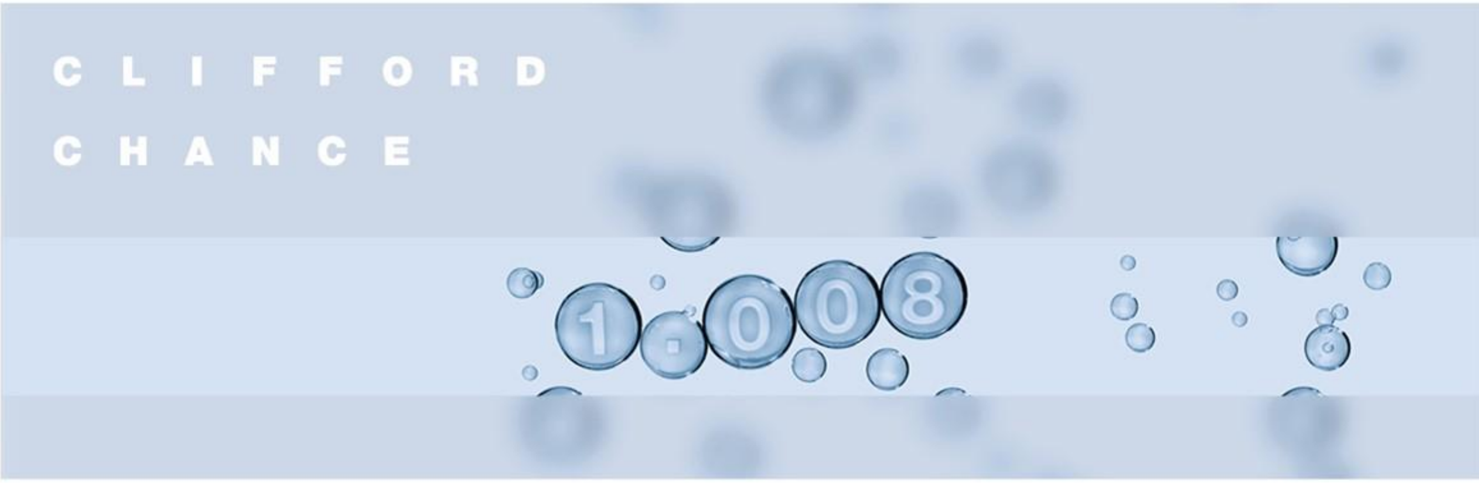

EUROPEAN HYDROGEN BANK: FIRST PILOT AUCTION

On 29 August 2023, the European Commission (the Commission) published the terms and conditions of the EU Hydrogen Bank's (EHB) first pilot auction with an Innovation Fund budget of EUR 800 million to be paid out as a fixed premium to renewable hydrogen producers. The auction is planned to be launched on 23 November 2023.

Key issues

- First auction to be launched on 23 November 2023.
- Proposals must relate to projects located in the EEA.
- EUR 4.50/kg of hydrogen produced as a maximum bid for the fixed premium.
- Maximum grant amount requested by each proposal up to EUR 266.7 million.
- 5 MWe of newly installed electrolyser capacity as minimum technical requirement.
- The production project shall enter into operation within five years after the signing of the grant agreement.
- The hydrogen produced should comply with the "renewability" criteria set out in the renewable hydrogen Delegated Acts under RED II.
- No indexation to cover any unforeseen electricity price changes or inflation.
- First joint European auction to be launched in the first half of 2024, with Member States' financial contribution.

GENERAL BACKGROUND

In March 2023, the Commission published a Communication on the proposed structure and operation of the EHB aiming primarily to create an EU domestic hydrogen market and eventually to support imports to the EU by accelerating investment and bridging the relevant investment gap.

Almost six months later and following several stakeholder consultations, the Commission published the terms and conditions of the first pilot auction to take place on 23 November 2023.

The auction will award up to EUR 800 million to renewable hydrogen producers in the European Economic Area (EEA) in the form of a fixed premium per kg of renewable hydrogen produced over 10 years of operation, bridging the gap between the production costs and the offtake price.

AUCTION TERMS AND CONDITIONS

We set out below the general auction design elements and the qualification requirements that applicant projects and bidders should meet in order to participate in the auction.

General auction design elements

Auctioned good: RFNBO hydrogen in line with the requirements and technical criteria set out in the Renewable Energy Directive (2018/2001/EU) (RED II) and the two Delegated Acts on renewable hydrogen deriving therefrom. RFNBO hydrogen needs to be produced by new production capacity (*i.e.*, capacity for which, at the time of application, start of works had not yet taken place).

Safeguards against over-subsidisation: Ensuring competition through market testing, total available budget and feedback on the level of competition from one round to another.

Bid components: (i) Fixed premium (*i.e*., bid price) in EUR/kg of RFNBO hydrogen production (basis for ranking of bids); (ii) Expected average yearly volume of RFNBO hydrogen production in kg per year over a 10-year production period.

Maximum grant calculation formula:

[Bid price in EUR/kg] × [expected average yearly volume in kg/year] × 10 years

Minimum and maximum yearly production thresholds: There are no upper or lower limits to the expected average yearly production. However, the maximum grant amount requested by each proposal must stay within one-third of the total available Innovation Fund budget for the auction (*i.e*., EUR 266.7 million).

Minimum technical requirements: 5 MWe of newly installed electrolyser capacity (which must be in a single location; virtual pooling of capacity is not permitted).

Production flexibility rule: Semi-annual production can be increased up to 140% compared to half of the expected average yearly volume of RFNBO hydrogen production. Semi-annual production beyond 140% is possible but not supported by grant payments. The total grant amount is restricted to 100% of the maximum grant amount.

Grant duration: The grant agreement will end 10 years after the entry into operation of the project (unless the total RFNBO hydrogen production volume stated in the bid is reached earlier due to the production flexibility rules mentioned above).

Indexation of support: No indexation is provided. Thus, the aid will not be adapted to price-related developments such as electricity prices or inflation.

Required documents and information

To qualify for the price ranking phase of the auction, applicants will have to submit certain application forms and supporting documents via the Commission's Funding and Tenders Portal, such as hydrogen off-take and price hedging strategy, electrolyser procurement strategy, letter of intent from a bank or financial institution to issue a completion guarantee and self-declarations of compliance with the eligibility requirements.

The Commission will assess carefully and mark on a pass/fail basis the following information submitted by the applicants:

- Renewable electricity sourcing strategy
- Timetable/Gantt chart, including financial close and entry into operation milestones
- Hydrogen off-take and price hedging strategy
- Electrolyser procurement strategy
- Environmental permits
- Grid connection permits
- Completion guarantee letter of intent (covering 4% of the maximum grant amount and able to be called by the granting authority if the project does

not reach approved entry into operation within five years after signing the grant agreement)

- Technical and financial maturity based on project plan, financing plan and business plan

Cumulation of aid

Under EU State aid rules, aid may be awarded concurrently under several aid schemes or cumulated with *ad hoc* or *de minimis* aid related to the same eligible costs, provided that the total amount of aid for a project or an activity does not lead to overcompensation or exceed the maximum aid amount allowed under the applicable guidelines.

Cumulation of different measures is possible as long as they concern different identifiable eligible costs, *i.e.*, cumulation is not allowed for partly or fully overlapping costs.

As stated in section 68 of the Guidelines on State aid for climate environmental protection and energy (CEEAG): "…*aid may also distort competition by strengthening or maintaining substantial market power of the beneficiary. Even where aid does not strengthen substantial market power directly, it may do so indirectly, by discouraging the expansion of existing competitors or inducing their exit or discouraging the entry of new competitors. [...]* ***This is also relevant in competitive bidding processes in nascent markets, when there is a risk that a player with a strong market position succeeds in most bids and prevents significant new entry***".

The Commission provided clarifications and examples of aid already awarded to candidate projects that would ***not*** allow those projects to participate in the auction. For example:

- aid to cover part of the CAPEX or OPEX;
- compensation for indirect emission costs provided under the ETS State aid Guidelines;
- reductions from levies or taxes that reflect part of the cost of providing electricity to the beneficiaries, *e.g.*, reductions from network charges or charges financing capacity mechanisms or reductions in electricity taxes.

On the other hand, cumulation with the following types of aid will be allowed:

- previous aid for early project development stages such as research, feasibility studies or FEED studies preceding the commercial operation;
- previous aid for capacity development that is not part of the bid, *e.g.*, if a previous project stage of 5 MWe of capacity has received aid, and a 15 MWe capacity extension is bid into the auction, that bid is eligible (however, a combined 20 MWe bid, comprising 5 MWe previously funded, would not be eligible);
- aid for transport and storage infrastructure connected to the project (*e.g.*, funding under the Connecting Europe Facility), provided that the infrastructure is not dedicated to this project only ('non-dedicated infrastructure');

– reduction from levies on electricity consumption, which finance energy and environmental policy objectives (as described in point 403 and section 4.11 of the CEEAG), even if they qualify as State aid (however, this will be reassessed in future auctions);
– support provided to the electrolyser manufacturers supplying equipment for projects.

It is important to note that, pursuant to the Delegated Act on renewable hydrogen, for RFNBO production projects entering into operation after 1 January 2028 to comply with the 'additionality principle', the renewable electricity installation from which power is sourced should not receive State aid. On the other hand, RFNBO production projects entering into operation before 1 January 2028 do not need to comply with the additionality requirement, and therefore, the relevant renewable electricity production installations can be granted State aid.

Participants will have to submit a self-declaration as part of the application that, by the time of the grant agreement signature, the project is not cumulating excluded types of support and will not do so in the future.

NEXT STEPS

The new auction mechanism will expand the portfolio of support mechanisms that the Innovation Fund currently provides through grants, project development assistance, and other blended financial instruments.

The Commission is expected to launch more auctions in 2024 both for domestic and imported renewable hydrogen. In this context, the Commission has consulted the Member States checking their intention and willingness to contribute to the first joint European auction that is expected to take place in the first half of 2024. In addition, on 28 September 2023, the Commission held a workshop to present its plan for the next auctions and hear the views of with the private sector.

The Commission proposed to use the H2Global instrument to support a Team Europe approach under the European Hydrogen Bank. The instrument will allow them to pool Member States' resources to organise joint European auctions, but it is at the same time flexible enough to accommodate any specific requests from Member States.

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