

ENERGY ACT 2013

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 2: Electricity Market Reform

Chapter 5: Conflict of interest and contingency arrangements

Section 45: Modifications of transmission and other licences: business separation

237. *Subsections (1) to (5)* of this section provide that the Secretary of State may modify the conditions of existing electricity licences and codes for the purposes of imposing business separation measures between “system operation functions” (or one or more individual system operation functions), and other functions. But he or she can only do this where it is necessary or desirable as a result of new functions being given to the national system operator in respect of electricity market reform.
238. *Subsection (3)* defines “system operation functions” so as to include system operation functions authorised under a transmission licence and “EMR functions”. *Subsection (10)* subsequently defines “EMR functions” as functions conferred by or by virtue of Chapter 2, Chapter 3 or Chapter 4 – being the delivery functions conferred on the national system operator in relation to contracts for difference, the capacity market and investment contracts.
239. *Subsection (5)* requires the Secretary of State, in exercising this power, to consider the possible impacts it would have on the efficient and effective operation of the electricity system.
240. *Subsection (6)* provides a list of the types of measures this could include, for example:
- legal separation: requiring a separate subsidiary to carry out EMR functions;
 - limiting the control or influence which a parent company or other subsidiary can exercise over the body which carries out EMR functions;
 - requiring functions to be carried out in separate locations, on separate IT systems or by separate employees;
 - requiring separate accounts to be produced, and
 - requiring information separation between EMR and/or system operation functions, and other parts of the national system operator’s business.
241. *Subsection (7)* gives the Secretary of State power to require the national system operator to produce annual compliance reports concerning the separation measures.

Section 46: Power to transfer EMR functions

242. This section confers a power on the Secretary of State to transfer the delivery functions for the CFD and capacity market schemes and those relating to investment contracts (“EMR functions”) to a new delivery body in certain situations.

243. *Subsection (1)* confers the power to transfer the EMR functions from the national system operator to a different delivery body. The power is exercisable by negative resolution order (see *subsections (6) and (7)* of section 47).
244. *Subsection (2)* provides that the EMR delivery functions can be transferred in five circumstances.
- where the national system operator requests a transfer;
 - where the national system operator is subject to an energy administration order granted under the Energy Act 2004; energy administration orders may be made by the court under a special regime to ensure that energy network companies provide secure energy supplies in insolvency situations;
 - where there has been a change of control of the national system operator and the Secretary of State considers it necessary or desirable to transfer the functions as a result of that change;
 - where the Secretary of State considers that the EMR delivery functions are not being performed efficiently and effectively;
 - if the Secretary of State considers it necessary or expedient in order to further the purposes for which CFD or capacity market regulations are made; for example, if he or she considers that it is necessary to change delivery body in order to encourage low carbon electricity generation, or in order to meet the demands of consumers for the supply of electricity in Great Britain.
245. *Subsection (3)* defines the circumstances in which the national system operator poor performance trigger could be used. The Secretary of State is required to notify the national system operator of his or her opinion that it is failing to perform its functions in an efficient and effective manner. If, after six months, the Secretary of State considers that the failure has not been rectified, the functions may be transferred.
246. *Subsection (4)* explains the definition of control to be used in relation to the change of control trigger in *subsection (2)*.
247. *Subsection (5)* requires that the national system operator be consulted if the Secretary of State transfers the functions because he or she considers it necessary or expedient in order to further the purposes for which CFD or capacity market regulations are made. *Subsection (6)* allows the Secretary of State to avoid consulting where the urgency of the case would make it inexpedient to do so.
248. *Subsection (7)* allows the Secretary of State to make further transfers of the EMR delivery functions, including a transfer of the EMR delivery functions back to the national system operator.
249. *Subsections (9) and (10)* require the consent of the alternative delivery body when this is someone other than the Secretary of State. This includes any re-conferral of the functions on the national system operator.

Section 47: Orders under section 46: fees and other supplementary provision

250. *Subsections (1) and (2)* of this section allow the transfer of functions order to provide the alternative delivery body with the power to require fees to be paid in relation to any EMR functions it carries out. It also makes provision about the scope of the power under section 46 (*subsections (3) to (5)*), the parliamentary procedure for orders (*subsections (6) and (7)*) and requires the Secretary of State to consider whether licence modification powers should be used, for example to remove any obligations intended to manage conflicts of interest of the national system operator (*subsections (9) and (10)*).
251. *Subsection (8)* introduces Schedule 3, which confers a power on the Secretary of State to transfer property, rights and liabilities, by transfer scheme, when he or she exercises

his or her power to transfer EMR delivery functions under section 46. Transfer schemes are used to enable the transfer of functions to operate efficiently and effectively.

252. *Paragraph 1* of Schedule 3 sets out the power to make one or more transfer schemes. The transfer schemes would list the property, rights and liabilities being transferred, and state the date on which the transfer is to take place. Transfer schemes are not subject to any parliamentary procedure. *Paragraph 2* sets out the full scope of the transfer power. *Paragraph 3* requires the Secretary of State to include provision for payments of compensation to those whose interests are adversely affected by a transfer.

Section 48: Energy administration orders

253. This section amends the Energy Act 2004 to extend the special administration regime for the national system operator to include its EMR functions.
254. Special administration regimes act as an alternative to general insolvency law and procedures. They are designed to ensure uninterrupted and safe operation of essential services in the event of a company becoming insolvent. Special administration regimes exist for electricity transmission (including system operation) and distribution, gas transportation licensees, water and rail companies and parts of the banking sector.
255. Under the special administration regime introduced by the Energy Act 2004, the Secretary of State (or the Authority with the Secretary of State's consent) can apply to the court for an energy administration order, which may be granted where the company meets the statutory tests for insolvency. In these circumstances, the court would appoint an energy administrator, whose statutory objective would be to ensure "that the company's system is and continues to be maintained and developed as an efficient and economic system". The energy administrator is required to do this by (if possible) managing the company as a going concern.
256. This section amends the special administration regime to provide that where EMR delivery functions have been conferred on the system operator then the administrator has an additional objective of ensuring that the EMR functions are performed in an efficient and effective manner. In a situation where the old and new objectives could not be secured in a consistent way, the new objective would be subordinate to the primary objective of maintaining and developing an efficient and economic system.