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| From: | General Secretariat of the Council |
| To: | Delegations |
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| Subject: | Implementation of the European Hydrogen Bank Auctions as a service for Member States - Concept Note - Information from the Commission |

Delegations will find in the Annex an information note from the Commission on the above subject, to be dealt with under "Any other business" at the Council (Environment) meeting on 20 June 2023.

Implementation of the European Hydrogen Bank**Auctions as a service for Member States****Concept Note****- Information from the Commission -****1. Pilot auctions under the Innovation Fund**

As announced in the European Hydrogen Bank Communication¹, the Commission will launch a first pilot auction for renewable hydrogen production in autumn 2023, with an indicative budget of EUR 800 million, coming from the EU Innovation Fund. This pilot auction will select projects to receive a subsidy in the form of a fixed premium, i.e. in EUR/kg of renewable hydrogen produced. Such an auction is a new financial mechanism at the EU-level with a number of advantages notably in terms of cost-efficiency in awarding the support, connecting demand and supply, unlocking private investment and creating vetted price signals that can form the core of future market formation. Last but not least, compared to grants programmes, the auctions mechanism can be administratively leaner.

The Commission has been developing the economic design for the pilot auction (“economic terms and conditions [T&C]”). The Commission will publish these T&C at the beginning of April for stakeholders’ consideration. After stakeholder feedback, the final version of the economic T&C will be published and incorporated into the call for proposal as well as the model grant agreement. The call will open formally in December 2023 but final economic T&C will enable potential bidders to prepare their bids already in advance. This pilot auction will enable the Commission to collect reliable data about the renewable hydrogen project pipeline in the EU, the level of competition, the costs of renewable hydrogen production and types of project interested in such support. Experience from the first auction will be fed into future auction rounds for renewable hydrogen and additional auctions that could be developed for other decarbonisation technologies/products.

The auctions will be implemented by the Commission’s executive agency, CINEA.

¹ 7601/23 - COM(2023) 156 final

2. Rationale for Auctions as a Service

In the European Hydrogen Bank Communication, the Commission has proposed to offer the auctions developed at the EU level also “as a service” to Member States. This would enable Member States to contribute their own financial resources for awarding support to additional projects, located on their territory while relying on an EU-wide auction mechanism for the identification of the most competitive projects. Contributions are voluntary.

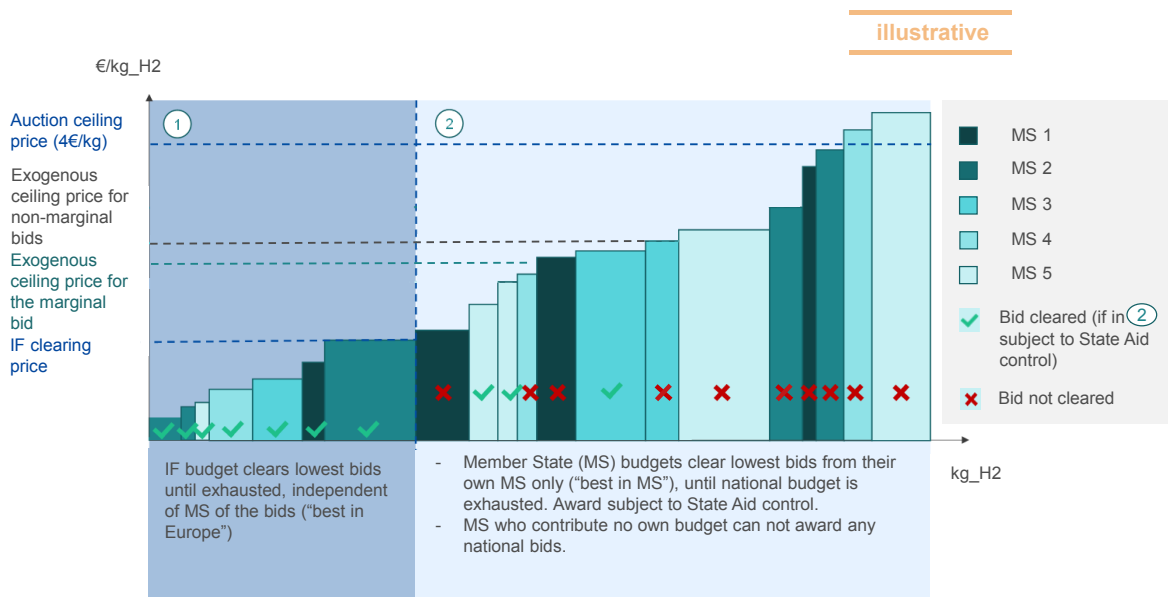
Such a possibility can play an important role for the nascent hydrogen market or markets for other decarbonisation technologies/products where public subsidies may still be needed to incentivise early projects. For these kinds of new markets, it is important to prevent market fragmentation in terms of different national support schemes and the resulting price signals². Project developers, too, would benefit from a single set of rules for winning a subsidy across Europe rather than having to apply to various different funding schemes with different application procedures and timelines. The service can further save administrative costs in developing a number of support schemes by different Member States and bring such subsidies to the market earlier, when they are needed the most.

3. The “Auctions as a Service” (AS) concept

With an “auction-as-a-service” offer, the Commission would run a single auction identifying the projects to be awarded first from the IF budget and then from national budget(s). In this way, the IF budget is spent on the most competitive projects and thus awarding the highest possible volume (of renewable hydrogen production in case of the pilot auctions). This approach would show advantages of an EU-wide market and EU-wide competition: i.e. awarding support to the most competitive projects across the Union (e.g. in more RES-endowed regions or regions that have already relevant industrial clusters) with Union funds. On the other hand, *additional Member State* resources would support projects in that specific Member State.

² A key goal of the EU-wide auctions is price discovery (finding out the levelised cost of renewable hydrogen in Europe). Prices resulting from different kinds of support schemes with different rules are hard to compare.

The auction clearing system is illustrated by the graph below.



Following the qualification assessments of the proposed projects, the ranking of eligible bids and the clearing of those bids awarded within the Innovation Fund budget, the information on the ranking of the additional "supply curve" of further national projects would be passed to respective Member States that have an approved matching State aid scheme, see below. Member States who have committed a national auction budget would award projects on their own territory, beyond those awarded by the IF budget, fully respecting the ranking resulting from the auction. Member States would be also in charge of contract signature, monitoring and payments. In terms of contracts to be signed on national level, the Commission will provide guidance as to the minimum requirements for national contracts.

Once Member State contributions are known, in practice the “auctions as service” consists of the Commission/CINEA informing Member States about results of auction clearing:

- 1) up to Innovation Fund budget amount (this will be projects that will be awarded from the IF budget)
- 2) up to the relevant price ceiling for projects to be funded by a given Member State, or the national budgetary constraint if all bids from that Member State fall below that price ceiling. An exogenous price ceiling formula will be established on the EU-level³.

Member States would then award support to the projects that would be located on their territory, which passed the eligibility checks and made bids within the national budget constraint and the price ceiling for national compartment, provided that the State aid scheme is approved by the European Commission. Member States would need to fully respect the ranking resulting from auction and once budget is committed, there cannot be ex-post budget reduction or withdrawal.

National contributions would not enter the EU or Innovation Fund budget at any point and therefore remain State resources.

The Commission would play an active role in the organisation of knowledge- and best-practice sharing for all awarded projects, both at EU and national level.

³ A price ceiling on the Member State specific part of the supply curve of projects bidding, expressed as a factor x * the price of the last project that cleared in the IF section of the supply curve that is not from that same Member State (=exogenous). The formula will be established at the EU-level.

4. National contributions and State aid clearance

Before the auction is organised, it would be necessary to know Member State contributions. These contributions could come under the new “REPowerEU” chapters of updated Recovery and Resilience Plans, Modernisation Fund, national revenues from ETS auctioning or possible other sources. As national contributions represent State aid, a formal notification of a scheme (or preferably pre-notification) would have to be made by the respective competent national authorities. State aid would be in the form of a scheme (as potentially multiple projects could benefit) and in case of support for renewable hydrogen production it would need to respect the provisions of the Guidelines on State aid for climate, environmental protection and energy (CEEAG)⁴. The Commission aims at facilitating the notification of such schemes and notably specify the conditions on sufficient volume of competition.

For national contributions, Member States would have to notify (or preferably pre-notify) a State aid scheme in advance of the auction in order to verify the respect State aid rules.

The notified State aid scheme would comply entirely with the environmental conditions and subsidy allocation/award process of the IF. The scheme should not introduce additional pre-selection/award criteria compared to those set out under the IF auction.

The approval of the State aid scheme is dependent on full compliance with State aid rules. One important compatibility criterion is a sufficient level of competition in the auction. In order to avoid the situation that the final approval can only be made once the auction is cleared and the level of competition is revealed, the design of the scheme will need to include features that ensure upfront the necessary level of competition (e.g. commitment to reducing the auction budget in the next round should there be insufficient competition and exogenous Member State specific price ceilings). To facilitate and streamline the pre-notification of such State aid schemes, the Commission will provide guidance to Member States signalling their intention to use the EU auction as a service for their national auction. The pre-notification should start well ahead of the launch of the EU auction to facilitate the adoption of a State aid decision before the auction is launched.

⁴ https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv%3AOJ.C_.2022.080.01.0001.01.ENG&toc=OJ%3AC%3A2022%3A080%3ATOC

Importantly, pooling the resources from the EU Innovation Fund and Member States means that the auction could potentially become less competitive. The auctions will therefore feature safeguards against such a situation, including possible project pipeline analyses by participating Member States, an exogenous Member State specific ceiling price, and resizing the budget between the auction rounds in function of the expected level of competition.

5. Engagement with Member States

The national contributions depend on the fiscal space of Member States, whether they already have a support scheme for renewable hydrogen production (only few have) and the benefits that they see in this service. This is why the following process is currently envisaged for engagement with Member States:

1. The Commission published the draft economic design/T&C of the auction on 31 March.
2. The Commission is consulted Member States and stakeholders on the economic design/T&C of the auction (until early June).
3. Letter sent to Deputy Permanent Representatives to ask about interest to use auctions as service. Commission organised informational meeting (26 May 2023).
4. The economic design of the auction will be finalised and published, taking on board feedback from Member States (July/August 2023).
5. Member States signal interest in taking part in AS. Commission provides further detailed guidance/template on the essential elements that the MS schemes should have⁵, after interest to dedicate budget has been indicated (open for expression of interest).
6. Member States start pre-notification discussions with EC. If necessary, bilateral CLIMA/COMP meetings are organised with the interested Member States.

⁵ For example provisions on monitoring, transparency, reporting and payment arrangements, indication of the budget that Member States intend to allocate for the national compartment of the auction.

7. Member States send the complete notification of national schemes for the use of AS. These notifications include provisions on monitoring, transparency, reporting and payment arrangements. As part of the notification, Member States must indicate the budget that they intend to allocate for the national compartment of the auction.
8. EC (DG COMP) issues swift decision on national schemes.
9. EC launches the auction in December (final T&C will be available in July/August).
10. CINEA clears the auctions in Q1 2024 and passes the information about national projects cleared with respective national budgets (these are projects that (1) pass qualification, (2) are ranked, (3) within the budget limits and price ceilings) to Member States.
11. CINEA signs the contracts with projects cleared within the IF budget. Member States sign contracts with additional auction winners, fully respecting the ranking resulting from the auction.
12. Member States monitor the respective projects and pays grants based on performance. CINEA monitors projects and pays grants that are awarded with the IF budget.
13. CINEA and Member States cooperate to organise knowledge-sharing for projects awarded at EU and Member States level.

Illustration of the AS process

