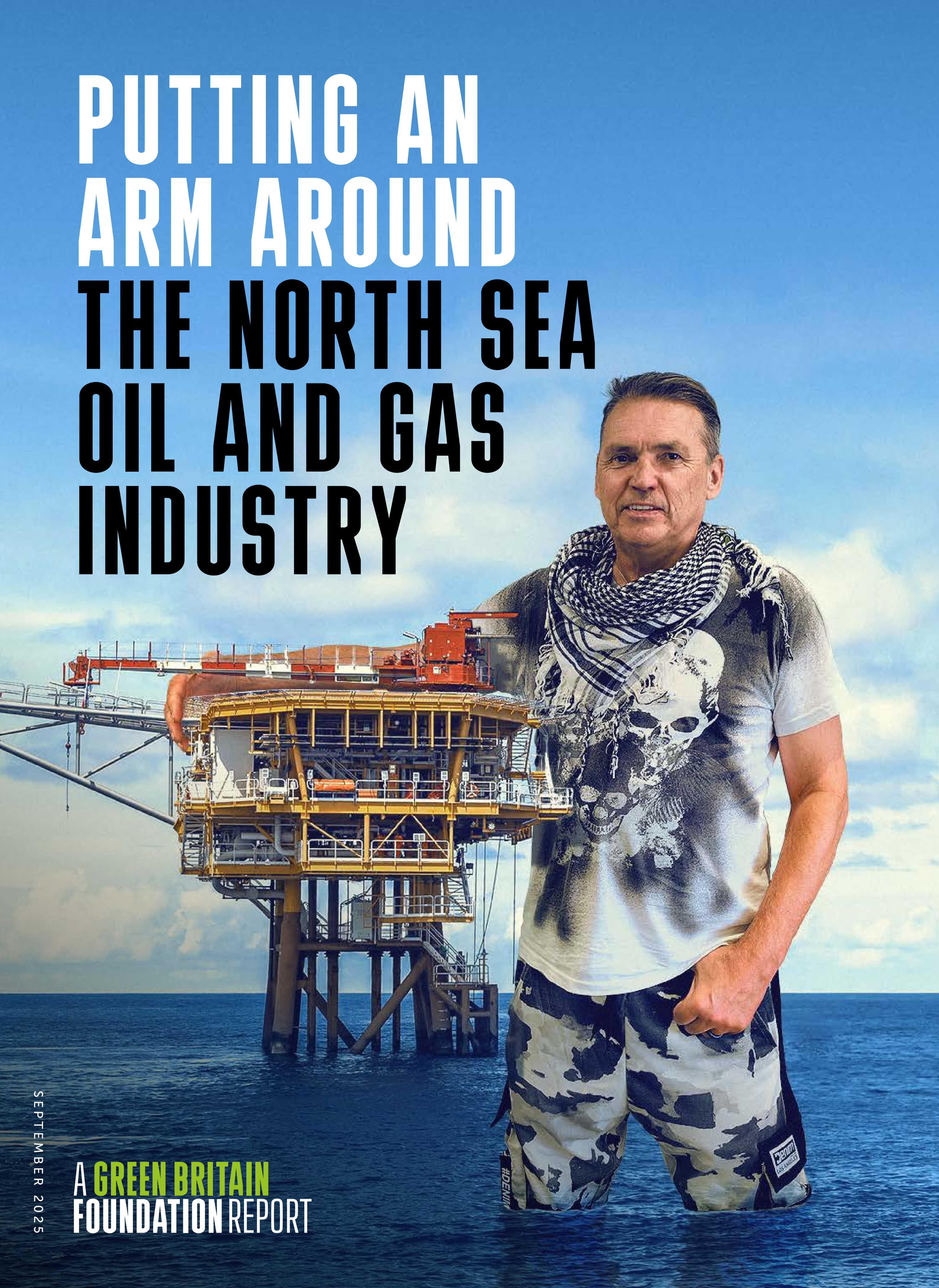
PUTTING AN ARM AROUND THE NORTH SEA OIL AND GAS INDUSTRY



A GREEN BRITAIN FOUNDATION REPORT

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Introduction
It's Time for CfDs in the North Sea

I'm calling on the government to put an arm around our North Sea oil and gas industry – and protect it. Here's why.

The green transition is well underway. The move from fossil to green fuels, from finite and polluting to infinite and clean, is nothing less than the next industrial revolution. It's never been about turning off the taps of oil and gas, stopping the use of fossil fuels overnight – and destroying jobs and investment in our fossil fuel sector in the process. That's a right-wing narrative. The transition is simply about replacing fossil fuels, step by step, with green energy. And, we are well underway.

Our North Sea production peaked a quarter of a century ago and has been in decline since then – we have maybe 10 years left. I believe we should protect this industry and the people that work in it during that last ten years. It's not just a moral issue, it's a matter of common sense and national self-interest. Our oil and gas industry is exposed to the volatility of the international markets which set the price paid – in the next ten years we could easily have a cliff-edge event, whereby operators abandon the sector due to adverse prices. That's no good for anyone.

My suggestion is as simple as it is fair – treat our fossil fuel industry the same way we treat our green energy industry – using the Contract for Difference (CfD) scheme. CfDs are a government-backed scheme that provide a fixed price, fluctuations above or below that are absorbed by the scheme. This scheme has been fundamental in enabling the growth of green energy in our country, by providing stability and certainty – exactly what our North Sea sector needs now.

We can protect jobs, maximise extraction, scrap the widely hated 'windfall tax' – and cut our energy bills. And we can end the toxic narrative that we've seen recently, where net zero has been set up as the enemy of North Sea oil and gas – it simply isn't, and this will show that.

What could be more fair than to treat fossil fuels the same way we treat green energy. It really could not be more simple or more effective. Or more fair.

Let's manage the last part of our transition to green energy in a sensible, grown-up fashion – end the culture war arguments over a tiny remaining resource. And focus on the job of building more green energy, a forever fuel that creates forever jobs and energy security. The wind and sun will never run out on us – as the North Sea has.

Dale Vince OBE
Founder of Ecotricity

What are Contracts for Difference?

The Contracts for Difference (CfD) scheme was introduced in 2014 as a way to support investment in renewable energy and has cross-party support. The scheme was introduced by the Conservative-led Coalition Government and continues to be a key part of Labour's Clean Power 2030 target.

It incentivises investors by guaranteeing a long-term and stable price for the energy produced by the renewable energy asset/generator, which gives investors certainty. Without this guaranteed price, investors would face uncertainty from the volatile wholesale market and be unsure whether they would recover their initial investment.

A CfD is essentially a contract between a renewable energy generator and the Low Carbon Contracts Company (LCCC), which is a government-owned company that administers the scheme. It guarantees a set price for every kWh of energy that the supplier produces and lasts for a set number of years (currently 15 years), which is known as the 'strike price'.

These contracts depend on the wholesale electricity price. If the market price is below the strike price, then generators are topped up with payments from the Low Carbon Contracts Company (LCCC) (with the cost being passed on to suppliers/ consumers on their bills). However, if the market price is above their strike price, then it works in reverse and the generator pays the difference (or surplus) back to the LCCC, with this surplus then being passed back to consumers.

CfD contracts are awarded through auctions, which are known as Allocation Rounds (AR). The first of these – AR1 – took place in 2014 and the most recent – AR6 – took place in 2024.

Policy overview - a CfD for the North Sea

CfDs are therefore a well-established mechanism in the UK energy sector. They provide price guarantees and long-term certainty to investors and businesses.

The UK government should move all North Sea gas generators onto a CfD, which would provide the sector with long-term certainty and protect jobs while the UK reduces its reliance on fossil fuels.
This would set a fixed strike price for electricity produced from North Sea gas, which would be based on the true cost of production and an allowable profit margin. If the market price clears above this strike price, then the difference will be passed back to consumers through lower bills as it is now for renewable generators. If the market price clears lower to the strike price, then the difference will be topped up from consumer bills via the LCCC.

Not only would this provide certainty to these operators, but it would also provide stable energy prices for British businesses and households by reducing the UK's exposure to volatile international energy markets and price spikes.

The strike price for North Sea CfDs could be based on the cost of production with an acceptable profit margin of 10%.

The exact length of these CfDs could be agreed in consultation with the industry and other stakeholders but could align with the length of renewable energy CfDs at 15 years.

Policy benefits – long-term certainty and lower bills

Moving North Sea suppliers to a CfD would provide the following benefits:
Lower bills – by fixing the price generators receive to something closer to the true cost of producing this energy and a fair profit margin, it would remove the excess international market prices that drive up bills.

Price cap - the price cap would no longer need updating as frequently as now due to the price of gas being fixed, which would mean energy bills would be stable.
Price spikes - protect against volatility in international energy markets and price spikes by having a fixed price. A market price above the CfD price would just mean this additional amount is returned to consumers in lower bills.

North Sea jobs – the long-term certainty would protect jobs in the North Sea and the communities they support, allowing the industry to transition in a more orderly fashion.

Cliff edge – CfDs would avoid the potential for a cliff edge with North Sea operators where they walk away if low energy prices render their business unprofitable.

Windfall tax – there would no longer be a need for the Energy Profits Levy, which is politically toxic, complex and much harder for businesses to plan for.

Potential cost savings

The potential cost savings from such a policy are extensive, especially during energy crises and gas price spikes.

Our calculations show that this policy could have saved £50bn over the past five years, with over £20bn saved in 2022 at the height of the energy crisis.

Year	Market price for electricity (£/MWh)	North Sea gas production (TWh)	Savings with a CfD strike price of £13.64/MWh
2020	19.59	439	£2.6bn
2021	44.36	364	£11.2bn
2022	61.42	423	£20.2bn
2023	26.7	383	£5bn
2024	41.48	341	£9.5bn
2025 year to date	27.74	144	£2bn
Total savings			**£50.5bn**

Methodology

To calculate potential cost savings, we have used the assumption of 40p/therm for a theoretical North Sea gas CfD. This equates to a £13.63/MWh strike price and assumes a 10% margin on production costs to allow North Sea operators to make a profit.

We then analysed forward curve gas prices over the past five years and North Sea gas production to calculate how much a CfD would have saved compared to market prices in each year.
Assumptions

Market price – based on forward prices, using a weighted average forward curve price. This most accurately reflects the way that market participants operate and how costs are passed through to customers.

North Sea gas CfD strike price – we have used a strike price of £13.64/MWh, which assumes a 10% margin on production costs to allow firms to make a profit.

North Sea gas output – taken from official UK government statistics on gas production from the UK Continental Shelf in the North Sea.

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Green Britain Foundation
The Green Britain Foundation provide data, insight and information to enable the changes that need to be made — in pursuit of a truly green Britain.

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The analysis was conducted by Carbon Jacked, an independent advisory business that provides technical analysis of environmental policy.

They also offer a range of services for businesses, including carbon accounting, Net Zero target setting, corporate reporting and employee education.