Subsidy Advice Unit Report on the Low-Carbon Dispatchable Contract for Difference to EP Lynemouth Power Limited

Referred by the Department for Energy Security and Net Zero

29 May 2026

Subsidy Advice Unit

Part of the Competition and Markets Authority

CONTENTS

1. The Referral

1.1 On 10 April 2026, the Department for Energy Security and Net Zero (DESNZ) requested a report from the Subsidy Advice Unit (the SAU)[1] in relation to its proposed Low-Carbon Dispatchable Contract for Difference to EP Lynemouth Power Limited (Lynemouth Power) (the Subsidy) under section 52 of the Subsidy Control Act 2022 (the Act).[2]

1.2 This report evaluates DESNZ's assessment of compliance (the Assessment) of the Subsidy with the requirements of Chapters 1 and 2 of Part 2 of the Act.[3] It is based on the information and evidence included in the Assessment.

1.3 This report is provided as non-binding advice to DESNZ. It does not consider whether the Subsidy should be given, or directly assess whether it complies with the subsidy control requirements.

Summary

1.4 The Assessment uses the four-step structure described in the Statutory Guidance for the United Kingdom Subsidy Control Regime (the Statutory Guidance) and as reflected in the SAU's Guidance on the operation of the subsidy control functions of the Subsidy Advice Unit (the SAU Guidance).

1.5 In our view, DESNZ has considered in detail some aspects of the compliance of the Subsidy with the subsidy control and energy and environment principles. In particular, the Assessment:

(a) clearly describes and evidences the specific policy objective of the Subsidy and clearly describes the market failures that the Subsidy seeks to remedy (Principle A); and

(b) clearly explains and evidences how the Subsidy complies with Principles B, C, D, E and H of the energy and environment principles.

1.6 However, we have identified the following areas for improvement. The Assessment should:

[1] The SAU is part of the Competition and Markets Authority.
[2] Referral of the proposed subsidy to EP Lynemouth Power Limited by the Department for Energy Security and Net Zero - GOV.UK.
[3] Chapter 1 of Part 2 of the Act requires a public authority to consider the subsidy control principles and energy and environment principles before deciding to give a subsidy. The public authority must not award the subsidy unless it is of the view that it is consistent with those principles. Chapter 2 of Part 2 of the Act prohibits the giving of certain kinds of subsidies and, in relation to certain other categories of subsidy creates a number of requirements with which public authorities must comply.

(a) consider other sources of public finance (such as the National Wealth Fund or Great British Energy) as potential providers of equity or debt and explain why these were deemed inappropriate (Principle E);

(b) make better use of evidence in relation to Lynemouth Power's financial position and incentives, to support its conclusions as to why decommissioning the plant is the most likely outcome absent the Subsidy (Principle C);

(c) make better use of evidence in relation to how the Subsidy changes Lynemouth Power's incentives to continue operating (Principle D);

(d) consider in further detail the competitive impact of the Subsidy on other biomass generators (Principle F);

(e) explicitly weigh the benefits and negative effects of the Subsidy against each other in the balancing exercise (Principle G); and

(f) set out how the Subsidy is compliant with the environmental limb of Principle A of the energy and environment principles.

1.7 We discuss these areas below, along with other issues, for consideration by DESNZ in finalising its assessment.

The referred subsidy

1.8 The Subsidy supports the generation of electricity produced by Lynemouth power station from biomass, an organic matter used as fuel for the generation of electricity. Lynemouth power station is located in Northumberland in England. DESNZ decided to progress a short-term support mechanism for large scale biomass generators following a consultation held in January 2024.[4]

1.9 The Subsidy consists of a variable top-up payment in the form of a Contracts for Difference (CfD) to Lynemouth Power, the owner of Lynemouth power station. The total value of the Subsidy is estimated to be around £260 million (2024 prices) and will run for four years between 1 April 2027 and 31 March 2031. Until now, Lynemouth Power has relied on existing government support under the Renewables Obligation[5] and the CfD for renewable energy schemes to generate electricity competitively. However, existing support arrangements are due to end on 31 March 2027.

[4] Transitional support mechanism for large-scale biomass generators: consultation - government response.
[5] For more information on the Renewables Obligation, see the Renewables Obligations (RO) Guidance.

1.10 The main features of the CfD are:

(a) The variable payment is calculated as the difference between an agreed strike price and an estimate of the market price for electricity, called the baseload market reference price (BMRP). The BMRP represents an average market price of electricity for the season, based on forward contracts traded before the season starts. The BMRP is calculated on a seasonal (winter and summer) basis and is fixed ahead of the season.

(b) If the BMRP falls below the agreed strike price, then the generator receives a top-up payment from a government owned counterparty, the Low Carbon Contracts Company Ltd (LCCC) for the difference. The CfD contains an excess returns mechanism, requiring a share of returns to be paid back to LCCC if total returns achieved by Lynemouth Power across the four-year term exceed certain thresholds.[6]

(c) The CfD includes a minimum and a maximum volume in megawatts (MW) that is eligible for the top-up payment. The Subsidy is capped to a maximum load factor of 27%,[7] including seasonal caps and floors. The Assessment states that subsidy payments will not be made for any generation that exceeds the cap.

1.11 DESNZ explained that the Subsidy is a Subsidy of Particular Interest because it exceeds £25 million in value.

[6] The lower threshold will be £18 million per annum and requires a 30% share of profits above that level to be returned to LCCC. The upper threshold will be £26 million per annum and require a 60% share of profits above that level to be returned.
[7] Load factor refers to the percentage of generation from a technology relative to its maximum generating capacity in a given period.

2. The SAU's Evaluation

2.1 This section sets out our evaluation of the Assessment, following the four-step structure used by DESNZ.

Step 1: Identifying the policy objective, ensuring it addresses a market failure or equity concern, and determining whether a subsidy is the right tool to use

2.2 Under Step 1, public authorities should consider compliance of a subsidy with:

(a) Principle A: Subsidies should pursue a specific policy objective in order to remedy an identified market failure or address an equity rationale (such as local or regional disadvantage, social difficulties or distributional concerns); and

(b) Principle E: Subsidies should be an appropriate policy instrument for achieving their specific policy objective and that objective cannot be achieved through other, less distortive, means.[8]

Policy objectives

2.3 The Assessment states that the policy objective of the Subsidy is to maintain Great Britain's security of supply between 2027 and 2031 by providing low-carbon, dispatchable electricity to the grid, in turn supporting the clean power 2030 mission. It explains that the Subsidy aims to facilitate the generation of large-scale sustainable biomass power through Lynemouth Power.

2.4 The Assessment explains that the Subsidy is intended to provide electricity to the grid at times when the market does not sufficiently deliver capacity from a source with lower carbon emissions and a lower overall cost to consumers than its most likely alternative, unabated gas. It states that, when sourced sustainably, biomass can be used as a low carbon energy source to displace more carbon-intensive energy sources, such as natural gas.

2.5 The Assessment also mentions that Lynemouth Power may transition to power Bioenergy with Carbon Capture and Storage (power BECCS)[9] in the future. It states that, while the Subsidy does not guarantee this outcome, by keeping Lynemouth Power operational, DESNZ considers that it is retaining the potential for another decarbonisation pathway.

[8] See Statutory Guidance, paragraphs 3.33–3.59 and the SAU Guidance, paragraphs 3.6–3.10 for further detail.
[9] Power BECCS is the process of using sustainable biomass feedstocks to fuel a combustion process to generate electricity in combination with carbon capture and permanent storage. In this process, carbon sequestered in plant material is captured after combustion and stored underground.

2.6 In our view, the Assessment clearly describes and evidences the specific policy objective of the Subsidy.

Market failure

2.7 Market failures arise where market forces alone do not produce an efficient outcome. When this arises, businesses may make investments that are financially rational for themselves, but not socially desirable.[10]

2.8 The Assessment describes the following market failures:

(a) **Carbon emission externalities of fossil fuel**: The Assessment discusses two aspects of these externalities:

(i) *The loss of a low-carbon, firm and flexible energy source*. The Assessment states that the greenhouse gas emissions from the use of unabated fossil fuels for electricity generation impose global climate costs that are not fully reflected in market prices. It states that this leads to higher-emitting generation being favoured over socially optimal outcomes. It explains that, in the absence of further support, Lynemouth Power would be unlikely to continue operating and that it would likely be replaced by increased reliance on other dispatchable technologies, most notably unabated gas.

(ii) *The potential loss of negative emissions through conversion to power BECCS*. The Assessment states the value to climate targets of a plant remaining online until power BECCS can be deployed does not in itself provide the financial incentive for operators to remain in the market. DESNZ therefore expects those operators to retire, resulting in the loss of the option to convert to power BECCS and deliver substantial negative emissions.

(b) **Under-provision of electricity security**: The Assessment explains that electricity security is a quasi-public good, as security of supply is non-rivalrous and largely non-excludable.[11] This is because consumers cannot choose their desired level of reliability, nor can the system operator deliver it selectively. It states that there is no way for consumers to express their willingness to pay for reliability, and markets do not provide an efficient price signal to indicate that sufficient firm and flexible capacity will be available to consumers at times of system stress. There is therefore a market under-investment in reliability, particularly with regard to low-carbon dispatchable technologies.

[10] Statutory Guidance, paragraphs 3.36–3.51.
[11] Non-excludability refers to the fact that a person cannot be prevented from consuming a good.

2.9 The Assessment explains how the Subsidy will remedy these market failures. It states that, by allowing Lynemouth Power to continue generating electricity from biomass, it is securing dispatchable capacity to the grid from a source with a lower emissions intensity than fossil fuels, which are the most likely alternative when intermittent renewables do not provide sufficient capacity. The Assessment explains that biomass is regarded as low carbon fuel because the carbon emissions released during biomass combustion is offset by continuous new growth in sustainably managed forests. It cites evidence from the UK Climate Change Committee and Intergovernmental Panel on Climate Change to support this view.

2.10 The Assessment further details that Lynemouth Power has plans to potentially convert to power BECCS in the long term. It states that the Subsidy is intended to keep Lynemouth Power operational where there is otherwise a lack of financial incentive to do so, thereby retaining this optionality to convert to power BECCS and deliver substantial negative emissions.

2.11 In our view, the Assessment clearly describes the market failures that the Subsidy seeks to remedy. However, it could evidence its conclusions in more detail. The Assessment could also better explain how carbon emission externalities arising from the loss of negative carbon emissions through conversion to power BECCS fits with the identified policy objective.

Appropriateness

2.12 Public authorities must determine whether a subsidy is the most appropriate instrument for achieving the policy objective. As part of this, they should consider other ways of addressing the market failure or equity issue.[12]

2.13 The Assessment explains that DESNZ has considered the following means to achieve the policy objective and details why they were discounted: regulation, HM Treasury loan, HM Treasury share acquisition, nationalisation and procurement of alternative generation through the Capacity Market scheme.[13]

2.14 In our view, the Assessment demonstrates that DESNZ has considered other ways of achieving its policy objective. However, the Assessment should consider other sources of public finance (such as the National Wealth Fund or Great British Energy) as potential providers of equity or debt and explain why these were deemed inappropriate.

[12] Statutory Guidance, paragraphs 3.57–3.59.
[13] The Capacity Market is a Subsidy Scheme that provides payment to electricity providers to guarantee sufficient generating capacity will be available in the future, ensuring that the grid can meet peak demand even if that capacity is not always used. See Capacity Market - GOV.UK for further information.

Step 2: Ensuring that the subsidy is designed to create the right incentives for the beneficiary and bring about a change

2.15 Under Step 2, public authorities should consider compliance of a subsidy with:

(a) Principle C: Subsidies should be designed to bring about a change of economic behaviour of the beneficiary. That change should be something that would not happen without the subsidy and be conducive to achieving its specific policy objective; and

(b) Principle D: Subsidies should not normally compensate for the costs the beneficiary would have funded in the absence of any subsidy.[14]

Counterfactual

2.16 In assessing the counterfactual, public authorities should consider what would likely happen in the future – over both the long and short term – if no subsidy were awarded (the 'do nothing' scenario).[15]

2.17 The Assessment considers multiple counterfactual scenarios where the plant could be mothballed (shut down and preserved), repurposed, or decommissioned (closed permanently). It states that DESNZ considers that the most likely counterfactual would be that the plant is decommissioned. The Assessment states that this conclusion was drawn based on an assessment of Lynemouth Power's historical trading performance and expected operating costs relative to forecast wholesale electricity prices between 2027-2031. It describes how electricity generation from biomass involves high and largely unavoidable costs driven by the cost of biomass fuel, processing, transport and handling. The Assessment explains that forecast wholesale electricity prices will not be sufficient on a sustained basis to cover these costs whilst also maintaining other fixed costs.

2.18 The Assessment then outlines that unabated gas would replace Lynemouth Power's generating capacity absent the Subsidy. It relies on a dynamic dispatch model to support this conclusion.[16] The Assessment outlines that this scenario would undermine the policy objective as, in the absence of Lynemouth Power, DESNZ does not anticipate that the market will address the social cost of carbon emissions across industries, therefore impacting carbon targets.

2.19 The Assessment also explains that the closure of Lynemouth Power could eliminate the option of future conversion of the biomass plants to power BECCS,

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[14] See Statutory Guidance, paragraphs 3.60–3.74 and the SAU Guidance, paragraphs 3.11–3.13 for further detail.
[15] Statutory Guidance, paragraphs 3.63–3.65.
[16] The dynamic dispatch model is a power system model. This predicts when specific plants will generate, based on their relative costs and assumed future demand, and estimates the implied wholesale price. It also adds up the cost of policy support. These outputs are then added together to produce an estimate of the cost to consumers of the modelled scenario.

thus limiting the range of technologies available to meet Carbon Budget 6.[17] It outlines that even short-term plant closures would result in the loss of biomass supply chain networks, making it challenging for plants to resume operations in time to support carbon targets.

2.20 In our view, the Assessment describes and evidences what would be likely to happen if the Subsidy was not awarded. However, the Assessment should discuss in further detail how the evidence on Lynemouth Power's financial position and incentives supports its conclusions that decommissioning the plant is the most likely outcome absent the Subsidy.

Changes in economic behaviour of the beneficiary and additionality

2.21 Subsidies must bring about something that would not have occurred without the subsidy.[18] They should not be used to finance a project or activity that the beneficiary would have undertaken in a similar form, manner, and timeframe without the subsidy ('additionality').[19]

2.22 The Assessment explains that the Subsidy incentivises Lynemouth Power to generate electricity under conditions in which it would otherwise not produce. It explains that, unlike intermittent renewables,[20] Lynemouth Power incurs costs for its fuel supply that mean that it is unlikely that it would make an operating profit unsubsidised and therefore will not be able to cover variable costs (namely related to fuel) and fixed costs.

2.23 The Assessment notes [✂].[21]

2.24 The Assessment explains that the Subsidy mechanism also incentivises Lynemouth Power to produce electricity at times when the network need is high (as reflected in high prices), namely during periods of high demand and low output from intermittent renewables. It outlines that this is because Lynemouth Power receives both the achieved power price at which the electricity is sold, and the top up payment under the CfD (see paragraph 2.28(b)). The Assessment explains that this mechanism combined with a generation cap, will maintain reliable energy capacity while minimising subsidy funding.

2.25 The Assessment also describes how the Subsidy design features support regular electricity generation from Lynemouth Power through minimum load factor

[17] Sixth Carbon Budget - Climate Change Committee covering the years 2033-2037.
[18] Statutory Guidance, paragraph 3.67.
[19] Statutory Guidance, paragraphs 3.66–3.70.
[20] For example, wind or solar.
[21] The SAU has excluded from this published version of the report information which it considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂].

requirements, ensuring that Lynemouth Power's output is available at times of system stress (see paragraph 2.8(b)).

2.26 In our view, the Assessment explains how the Subsidy would change the beneficiary's economic behaviour and that the Subsidy brings about changes that would not have occurred absent the subsidy. However, the Assessment should evidence in more detail how the Subsidy changes Lynemouth Power's incentives to continue operating.[22]

Step 3: Considering the distortive impacts that the subsidy may have and keeping them as low as possible

2.27 Under Step 3, public authorities should consider compliance of a subsidy with:

(a) Principle B: Subsidies should be proportionate to their specific policy objective and limited to what is necessary to achieve it; and

(b) Principle F: Subsidies should be designed to achieve their specific policy objective while minimising any negative effects on competition or investment within the United Kingdom.[23]

Proportionality

2.28 The Assessment states that the Subsidy is expected to total approximately £260 million. As explained in paragraph 1.10, the value of payments is determined by the strike price and BMRP.

(a) The strike price is set at £110/MWh (2012 prices) and will remain constant in real terms for the four-year period.[24] The Assessment states that it was determined as the price that would make the expected payments to Lynemouth Power approximately equal to the cost of procuring the same supply though future Capacity Market auctions rather than an offer grounded in costs, revenue and return assumptions.

(b) The BMRP is calculated as a volume-weighted average of forward-season electricity prices.[25] It is calculated seasonally to allow the top-up payment to reflect recent market expectations of the price of electricity for the upcoming season.

2.29 The Assessment identifies the following aspects of the Subsidy that are also relevant to proportionality:

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[22] To do this, it could draw on the further analysis recommended in paragraph 2.20.
[23] See Statutory Guidance paragraphs 3.75–3.112 and the SAU Guidance, paragraphs 3.14–3.18 for further detail.
[24] The nominal value of the strike price will increase annually with the annual rate of CPI inflation.
[25] The winter season is from October to March, and the summer season is April to September.

(a) Only power generated below defined seasonal caps is eligible for CfD payments.[26] The Assessment states that the cap represents a proportionate measure to balance the objective for reliable capacity with addressing the identified market failure related to carbon emissions (see paragraph 2.8(a)). The Assessment also explains that these caps were set following discussions with the National Energy System Operator.

(b) The Subsidy contains an excess returns mechanism (see paragraph 1.10(b)). The Assessment states that this mitigates the risk of over-compensating Lynemouth Power and that DESNZ has taken into account the material additional risks that Lynemouth Power would bear under the Subsidy in determining these thresholds. It compares these thresholds to that of the Hinkley Point C CfD and notes that these thresholds are lower.

(c) The Subsidy includes several performance criteria within the contract conditions with penalties in place in case of non-compliance. The conditions the Assessment outlines include verification of installed capacity, obligation to maintain capacity, and minimum generation levels. It states that the contract also contains enhanced sustainability requirements relating to the level of supply chain emissions and the sustainable sourcing of biomass. The Assessment explains that the LCCC will audit payments to ensure that the terms of the contract are complied with and that failures on the part of Lynemouth Power to comply the performance criteria will allow the LCCC to terminate the contract or suspend payments in the case of breaching the sustainability requirements.

(d) The Assessment explains that the risk of over-compensation is further mitigated by the fact [✂].

2.30 The Assessment also states that DESNZ considered a range of alternative subsidy designs (including a direct grant and a payment for maintaining asset availability) to identify the most proportionate approach and outlines why they were discounted.

2.31 In our view, the Assessment demonstrates and evidences how aspects of the Subsidy's design contribute to demonstrating that the Subsidy is proportionate and limited to the minimum necessary to achieve its specific policy objective, in line with the Statutory Guidance.

2.32 The Assessment clearly explains how supporting Lynemouth Power through this Subsidy is comparable value for money to procuring the equivalent capacity through the Capacity Market. However, the Assessment could articulate more

[26] There are different caps for winter and summer seasons to reflect the fact that potentially cheaper intermittent renewables, such as solar power, is more readily available in the summer.

clearly why the Subsidy is set at the minimum level necessary to achieve the policy objective, as opposed to demonstrating that this Subsidy represents better or equivalent value for money than alternative policy options such as Capacity Market procurement.

2.33 The Assessment could also provide more details on the design of the excess returns mechanism. For example, it could explain in more detail its reasoning for the chosen proportions to be returned by Lynemouth Power and the thresholds above which profits are returned to the LCCC. The Assessment could do this by discussing in more detail how the risks imposed on Lynemouth Power by the Subsidy factored into the setting of the thresholds and proportions or by comparing them to an excess returns mechanism used in the Subsidy for a generator of comparable scale or technology.

Design of subsidy to minimise negative effects on competition or investment

2.34 The Assessment discusses several aspects of subsidy design mentioned in the Statutory Guidance in relation to minimising distortive effects on competition or investment in the UK, including the fact that the Subsidy is time-limited to between April 2027 and March 2031.

2.35 The Subsidy includes a cap on generation volumes above which power is not eligible for CfD payments.[27] The Assessment states that this reduces the risk that Lynemouth Power would be incentivised to operate in a way that risks distorting the contribution of potentially cheaper intermittent renewables and is instead incentivised to generate when electricity is most needed (at peak demand or when renewable generation is limited).

2.36 In relation to the breadth of beneficiaries, only generators who met a set of eligibility criteria are eligible to receive funding. One of these criteria is that the generator must have a capacity of at least 100 MW.[28] The Assessment states that only Lynemouth Power and one other generator meet these criteria. The Assessment also states that agreeing many contracts with smaller generators is less appropriate and less efficient than negotiating with a large-scale generator.

2.37 In our view, the Assessment broadly demonstrates and evidences how design features of the Subsidy contribute to minimising any negative effects of the Scheme on competition or investment within the United Kingdom. However, the Assessment should clearly articulate how each of the eligibility criteria represent the least distortive approach to achieving the policy objective. For example, the

[27] This cap is seasonal, with a value of 46% in winter (October-March) and 8% in summer (April-September).
[28] The Assessment states that this aligns with the eligibility criteria for the potential power BECCS business model.

Assessment could discuss the responses to the public consultation regarding the competitive impact of the eligibility criteria.

Assessment of effects on competition or investment

2.38 The Assessment acknowledges that the Subsidy will lead to displacement of unabated gas electricity generation. However, it explains that this is in line with the policy objective of correcting the market failure associated with carbon emissions and so represents a deliberate policy decision rather than a market distortion.

2.39 The Assessment also recognises that there will be competitive effects on other sources of power. These include the following:

(a) Other large-scale biomass generators who Lynemouth Power competes with and face similar challenges in selling their generated power at competitive market rates. The Assessment outlines that any support provided to Lynemouth Power could risk creating an uneven playing field with similar generators operating without revenue guarantees. It notes that DESNZ welcomed submissions from other large-scale biomass generators who believed they met the criteria to qualify for a CfD and the Assessment states that this approach should partially address competition concerns.

(b) Small-scale biomass generators who do not meet the capacity threshold of 100MW. The Assessment states that there are at least 104 biomass generators who fit this description.

(c) Other generation technologies (excluding unabated gas). The Assessment states that the Subsidy does not dissuade investor confidence in these technologies. It provides evidence that alternative technologies such as nuclear or battery storage can be scaled up to meet the forecasted capacity challenge faced in the late 2020s and so are unlikely to be distorted against. However, the Assessment also states that the Subsidy design ensures that Lynemouth Power only generates when needed rather than as a baseload, and the merit order system prioritises cheaper, forms of power (which are potentially also cleaner), which should mitigate distortive concerns.

2.40 In our view, the Assessment broadly considers and evidences the effect of the Subsidy on competition or investment, in line with Annex 3 of the Statutory Guidance.

2.41 However, the Assessment should discuss in further detail the competitive impact of the Subsidy on other biomass generators:

(a) it should discuss any difference in the support that other large-scale generators receive and how this difference could impact competition between them; and

(b) it should discuss in more detail the impact on smaller generators of this Subsidy increasing the competitiveness of Lynemouth Power's bids into the wholesale electricity market. In particular, the Assessment should discuss whether this Subsidy will distort the wholesale market in such a way that smaller generators may be forced to exit the market.

2.42 The Assessment could also discuss the potential for distortive effects on related markets, in particular, the market for wood pellets (stating clearly whether impacts are expected to be minimal).

Step 4: Carrying out the balancing exercise

2.43 Under step 4 (Principle G), public authorities should establish that the benefits of the subsidy (in relation to the specific policy objective) outweigh its negative effects, in particular negative effects on competition or investment within the United Kingdom and on international trade or investment.[29]

2.44 The Assessment discusses the following benefits of the Subsidy:

(a) a reduction in greenhouse gas emissions compared to the counterfactual of generating power by unabated gas, as the Subsidy incentivises Lynemouth Power to generate only at times of system need, with emissions savings estimated at around £40 million per annum;

(b) delivering security of supply by supporting Lynemouth Power to remain operational and provide dispatchable output during periods of system stress, reducing reliance on future capacity procurement; and

(c) retaining the option for future power BECCS conversion.

2.45 The Assessment explains that the consumer cost impacts of the Subsidy are not expected to be materially higher, and may be broadly comparable to or lower than, the counterfactual of replacing equivalent firm capacity through the Capacity Market.

2.46 The Assessment identifies potential negative effects of the Subsidy, including:

(a) an increase in the underlying production costs of electricity. The Assessment sets out that the economic cost of generating electricity from Lynemouth Power under the agreement is estimated to be higher than for gas, reflecting higher biomass production costs. However, the Assessment explains that this relates to production costs rather than consumer prices, which are assessed as broadly comparable to or lower than the counterfactual;

[29] See Statutory Guidance, paragraphs 3.113–3.121 and the SAU Guidance, paragraphs 3.19–3.21 for further detail.

(b) potential negative impact on competition, international trade and investment as the Subsidy will enable Lynemouth Power to continue operating where it would otherwise not be incentivised to continue operating, potentially disadvantaging unsubsidised dispatchable generators, particularly unabated gas. The Assessment explains that these impacts will be limited and temporary; and

(c) environmental impact of biomass power generation on local air quality.

2.47 The Assessment concludes that the positive effects of the Subsidy outweigh its negative effects.

2.48 In our view, the Assessment sets out the expected benefits of the Subsidy as well as potential negative effects. However, the Assessment should provide more detailed analysis that explicitly weighs the benefits and negative effects against each other. It should:

(a) draw on any cost-benefit analyses undertaken and relevant quantitative and/or qualitative evidence; and

(b) clearly differentiate between the direct benefits of the Subsidy and the longer-term benefits it may enable (for example, those relating to power BECCS).

Energy and Environment Principles

2.49 This section sets out our evaluation of the Assessment against the energy and environment principles.[30]

2.50 DESNZ has conducted an assessment of the Subsidy against Principles A, B, C, D, E and H. We have not identified any other principle that should have been addressed as part of the Assessment.

Principle A: Aim of subsidies in relation to energy and environment

2.51 Subsidies in relation to energy or the environment should be aimed at (1) delivering a secure, affordable and sustainable energy system and a well-functioning and competitive energy market, or (2) increasing the level of environmental protection compared to the level that would be achieved in the absence of the subsidy. If a subsidy is in relation to both energy and environment, it should meet both limbs.[31]

[30] See Schedule 2 to the Act, and Statutory Guidance, Chapter 4.
[31] Statutory Guidance, paragraphs 4.19–4.28.

2.52 The Assessment assesses the Subsidy against the first limb of Principle A, relating to energy subsidies. It explains that the Subsidy will be aimed at delivering:

(a) a secure energy system because absent the Subsidy, Lynemouth Power will cease operation from March 2027 (the point at which existing subsidies to Lynemouth Power will end). The Assessment outlines that the loss of Lynemouth Power would reduce available firm capacity, which will most likely be replaced by higher-carbon unabated gas capacity increasing both security-of-supply risks and carbon externalities and that alternative options are unlikely to scale up to the required level in the timeframe. The Assessment also explains that Lynemouth Power will be required to maintain its assets during the lifetime of the Subsidy avoiding further reductions in the UK's near-term capacity margins and strengthening energy resilience;

(b) an affordable energy system as the amount payable under the Subsidy will be lower compared to the existing support mechanism to Lynemouth Power. The Assessment also explains that by supporting Lynemouth Power to operate at a low load factor, this ensures that the beneficiary is more reactive to price signals and is incentivised to run mainly at times when power is most needed thereby providing price support at times of high power prices;

(c) a sustainable energy system as sustainable biomass generation is a renewable energy source that can provide low carbon electricity to support the government's decarbonisation objective. The Assessment also explains that through maintaining an existing plant the government retains the supplementary option of the plant being retrofitted to power BECCs in the future that by supporting Lynemouth Power to operate at a low load factor this ensures that the beneficiary is more reactive to price signals and is incentivised to run mainly at times when power is most needed thereby providing price support at times of high power prices; and

(d) a well-functioning and competitive energy market as the seasonal cap and floor mean that Lynemouth Power will play a limited role and will be required to dispatch electricity only at times when power is most needed.

2.53 The Assessment explains that DESNZ does not consider the second limb of Principle A, relating to environmental protection, as relevant to the Subsidy because the primary objective of the Subsidy is not to increase environmental protection levels.

2.54 In our view, the Assessment clearly explains and evidences how the Subsidy complies with the first limb of Principle A of the energy and environment principles. However, given that the policy objective of the Subsidy is to support the government's clean power 2030 mission and the Subsidy is aimed at addressing carbon emission externalities, we consider that the second limb is also likely to

apply to the Subsidy. The Assessment should therefore set out how the Subsidy is compliant with the environmental limb of the energy and environment principles.

Principle B: Beneficiary's liabilities as a polluter

2.55 Subsidies in relation to energy or the environment should not relieve the beneficiary from liabilities arising from its responsibilities as a polluter under the law of England and Wales, Scotland, or Northern Ireland.[32]

2.56 The Assessment explains that the Subsidy will not relieve Lynemouth Power from its duties and accompanying liabilities as a polluter as any breach of environmental standards and regulations will not be covered by the Subsidy and will be borne by Lynemouth Power. Further, the Assessment reports that the sustainability criteria have been strengthened, including that the proportion of woody biomass that must be sustainably sourced has increased from 70% to 100%.

2.57 In our view, the Assessment clearly explains and evidences how the Subsidy complies with Principle B of the energy and environment principles.

Principle C: Subsidies for electricity generation adequacy, renewable energy, or cogeneration

2.58 Subsidies or schemes for electricity generation adequacy, renewable energy, or cogeneration should not undermine the UK's ability to ensure that wholesale electricity and natural gas prices reflect actual supply and demand, and that the wholesale electricity and natural gas market rules will, in general terms, be transparent, encourage free price formation, and operate in an efficient and secure manner.[33] They should also not unnecessarily affect the efficient use of electricity interconnectors between the UK and the European Union. Finally, they should be determined by means of a transparent, non-discriminatory and effective competitive process, or, alternatively, an explanation should be provided for why a non-competitive process was used.[34]

2.59 The Assessment sets out that all the criteria under Principle C are met because the Subsidy:

(a) does not undermine the ability of the UK to meet its obligations under Article 304 of the Trade and Cooperation Agreement (TCA). The Assessment

[32] Statutory Guidance, paragraphs 4.29–4.34.
[33] Article 304 of the Trade and Cooperation Agreement between the United Kingdom of Great Britain and Northern Ireland, of the one part, and the European Union and the European Atomic Energy Community, of the other part (TCA).
[34] Statutory Guidance, paragraphs 4.36–4.44.

explains the Subsidy does not impose any form of price controls that limits the buying or selling of electricity on the wholesale market; and

(b) does not curtail the efficient use of electricity interconnections provided for under Article 311 of the TCA.

2.60 The Assessment explains that DESNZ was unable to follow a typical competitive auction process as only a limited number of generators came forward that met the relevant eligibility criteria, and so DESNZ had to follow a bilateral process to explore separate contracts with each generator. It explains the different measures taken to mitigate any risk of over-compensation to Lynemouth Power, as set out in Step 3 (see paragraph 2.29), including:

(a) designing the Subsidy to ensure Lynemouth Power only generates when the system requires it to do so;

(b) calculating the strike price and allowable profits based on historic and projected revenues from the two generators, cross-referenced against third party data for reliability and accuracy. The Assessment then sets out that the calculated strike price for Lynemouth Power was pinned to the comparable cost of securing alternative capacity through the Capacity Market which resulted in a strike price lower than Lynemouth Power's own assessment; and

(c) adding an Excess Returns Mechanism to act as a backstop that requires Lynemouth Power to pay back a proportion of profits above an agreed threshold.

2.61 [✂].

2.62 In our view, the Assessment clearly explains and evidences how the Subsidy complies with Principle C of the energy and environment principles.

Principle D: Subsidies for electricity generation adequacy

2.63 Subsidies for electricity generation adequacy may be limited to installations not exceeding specified CO_2 emission limits.[35]

2.64 The aim of this principle is to ensure that any such measures (that limit installation CO_2 emissions) are clearly set out in the Subsidy or otherwise signposted to the beneficiary.[36] There is no obligation on a public authority to include a limitation on

[35] Statutory Guidance, paragraphs 4.45.
[36] Statutory Guidance, paragraph 4.46.

CO_2 emissions in the design of a subsidy related to electricity generation adequacy.[37]

2.65 The Assessment explains that direct carbon emissions from Lynemouth Power are regulated at the installation-level through the UK emissions trading scheme, under which biogenic-CO_2 is rated zero. The Assessment explains that the UK emissions trading scheme includes monitoring and reporting requirements and would remain applicable under the Subsidy.

2.66 The Assessment also sets out that CO_2 emissions associated with the international biomass supply chain are capped by the Subsidy and further sustainability criteria within the terms of the Subsidy define strict requirements for biomass to be considered sustainably sourced as a pre-condition to the associated CO_2 emissions being deemed zero at the installation level.

2.67 In our view, the Assessment clearly explains how the Subsidy complies with Principle D of the energy and environment principles.

Principle E: Subsidies for renewable energy or cogeneration

2.68 Subsidies for renewable energy or cogeneration should not affect beneficiaries' obligations or opportunities to participate in electricity markets.[38]

2.69 The Assessment states that the Subsidy does not relieve Lynemouth Power of its existing obligations or restrict its ability to participate in the electricity markets but instead enables Lynemouth Power to continue to participate in the wholesale electricity markets as well as other secondary market arrangements such as the ancillary services markets**.**

2.70 In our view, the Assessment clearly explains and evidences how the Subsidy complies with Principle E of the energy and environment principles.

Principle H: Subsidies for the decarbonisation of emissions linked to industrial activities

2.71 Subsidies for the decarbonisation of emissions linked to industrial activities should achieve an overall reduction in greenhouse gas emissions, and reduce the emissions directly resulting from the industrial activities concerned.[39]

[37] Statutory Guidance, paragraph 4.47.
[38] Statutory Guidance, paragraphs 4.48–4.51.
[39] Statutory Guidance, paragraphs 4.60–4.68.

2.72 DESNZ states that the Subsidy is consistent with Principle H by achieving an overall reduction in greenhouse gas emissions by avoiding the use of unabated gas. The Assessment explains that:

(a) fossil fuel electricity (including gas) produces significant greenhouse gas emissions and the government aspires to replace those emissions with renewables and low-carbon alternatives (such as biomass); and

(b) accordingly, Lynemouth Power will contribute reliable power to the system while at the same time facilitating the decarbonisation of the power system as a result of its low carbon value.

2.73 In our view, the Assessment clearly explains and evidences how the Subsidy complies with Principle H of the energy and environment principles.

Other Requirements of the Act

2.74 DESNZ confirmed that no other requirements or prohibitions set out in Chapter 2 of Part 2 of the Act apply to the Subsidy.

29 May 2026