

## EXPLANATORY MEMORANDUM TO

### THE CARBON DIOXIDE TRANSPORT AND STORAGE REVENUE SUPPORT (DIRECTIONS AND COUNTERPARTY) REGULATIONS 2024

2024 No. [XXXX]

#### 1. Introduction

- 1.1 This explanatory memorandum has been prepared by The Department for Energy Security and Net Zero and is laid before Parliament by Command of His Majesty.

#### 2. Declaration

- 2.1 Lord Callanan, Parliamentary Under Secretary of State (Minister for Energy Efficiency and Green Finance), at the Department for Energy Security and Net Zero confirms that this Explanatory Memorandum meets the required standard.
- 2.2 Matthew Taylor, Deputy Director for Carbon Dioxide Transport and Storage Policy, at the Department of Energy Security and Net Zero confirms that this Explanatory Memorandum meets the required standard.

#### 3. Contact

- 3.1 Amanda Charles at the Department for Energy Security and Net Zero ([amanda.charles@energysecurity.gov.uk](mailto:amanda.charles@energysecurity.gov.uk)) can be contacted with any queries regarding the instrument.

### **Part One: Explanation, and context, of the Instrument**

#### 4. Overview of the Instrument

##### *What does the legislation do?*

- 4.1 These Regulations are made using the powers at section 57 of the Energy Act 2023 (“the Act”) that enable the Secretary of State to make provisions, by way of regulations, about revenue support contracts in relation to carbon dioxide transport and storage.
- 4.2 These Regulations do three things: they set out the manner by which the Secretary of State may direct a carbon dioxide transport and storage counterparty to offer to contract with an eligible transport and storage company; they establish requirements that certain information must be published by the counterparty in respect of contracts entered into, and they establish requirements on the counterparty to promptly notify the Secretary of State if it is, or considers it is likely to be, unable to perform its functions.

##### *Where does the legislation extend to, and apply?*

- 4.3 The extent of this instrument (that is, the jurisdiction(s) which the instrument forms part of the law of) is England and Wales, Scotland and Northern Ireland.
- 4.4 The territorial application of this instrument (that is, where the instrument produces a practical effect) is the United Kingdom. The activities of a carbon dioxide transport and storage company may take place in the United Kingdom, above or below the

territorial sea adjacent to the United Kingdom, and waters in a Gas Importation and Storage Zone (within the meaning given by Section 1 of the Energy Act 2008).

## 5. Policy Context

### *What is being done and why?*

- 5.1 Carbon capture and storage is the process of capturing carbon dioxide and permanently storing it, deep underground where it cannot enter the atmosphere. Carbon dioxide transport and storage networks will act as the enabling infrastructure for carbon capture and storage from a range of sources, including power plants, industrial facilities, low carbon hydrogen production and potentially direct air capture.
- 5.2 Carbon capture, usage and storage (CCUS) has a key role in the UK's Net Zero Strategy by helping meet the UK's legally binding commitment to reduce greenhouse gas emissions to net zero by 2050. As CCUS will also provide flexible energy deployment across power, it has the potential to strengthen our energy security and reduce reliance on unabated fossil fuels, as well as enabling greenhouse gas removals.
- 5.3 Central to deploying CCUS is establishing the infrastructure to transport and permanently store the captured carbon dioxide, the development of which will require large upfront capital expenditure. To overcome market barriers to private investment into first-of-a-kind transport and storage infrastructure, the Government has developed the Carbon Dioxide Transport and Storage Regulatory Investment model ('TRI model'). This model includes economic regulation and licensing, where a transport and storage network operator, under the provisions of an economic licence regulated by Ofgem, is able to receive an "Allowed Revenue" which reflects its efficient costs and a reasonable return on investments.
- 5.4 To provide investors with the revenue certainty needed to establish and scale up deployment of the first transport and storage networks, the regulatory investment model provides for Exchequer-funded revenue support to be available to first-of-a-kind carbon dioxide transport and storage network companies in certain circumstances. This "revenue support agreement" mitigates the financial risks faced by first-of-a-kind network investors by limiting the impact of demand-side risk in the early years of operations (for example, delay to the initial users joining the networks). Without management of this demand risk through provision of revenue support, due to the first of a kind nature of the technologies, investors are unable to price the associated risk and take a decision to invest in carbon dioxide transport and storage.
- 5.5 Revenue support, if required, will be delivered through a private law contract between an eligible transport and storage company and a counterparty. To be eligible for a revenue support agreement a transport and storage company must have been granted (or have been notified that it will be granted), a transport and storage licence under section 7 of the Energy Act 2023. The first such licences are expected to be granted through the Government's current CCUS cluster sequencing process.
- 5.6 This instrument supports the implementation of the Carbon Dioxide Transport and Storage Regulatory Investment model and the Government's ambitions for the deployment of CCUS in the UK.
- 5.7 The Regulations set out the process governing how the Secretary of State can direct a transport and storage counterparty to offer to contract, the requirements for information that should be made publicly available, and provisions to help ensure the

Secretary of State is aware of any potential issues with a counterparty being able to fulfil its role.

*Direction by Secretary of State*

- 5.8 The Secretary of State may, in accordance with any provision made by revenue support regulations, direct a transport and storage counterparty to offer to contract with an eligible transport and storage network operator under section 60(1) of the Act. These Regulations set out various requirements in respect of a direction, including that it must be in writing, specify a date by when the counterparty must comply with the direction, and specify the period for which the counterparty must keep the offer to contract open for acceptance. A direction will prohibit the counterparty from modifying the terms of the contract offered without prior written consent of the Secretary of State. Additionally, these Regulations set out the circumstances in which a direction ceases to have effect and enable the Secretary of State to revoke a direction before it has been accepted by the producer.

*Information Publication*

- 5.9 Given the nascency of CCUS in the UK, and the support available to establish commercial scale projects, it is important that information about their deployment is made available publicly. These Regulations therefore include provisions mandating a counterparty to publish each revenue support contract entered into pursuant to a direction from the Secretary of State under section 60(1) of the Act, apart from redactions of confidential information and personal data. To ensure important information is readily accessible, the Regulations also place an obligation on the counterparty to establish and maintain a public register that captures key project information.

*Counterparty notification of defaults*

- 5.10 The role of a transport and storage counterparty is essential in the ongoing management of contracts and administration of payments to projects supported through the regulatory investment model. To help ensure the smooth operation of this model, the Regulations require a counterparty to provide prompt notification to the Secretary of State if it is, or considers that it is likely to be, unable to perform its functions as transport and storage counterparty.

***What was the previous policy, how is this different?***

- 5.11 The framework of economic regulation for the transport and storage of carbon dioxide established by the Energy Act 2023 followed consultation by the Government in 2019 on commercial models to pull through the investment needed to deploy CCUS at scale. The model has been designed in response to improved understanding from previous CCUS competitions, in order to mitigate the risks and technical and commercial challenges involved in deploying CCUS across the UK that were identified in evaluations of these prior competitions.

**6. Legislative and Legal Context**

***How has the law changed?***

- 6.1 The Energy Act 2023 makes provision for the implementation of the Carbon Dioxide Transport and Storage Regulatory Investment Model, which establishes an economic regulation and licensing framework for carbon dioxide transport and storage. The regulatory investment model also provides for revenue support to be available to

licensed operators, to overcome market barriers to private investment in the first-of-a-kind transport and storage infrastructure developments, supporting the UK's net zero and energy security ambitions.

- 6.2 Section 57(1) of the Act sets out the overarching power for the Secretary of State to make regulations in relation to revenue support contracts. There are a number of provisions in Chapter 1, Part 2 of the Act which set out the matters which regulations made under the overarching power in section 57(1) may cover.
- 6.3 Section 59(1) of the Act provides for the Secretary of State to designate a person to be a counterparty for a transport and storage revenue support contracts. Section 60(1) provides for the Secretary of State, in accordance with any provision made by revenue support regulations, to direct a transport and storage counterparty to offer to contract with an eligible person, with eligibility defined in section 60(2) of the Act.
- 6.4 Section 60(3) of the Act provides for revenue support regulations to make further provision about a direction under section 59(1), in particular about the circumstances in which a direction may or must be given and the terms it may or must specify. Section 83(1) enables revenue support regulations to make provision about the provision and publication of information and advice. This instrument sets out the process which the Secretary of State must follow when issuing a direction to offer to contract, and information about revenue support contracts a transport and storage counterparty must publish. Section 58(1)(b) of the Act states that a revenue support counterparty must act in accordance with any provision included in revenue support regulations, and section 58(2) provides that revenue support regulations may make provision specifying things that a revenue support counterparty may or must do. Given the critical role of a transport and storage counterparty to effectively deliver a revenue support contract, this instrument will require a counterparty to promptly notify the Secretary of State if it is, or considers it is likely to be, unable to perform its functions.

***Why was this approach taken to change the law?***

- 6.5 Developing carbon dioxide transport and storage infrastructure will require large upfront capital expenditure. Due to the first of a kind nature of the technologies there are demand-side risks, relating to uncertainty around the scale and timing of demand for the use of network and therefore the future revenues of a network operator, that are market barriers to the deployment of CCUS in the UK, where investors are unable to price the associated risk and take a decision to invest in carbon dioxide transport and storage. The policy supported by this instrument seeks to manage these demand risks through provision of revenue support to the first transport and storage network operators to provide revenue certainty to investors.

## **7. Consultation**

***Summary of consultation outcome and methodology***

- 7.1 The Department consulted on the policy contained in this instrument. The “CCUS transport and storage business models: revenue support regulations consultation” was published on 13 September 2023 and closed on 25 October 2023.
- 7.2 This consultation set out proposals relating to the process by which the Secretary of State may direct a counterparty to offer to contract with an eligible carbon dioxide transport and storage company and requirements that certain information about contracts and projects must be published.

- 7.3 The Department received four responses to the consultation which were broadly supportive of the consultation proposals. The Government response to the consultation was published on 29 February 2024.
- 7.4 Some respondents raised concerns that the proposals for publishing information could reveal sensitive information. This has been taken into account in the Regulations where the information required to be published in a contract register has been formulated to address this risk.
- 7.5 The consultation, and the Government response to the consultation, are published on gov.uk at: <https://www.gov.uk/government/consultations/ccus-transport-and-storage-revenue-support-agreement-counterparty>.
- 7.6 The Devolved Administrations were consulted on the draft Regulations, in accordance with the provisions of section 85 of the Energy Act 2023.
- 8. Applicable Guidance**
- 8.1 There is no guidance requirement.

## **Part Two: Impact and the Better Regulation Framework**

### **9. Impact Assessment**

- 9.1 A full Impact Assessment has not been prepared for this instrument because the Department found the preferred option of appointing the LCCC as the transport and storage counterparty to fall below the threshold for producing one.
- 9.2 Appointing a counterparty is primarily an administrative measure where the costs considered would fall as either upfront costs to establish the capacity to fulfil the function of the counterparty, or as ongoing costs for administering the duties. As the initial costs for the transport and storage counterparty will be recovered from exchequer funding, there is risk that a poor value for money option could expose taxpayers or businesses to higher costs. After reviewing the available options, the Department found those of the LCCC to be the lowest, with an expected annual cost of £350,000 and no additional set up costs. Other options considered, including the counterfactual where counterparty duties would fall to the Government, had higher set up costs with ongoing costs estimated at being either the same or higher. As £350,000 falls below the threshold for conducting an impact assessment, and there were no other significant impacts identified for either businesses or taxpayers, a full impact assessment has not been prepared.

#### ***Impact on businesses, charities and voluntary bodies***

- 9.3 There is no, or no significant, impact on business, charities or voluntary bodies because the costs involved in appointing a counterparty will be recovered from a mixture of consumer levy and exchequer funding. Furthermore, the preferred option of appointing the LCCC as the RSA counterparty offers the best value for money, minimizing potential impacts.
- 9.4 There is no, or no significant, impact on small or micro businesses. Appointing the LCCC as the counterparty minimises any potential impacts. Additionally, any costs that are passed through will be shared proportionally to all users of the transport and storage network.
- 9.5 The impact on the public sector is limited. Appointing the LCCC as the counterparty avoids set up costs and minimises ongoing impacts, meaning costs fall below the

threshold for an Impact Assessment. In the future as we see increased interest in CCUS projects by the private sector, Users who are privately funded will also contribute to the counterparty costs through Network fees, further reducing impacts.

## **10. Monitoring and review**

### *What is the approach to monitoring and reviewing this legislation?*

10.1 The approach to monitoring this legislation will be through the ongoing development of the carbon dioxide transport and storage business model.

10.2 The instrument does not include a statutory review clause, and, in line with the requirements of the Small Business, Enterprise and Employment Act 2015 Lord Callanan has made the following statement:

“In my view the provisions of The Carbon Capture Revenue Support (Directions, Eligibility and Counterparty) Regulations 2023 do not require a review clause as they are exempt under section 28(3)(c) of the Small Business, Enterprise and Employment Act 2015.”

## **Part Three: Statements and Matters of Particular Interest to Parliament**

### **11. Matters of special interest to Parliament**

- 11.1 The Regulations will commence on the day after the day on which they are made. This will enable the first contracts to be awarded as soon as reasonably possible to support government ambitions for the deployment of CCUS in the UK. Those affected by the Regulations, namely carbon dioxide transport and storage companies and the anticipated counterparty, the Low Carbon Contracts Company (LCCC), have been aware of the policy for several months.

### **12. European Convention on Human Rights**

- 12.1 Lord Callanan, Parliamentary Under Secretary of State (Minister for Energy Efficiency and Green Finance), at the Department for Energy Security and Net Zero has made the following statement regarding Human Rights:

“In my view the provisions of The Carbon Dioxide Transport and Storage Revenue Support (Directions and Counterparty) Regulations 2024 are compatible with the Convention rights.”

### **13. The Relevant European Union Acts**

- 13.1 This instrument is not made under the European Union (Withdrawal) Act 2018, the European Union (Future Relationship) Act 2020 or the Retained EU Law (Revocation and Reform) Act 2023 (“relevant European Union Acts”).