement, and monitoring in place. A template for this plan is provided on the LCHS webpage[8] with further guidance detailed in Chapter 10 of the LCHS.

Shortlisted Projects have been contacted individually to confirm details of how to submit their RFI returns.

RFI project engagement

DESNZ intends to arrange an engagement session during the RFI period to provide an overview on the next stage of the HAR2 process. In addition, DESNZ intends to arrange meetings with each shortlisted project during the RFI period to understand how the project has progressed since application, and an opportunity to ask any questions. Shortlisted projects will be contacted about this individually.

[8] UK Low Carbon Hydrogen Standard, Version 3, December 2023: guidance on greenhouse gas emissions and sustainability criteria

2.2. Due diligence assessment

The aim of due diligence is to identify any delivery risks to shortlisted projects ahead of a potential contract award. DESNZ will continue to assess the deliverability of projects to ensure there is a credible path to deliver within the HAR2 delivery window, that projects are capable of complying with LCHA requirements (e.g. Initial Conditions Precedent) and operating viably over the 15-year term of an LCHA contract.

Once RFI returns are received from projects, submissions will be reviewed and assessed by DESNZ and its advisors. DESNZ may issue supplementary questions to projects to clarify or seek any further information. Unless specified otherwise, Projects will typically have two working days to respond to these requests. DESNZ may also request meetings with Projects to understand any aspects of the submissions further, if necessary.

Technical due diligence

Technical due diligence will be primarily based on evidence of progress since project application (e.g. design, equipment/services procurement, utility connections, electricity/offtaker agreement, planning, consenting), as well as scheduled plans for delivery. This includes assessment of progress against the planning Initial Conditions Precedent (ICP) and Milestone Requirements, key contractual requirements of the LCHA.

Throughout the RFI Technical submission, projects should aim to give DESNZ confidence in their deliverability. DESNZ will continue to assess risk to deliverability as per the definition below.

Deliverability Definition: Ability to achieve a Target Commissioning Date within the HAR2 delivery window, operate viably for the duration of a 15-year contract and comply with LCHA contractual milestones (e.g. Initial Conditions Precedent, Milestone Delivery Date Requirements).

Minimum Expected Evidence: minimum expected evidence requirements have been set out against all criteria in the RFI Technical section. These requirements represent the ambition of maturity for projects in the HAR2 process and are not a pass/fail criterion for the initial due diligence submission. Projects should provide quality evidence and be clear where minimum expectations are not fully met, demonstrating they are on track to meet these expectations.

Financial due diligence

Financial due diligence will be primarily based on assessing additional evidence submitted at this stage in relation to the applicant's organisational structure, financial health and funding plan proposal. The assessment will consider evidence at project and company level for all relevant entities. The project level assessment will focus on the organisational structure and funding plan specific to the project, whereas the company level assessment is broader, encompassing overall organisational structure and the financial health of entities involved. Definitions of the Project Company, Project Sponsor and Applicant Company are included in the Financial Statement Form.

Financial and commercial deliverability assessment at the due diligence stage will involve evaluating and scrutinising the project's feasibility based on additional evidence submitted at this stage outlining applicant's capabilities and resources. This includes:

- Organisational Skills and Experience: Ability to demonstrate the necessary organisational capability required to deliver the Project is present e.g. evidence of required skills and proven track record;
- Financial Health: Ability to demonstrate the Applicant, or other entities being assessed have robust financial health and performance e.g. evidence of a strong balance sheet and access to capital, providing DESNZ confidence in the Applicant's ability to deliver the proposed funding plan or manage financial risks; and
- Credible Funding Plan: Ability to demonstrate a realistic and achievable plan has been developed to secure the required investment to reach Final Investment Decision (FID), e.g. identifying funding sources, demonstrating cost competitiveness and mitigating financial risks.

Additional Low Carbon Hydrogen Standard (LCHS) checks

We will also carry out detailed checks as further quality assurance, following eligibility assessments undertaken during the HAR2 assessment stage, to ensure projects are capable of meeting the requirements of the LCHS. The quality of the HEC submission will be assessed, highlighting any potential risks with projects ability to comply with the LCHS. The Fugitive Hydrogen Emission Risk Reduction Plan will be assessed to see the expected rates of fugitive hydrogen emissions at the production plant and the mitigating actions to minimise these emissions. If anything has changed in the Hydrogen Emissions Calculator or the Fugitive Hydrogen Emissions Risk Reduction Plan since application stage, this should be clearly highlighted in the documents returned.

Due diligence outputs and ongoing monitoring

Once due diligence is complete, DESNZ intends to engage projects about any risks identified. Projects will be expected to evidence intended mitigations for any identified risks and progress towards these mitigations will be monitored beyond this initial due diligence period. Please note, without prejudice to any other rights reserved in this document or the application guidance, we may not progress Projects if any major risks are identified.

Section 3: Cost assurance

3.1. Overview

Alongside technical and financial due diligence we will carry out a detailed review of the submitted cost data. The main objective of cost assurance will be to ascertain the credibility of cost data submitted by projects, identify areas of high cost and engage with projects to seek clarification and justification on those. The process will be the first step after shortlisting in building DESNZ's detailed understanding of projects' cost profiles and the first opportunity to scrutinise areas where available evidence suggests there could be potential for cost reductions.

We will use cost information gathered during HAR1 and HAR2, as well as available external data to benchmark the cost information submitted by projects. We will combine this with information on projects' technical design gathered during the due diligence stage and analyse costs in the context of their unique plant designs.

Where we have identified cost areas that appear elevated relative to available benchmarks, or areas where cost data is not supported by evidence of sufficient quality, we will engage with projects, requesting further justification for the proposed cost levels and, where necessary, cost revisions where insufficient justification has been provided.

Cost competitiveness

The HAR2 Cost Challenge guidance[9] advises shortlisted projects in the Second Hydrogen Allocation Round (HAR2) on achieving cost-competitiveness during the next stage. Projects must demonstrate value for money (VfM) and justify costs across key components, with an aim to achieve lower average hydrogen production costs than seen in HAR1. Success in securing a potential contract depends on the project's deliverability, alignment with strategic objectives, affordability, and the balanced distribution of cost risk between the government, developers, and offtakers. Greater engineering maturity and evidence-based cost justifications will enhance a project's competitiveness and likelihood of being awarded a potential contract.

3.2. Evidence requirements

As per the application stage, projects are required to submit specific, targeted evidence to support the submission. The quality of evidence is critical in reviewing the submission. This applies to cost assessment as much as it does to technical and financial due diligence.

[9] HAR2 Cost Challenge: https://www.gov.uk/government/publications/hydrogen-allocation-round-2-har2-due-diligence-and-cost-assurance

Government will use the data and supporting evidence submitted by applicants to assess the robustness of the cost estimates and, where necessary, will make adjustments to account for any remaining uncertainty or lack of evidence provided to support cost estimates.

Projects are therefore encouraged to provide as accurate and robust cost information as possible to reduce uncertainty about any potential future cost escalations, especially where there is a risk these would jeopardise the viability of the project. Poorly evidenced costs will be challenged by DESNZ where there is a risk a project overstates these.

The table below gives examples of cost evidence items projects should provide where possible to support the cost data in their RFI returns. Where a project is unable to provide any of the items listed below, they should explain why that is the case and explain in as much detail as possible how the cost estimate in question was arrived at, including what assumptions it was based on.

HAR2 RFI-stage cost evidence requirements

Cost Category	Cost Evidence Requirements
Funding Source & IRR	Letter of support from project's financing provider; description of the assumptions behind the required IRR where available.
H2 Volumes & Sales Price	Either a Memorandum of Understanding, Letter of Interest, an Indicative Head of Terms, a Final Contract, or any other available offtaker communications that supports the hydrogen volumes and, where available, expected sale prices reported in the project datasheet.
Electricity Volumes/Production Efficiency	Power supply indicative term sheet referencing contracted electricity volumes. Excel model outlining electricity supply and consumption profiles, where available. Electrolyser technical specification and/or plant engineering design documentation with hydrogen production rate information (kg/hr). Plant engineering design documentation with total estimated plant electricity consumption (e.g. Electrical Load Schedule).
Electricity prices	Wholesale/Generation Costs: indicative power supply contract term sheet or electricity supplier communication with

	pricing information, and/or wholesale forward curve assumptions and sources. Network costs: TNUoS, DUoS, BSUoS charges assumptions and total network costs calculations. Supplier Margins and Sleeving Costs: indicative power supply contract term sheet or electricity supplier communication with pricing details. REGOs: future price assumptions/forecasts and sources.
CAPEX	Detailed supplier quotation and/or plant engineering design report outlining cost estimates for individual CAPEX items where available.
Non-Electricity OPEX	Detailed supplier quotation and/or plant engineering design report outlining cost estimates for individual CAPEX items where available.

3.3. Strike price guidance

Initial Electrolytic Strike Price methodology

As indicated above (see 'Request for Information (RFI)' section 2.1.) shortlisted projects will submit their updated cost information through the RFI process. DESNZ will then use the submitted cost data to estimate each project's indicative strike price.

Projects will be expected to express all cost information in the RFI Project Datasheet in real 2024 prices (defined as prices corresponding to ONS Jan 2024 CPI index[10]).

Projects should note that, once agreed, the strike price value that will be included in the LCHA Front End Agreement will be defined as the Initial Electrolytic Strike Price and expressed in October 2021 prices.

The example conversion is outlined in the equation below:

$$\text{Initial Electrolytic Strike Price (Oct 2021 Prices)} = \text{Example Strike Price (Jan 2024 Prices)} \times \frac{\text{October 2021 CPI index}}{\text{Jan 2024 CPI index}}$$

[10] CPI source dataset: ONS, Consumer price inflation time series (MM23), CPI INDEX 00: ALL ITEMS 2015=100, https://www.ons.gov.uk/economy/inflationandpriceindices/timeseries/d7bt/mm23

Strike Price: Eligible and Ineligible Cost Categories[11]

The financial value of the Strike Price and the set of specific subcomponents making it up will be derived on a project-by-project basis.

It is important that the Producer pays careful attention to the following schedule of eligible and ineligible costs for HAR2.

The cost categories which are eligible to be included in the Strike Price for HAR2, subject to compliance with applicable subsidy control requirements, are as follows:[12]

- Capex and opex associated with the construction and operation of the Facility (excluding capex funded by any Approved Scheme of Funding);
- Devex associated with the planning and/or pre-construction of the Facility, where that expenditure is initiated and incurred after the Shortlisting Date, and provided that such expenditure is essential to the project achieving a significantly enhanced level of engineering maturity and cost certainty.[13]
- An allowed return on investment (referred to as the Capital Return Component);
- Input energy costs (including associated network and/or use of system charges); (though note that estimates of such costs must account for the 60% compensation offered under Elexon's Network Charging Compensation Scheme.);
- On a case-by-case basis, and where agreed with DESNZ, capex associated with the construction of limited hydrogen transport infrastructure, electricity opex associated with compressing hydrogen for transport, but not any other opex associated with hydrogen transport infrastructure. (Excluding capex funded by any Approved Scheme of Funding);
- On a case-by-case basis, and where agreed with DESNZ, capex and/or opex associated with the construction and/or operation (as applicable) of limited hydrogen storage infrastructure. (Excluding capex funded by any Approved Scheme of Funding);
- On a case-by-case basis, and where agreed with DESNZ, capex and/or opex associated with the construction and/or operation (as applicable) of electricity battery storage infrastructure, in addition to that strictly necessary for safe operation of the plant, provided that such infrastructure is not connected to the electricity grid.

The cost categories which are ineligible to be included in the Strike Price for HAR2 (and will automatically be excluded from it) are as follows:

- Indirect and direct taxes and duties (including, but not limited to, VAT charged by suppliers, green levies on electricity, import tariffs on capital equipment);

[11] Note that this represents a HAR2-specific update to the proposed approach set out in the draft Hydrogen Production Business Model Heads of Terms published in December 2022.
[12] Note that the extent to which these eligible cost categories are actually included in the Strike Price, as well as the specific financial value assigned to them, is subject to DESNZ agreement, taking several factors into account including necessity, affordability and value for money for Government.
[13] Any such spend is at your own risk and only recoverable under the terms of a signed Low Carbon Hydrogen Agreement.

- Any capex and/or opex associated with capturing additional revenue streams from the sale of By-Products;
- Any costs associated with the provision of ancillary services (including, but not limited to, liquefaction);
- Any costs incurred prior to the Agreement Date, except – where such costs were initiated and incurred after the Shortlisting Date – devex, and/or, by agreement, capital expenditure on Long-Lead Time Capital items[14];
- Any costs associated with the procurement of an auditor pursuant to the LCHA audit obligations;
- Any costs associated with decommissioning the Site and/or Facility, including e.g. land remediation.

Strike Price: Treatment of Strike Price Inclusions and Strike Price Exclusions

The primary purpose of the Strike Price Exclusion mechanism is to permit the Producer to recover from the offtaker a) the value of any costs which are ineligible for inclusion in the strike price, and b) the value of any investments which – as a matter of fact – were not funded by the Strike Price because they were deemed not strictly necessary for the project's successful delivery (i.e. were effectively self-financed by the Producer at the Producer's own risk). This latter case would typically cover e.g. the cost of capital equipment used specifically to offer 'added value' or 'bespoke' services to offtakers.

Nonetheless, there may be circumstances where the Producer wishes to exclude one or more categories of cost which are both eligible and strictly necessary for the project's successful delivery. The table below sets out our approach to this kind of case for HAR2.

Mandatory Inclusions	Negotiable Inclusions (i.e. possible exclusions)	Mandatory Exclusions (i.e. ineligible costs.)
All eligible and necessary costs of production. (Inc. e.g. REGOs, network costs, and costs associated with any compression necessary for production.)	All eligible costs of hydrogen transport and/or storage. All eligible costs of electricity battery storage. All eligible costs of onsite hydrogen refuelling/dispensing stations. (i.e. where hydrogen is sold directly from the production site.)	See list of ineligible costs above.

[14] Any such spend is at your own risk and only recoverable under the terms of a signed Low Carbon Hydrogen Agreement. It is subject to compliance with applicable subsidy control requirements (as set out above for all cost categories).

DESNZ will retain the right to reject any proposed exclusion – e.g. where it would involve the project taking on too much risk, and so start to diminish the long-term deliverability of the project from HMG's perspective.

DESNZ will not permit 'partial' or 'split' inclusions – e.g. 64% of the value of a given category included, 36% excluded. This is to streamline the operation and enforcement of the LCHA by clearly delineating which categories of cost are included in the Strike Price.

Projects will be able to declare in the RFI Project Datasheet which of the cost areas listed in the table above they would like to be treated as Strike Price Exclusions.

This publication is available from: https://www.gov.uk/government/publications/hydrogen-allocation-round-2-har2-due-diligence-and-cost-assurance

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