

# **ENERGY ACT 2013**

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## **EXPLANATORY NOTES**

### **COMMENTARY ON SECTIONS**

#### **Part 2: Electricity Market Reform**

##### ***Chapter 1: General considerations***

##### ***Section 5: General considerations relating to this Part***

83. This Chapter places a duty on the Secretary of State to have regard to certain matters when setting up the CFD scheme and the capacity market or making changes to them. The section requires the Secretary of State to take account of the government's obligations under the Climate Change Act 2008 to meet the 2050 target and to stay within carbon budgets, the duty to meet any decarbonisation target range once this has been set, the need to ensure security of electricity supplies (which might include, for example, having a diverse mix of generation technologies), the likely cost to consumers in the parts of the United Kingdom affected by the decision he or she is taking and the United Kingdom's obligation to meet European Union targets on the use of energy from renewable sources.
84. This Chapter also sets a duty for the Secretary of State to lay an annual report to Parliament on how the EMR functions under Part 2 have been carried out.

##### ***Chapter 2: Contracts for difference***

##### ***Section 6: Regulations to encourage low carbon electricity generation***

85. This sets out the Secretary of State's power to make regulations about contracts for difference.
86. A CFD is a contract between a CFD counterparty and an eligible generator which was offered by the CFD counterparty because the legislation has required the CFD counterparty to offer it. Whether a generator is eligible or not will be set out in regulations. The regulations can only make provisions which, in the opinion of the Secretary of State, will encourage low carbon electricity generation. Therefore only low carbon electricity generation will be eligible. This would include renewable generation, nuclear generation and generation using carbon capture and storage.
87. *Subsections (7) to (9)* provide that regulations must be made by statutory instrument and that:
- the first time regulations are made relating to:
    - CFD notification: offer to contract on standard terms (section *14*);
    - Modification of standard terms (section *15*);
    - Information and advice (section *19*);

- Functions of the Authority (section20).
- Or any regulations relating to:
  - Supplier obligation (section9);
  - Direction to offer to contract (section10);
  - CfD notifications (section12);
  - Allocation of CfDs (section13);
  - Payments to electricity suppliers (section17);
  - Application of sums held by a CFD counterparty (section18);
  - Regulations: further provision (section21);
  - Enforcement (section22);
  - Limits on costs to be incurred (section23).

they must be laid in draft before, and approved by affirmative resolution of, each House of Parliament.

88. *Subsection (10)* provides that regulations relating to Contracts for Difference should not be treated as a hybrid instrument. The regulations are expected to specify a private company and confer functions on it which could be regarded as adversely affecting its private interests (i.e. they would be unable to stop performing functions without amendment to the regulations), raising the possibility that they could be considered hybrid. It is not considered necessary for the regulations to be treated as hybrid because the existing duty to consult before making regulations should provide adequate protection that private interests will be fully considered.

### ***Section 7: Designation of a CFD counterparty***

89. This sets out the power allowing the Secretary of State to designate a company or a public authority, with the consent of that person, to act as the counterparty for the CFD. The counterparty will enter into and manage CFDs with eligible generators, and will act as the interface between generators and suppliers.
90. *Subsection (3)* allows the counterparty to be a registered company or a public authority. Whilst it is expected that the counterparty will be owned by Government, any designated counterparty would have access to the same rights (such as to the Supplier obligation) and be bound by the same duties under the legislation, regardless of whether it was a company and / or public authority, or whom it was owned by.
91. Under *subsection (6)* the designation of a company as the CFD counterparty can be revoked by the Secretary of State. Designation will also cease if the CFD counterparty elects to withdraw its consent and gives 3 months prior notice to the Secretary of State of that withdrawal. *Subsections (7) to (10)* deal with the continuity of CFD counterparties. If the designation of a CFD counterparty were to lapse the Secretary of State must as soon as reasonably practicable designate another counterparty and make a transfer scheme under *Schedule 1* transferring all CFDs to that new counterparty. This is designed to ensure that there is always a CFD counterparty and that where a CFD counterparty ceases to be designated the contracts are transferred to a new CFD counterparty.
92. *Schedule 1* sets out the process by which the property, rights and liabilities of the CFD counterparty may be transferred from one counterparty to another, should this prove necessary either because a counterparty no longer wishes to be designated, or because it has become inappropriate for a counterparty to be designated in this role. A scheme

may provide for compensation for any property that is required to be transferred where this is appropriate.

### ***Section 8: Duties of a CFD counterparty***

93. This section makes it clear that it is a duty of a person who has been designated as a CFD counterparty to comply with the regulations and any direction made under these provisions. This will include the requirement for the CFD counterparty to enter into a CFD with a generator when the Secretary of State has directed it to or the national system operator has given a notification under section 12, and to comply with any requirements designed to ensure it manages the contracts in line with the direction of the Secretary of State. The national system operator is currently National Grid Electricity Transmission PLC.
94. *Subsection (2)* also places a duty on the CFD counterparty to exercise its functions to ensure that it can meet its liabilities under a CFD. Those functions are principally those conferred under or by virtue of *section 9* (Supplier obligation) in relation to the ability of the CFD counterparty to recover sums from licenced electricity suppliers. “Liabilities” in this context includes all liabilities under a CFD. For these purposes, liabilities will exist in respect of any sums that are owed at a particular time by the counterparty under the CFD, irrespective of whether they have yet become payable in accordance with any payment provisions it contains.

### ***Section 9: Supplier obligation***

95. This places an obligation on the Secretary of State when making regulations under section 6 to include provision requiring electricity suppliers in GB and Northern Ireland to make payments to the CFD counterparty so that the body has sufficient funds to make the totality of the payments to generators that are required under CFD contracts. Suppliers may also be obliged to make payments to cover administration costs for managing the CFD counterparty. Payments may also be required in order to enable the CFD counterparty to hold sums in reserve (*subsection (2)(b)*), and to mutualise costs across suppliers to cover those not made by an insolvent or defaulting supplier (*subsection (2)(c)*). *Subsection (4)* enables the regulations to require suppliers to provide collateral.
96. *Subsection (5)* specifies that the regulations will place the CFD counterparty under a duty in relation to the collection (including enforcement) of sums that are owed to generators.
97. *Subsections (6) to (8)* enable the Supplier Obligation to be varied according to the supplier or factors in relation to a supplier (such as the amount of electricity it supplies to particular groups of consumers). It also provides for the CFD counterparty to provide notices to suppliers and to enforce such notices, and for dispute resolution arrangements.
98. *Subsection (9)* clarifies that any sum which the supplier is required to pay the Secretary of State, the investment contract counterparty or the CFD counterparty by virtue of the supplier obligation regulations and which is not paid when it is due under the regulations is recoverable as a civil debt.

### ***Section 10: Direction to offer to contract***

99. *Section 10* confers a power on the Secretary of State to issue a direction to the CFD counterparty to offer a CFD to eligible generators in accordance with provisions set out in regulations. It is expected that most CFDs will be allocated to eligible generators by the national system operator, National Grid, in accordance with section 12 and any provision made using the power in section 12. However, where flexibility is needed to vary the terms for particular projects beyond what is permitted by the modification of

standard terms process (section 15), the Secretary of State will allocate CFDs using the power conferred under section 10.

100. A contract will only come into being on the agreement of a generator to whom an offer is made by the CFD counterparty.
101. *Subsection (3)* requires that regulations define an “eligible generator” for CFD purposes.
102. *Subsections (6) to (8)* provide that any direction which relates to generating stations in Northern Ireland may not be made without consent of the Department of Enterprise, Trade and Investment. This will enable Northern Ireland Ministers to play a role in being satisfied that the terms to be offered to generators in Northern Ireland are suitable.

### ***Section 11: Standard terms***

103. This gives the Secretary of State power to issue and, from time to time, revise standard terms for the CFD (*subsections (1) and (2)*, respectively). This section works in concert with sections 12 to 14 to make up the standard system for CFD allocation, from application to offer of a contract.
104. *Subsection (3)* places the Secretary of State under a duty to issue or revise standard terms in accordance with provision made in regulations. *Subsection (4)* requires the Secretary of State to have regard to the matters listed in section 5(2) when issuing or revising standard terms. *Subsection (5)* places the Secretary of State under a duty to publish standard terms as issued or revised under this section. *Subsection (7)* would allow for different standard terms to be issued for different categories of CFD (for example, for generators in Northern Ireland). *Subsection (6)* enables the Secretary of State to designate particular standard terms as terms which may not be modified under section 15.

### ***Section 12: CFD notifications***

105. This sets out how the System Operator is to notify the CFD counterparty of an allocation decision. *Subsection (1)* states that such a notification must specify the eligible generator and “such other information as may be required by the CFD counterparty for the purpose of making an offer under section 14”. *Subsection (2)* prevents a notification from being given if regulations made under section 23 (regarding maximum costs and targets) prevent it. *Subsection (3)* allows for regulations to make further provision about the circumstances in which a notification may or must be given, the kinds of information that must be specified in a notification, and appeals against decisions not to give a notification.
106. *Subsections (4), (5) and (6)* make provision for the involvement of the Department of Enterprise, Trade and Investment in the application of this section in Northern Ireland.

### ***Section 13: Allocation of CFDs***

107. This section builds on the power in section 12 and specifies the process by which the Secretary of State may make provision setting out detailed rules about the CFD allocation process. The rules are likely to be applicable to those wishing to apply for a CFD and to National Grid who, as the System Operator, will be acting as the Delivery Body.
108. *Subsection (1)* confers a power enabling the Secretary of State to make provision setting out how CFDs are to be allocated to eligible generators. *Subsection (2)* confers a power for setting the rules of allocation in an “allocation framework” – a document which will sit outside of regulations but be constrained by provision made in regulations. An “allocation framework” will be produced and published for allocation rounds, and include information about when allocation rounds will be held. The “allocation framework” will act as a “rule book” for how allocation rounds will operate. *Subsection*

(2)(e) confers a power enabling the Secretary of State to make provision about what must be included in an “allocation framework”.

109. For example, the Secretary of State may decide that it is important to investors to ensure that an “allocation framework” includes information about the budget available for a particular allocation round and may therefore require an “allocation framework” to contain this information when it is produced.
110. *Subsection (3)* confers a power enabling the Secretary of State to set out requirements on the Secretary of State. For example, the Secretary of State may stipulate in regulations for specified notice periods to be adhered to before the start of allocation rounds, and separately restrict the Secretary of State’s ability to amend the allocation framework for those participants already engaged in an open allocation round. These sorts of requirements on the Secretary of State will help to provide certainty to industry that the process will not change without due warning. This is necessary to allow them to engage with the allocation process.
111. The powers in *subsections (4) to (6)* enable the Secretary of State to set out further detail of those areas that an Allocation Framework may provide. These include conferring functions on the System Operator to allow them to carry out the allocation process, the setting of targets for types or location of generation, the mechanics of competitive allocation, and allowing for calculations and determinations to be made to support the allocation of CFDs. These are all functions which may need to change at short notice, allowing the Government to respond in a timely manner to external factors, to protect budgets and to protect consumers by preventing gaming. Examples of such changes that might be necessary are responding to a sudden change in the costs of a particular technology, or allowing change to the mechanism for competitive allocation in response to lessons learned during operation.
112. *Subsection (7)* allows any allocation framework made to be amended, and *subsection (8)* provides that *subsections (4) to (7)* are subject to any provision in regulations which could set limits on what can be contained in the allocation framework.

#### ***Section 14: CFD notification: offer to contract on standard terms***

113. This section sets out how the CFD counterparty must act upon a notification from the System Operator to offer a CFD contract. *Subsection (1)* places a duty on the CFD counterparty to offer a contract to the eligible generator specified in a notification, and requires that this offer be on the standard terms, or on the standard terms as modified in accordance with the procedure provided for in section 15.
114. *Subsection (2)* confers a power on the Secretary of State to make further provision regarding matters such as how the CFD counterparty is to apply or complete the standard terms in response to a notification and how the eligible generator to whom the offer is made may enter into a CFD as a result.

#### ***Section 15: Modification of standard terms***

115. **Section 15** enables the CFD counterparty to agree modifications to the standard terms with generators, on a case by case basis, pre-signature. This flexibility to make such modifications allows a wider range of eligible generators to participate in the CFD regime than would otherwise be the case. This will be because, especially in the early stages of the CFD regime, the standard terms will not be acceptable to some generators for reasons such their specific types of company, financing or debt structure, without such small modifications.
116. This flexibility is constrained in order to reduce the risk of generators using it to negotiate improvements to the standard terms for competitive reasons. *Subsection (3)* specifies that a modification can only be agreed if it is both ‘minor’ and ‘necessary’, as determined by the CFD counterparty, following provision made in regulations.



*Subsection (4)* provides for further provision to be made in regulations, including regarding the circumstances in which a generator may request a modification, the procedure to be followed in requesting a modification, and how the CFD counterparty is to make a determination on such a request.

### ***Section 16: Sections 12 to 15: further provision***

117. **Section 16** confers a power enabling the Secretary of State to, when making provision under the powers in sections 12 to 15, make further provision enabling calculations and determinations to be made by such persons and in accordance with such procedure as is specified.
118. For example, in relation to section 12, section 16 enables the CFD counterparty to make determinations or calculations about what information should be included in the notification provided by the System Operator. In relation to section 14, section 16 enables the CFD counterparty to determine precisely how the information in the notification should be applied to the contract, and whether a generator's response to an offer is acceptable. Finally section 16 may also be used in relation to section 15 to enable the CFD counterparty to determine whether a generator has provided sufficient information and evidence that a modification is both minor and necessary.

### ***Section 17: Payments to electricity suppliers***

119. **Section 17** enables regulations to require the CFD counterparty to make payments to suppliers. This is designed to enable payments to suppliers where the contracts provide for money to be paid to the CFD counterparty e.g. where the reference price is higher than the strike price.

### ***Section 18: Application of sums held by CFD counterparty***

120. This section enables the regulations to make provision about the allocation of sums between generators by the CFD counterparty in circumstances where the supplier obligation is not large enough to meet all of its obligations in full. In making these regulations, the Secretary of State must have regard to the principle that sums should be apportioned in proportion to the amounts which are owed, i.e. that they are pro-rated between generators (*subsection (3)*).
121. *Subsections (4) and (5)* enable the regulations to make provision about the use of sums a CFD counterparty holds and for the circumstances where monies received should or should not go to the Consolidated Fund.

### ***Section 19: Information and advice***

122. **Section 19** enables the regulations to make provision to ensure that information and advice required to make the scheme work is provided to the bodies requiring it at appropriate points, including from generators and suppliers, as well as from the Northern Ireland system operator and Authority for Utility Regulation for the purpose of allowing the CFD to operate in Northern Ireland. It enables regulations to make provision governing the use and protection of information so received to ensure it is handled in an appropriate manner.
123. It will also allow the Secretary of State and the Regulator to monitor the scheme and for the Secretary of State to require advice from the national system operator, the CFD counterparty body and the Regulator necessary for making decisions about the running of the scheme.

### ***Section 20: Functions of the Authority***

124. **Section 20** enables the regulations to confer functions upon the Authority (the regulator for the electricity markets in Great Britain) to provide advice to and make

determinations for the parties to CFDs. This could include, for example, monitoring obligations under the contract such as biomass sustainability and determining whether such obligations have been met, where the Authority will be exercising the role of expert determination in relation to the contract.

### ***Section 21: Regulations: further provision***

125. This section enables the regulations to make provision to require the CFD counterparty to enter into arrangements or to offer contracts for purposes connected to a CFD, or to specify things that the CFD Counterparty can or can't do. This provision only regulates the behaviour of the CFD counterparty and does not enable the Secretary of State to vary any CFD without the consent of the generator in question.
126. *Subsection (1)(c)* enables regulations to make provision about the making of directions to the counterparty. This will enable specific directions to be given in relation to particular contracts or matters (such as where a generator has proposed a variation to the contract and the Secretary of State wishes to require the counterparty to agree to it).
127. *Subsection (3)* places a duty on the Secretary of State. The regulations that he or she makes must include such provision as he or she considers necessary to ensure that the CFD counterparty can meet its liabilities under CFDs. As set out in relation to section 8 above the reference to liabilities means all sums which are owed under a CFD.

### ***Section 22: Enforcement***

128. **Section 22** enables the obligations of suppliers under regulations made under this Chapter to be enforced by the Authority in Great Britain, or the Northern Ireland Authority for Utility Regulations in Northern Ireland, as if they are relevant requirements. This means that a breach can be treated, in effect, as if it were a breach of a licence condition allowing the enforcement authorities to get an order to secure compliance, and/or impose financial penalties.
129. It also enables the system operator's functions to be enforced by the Authority.

### ***Section 23: Limits on costs to be incurred***

130. This enables the Secretary of State to make regulations setting out a limit on the cost of the scheme.
131. It also includes powers for the Secretary of State to instruct the national system operator that the maximum cost has been reached and prevent them from giving a notification to the CFD counterparty if the Secretary of State believes it may cause the maximum cost to be breached.

### ***Section 24: Consultation***

132. This section requires that the Secretary of State must consult licensed suppliers in Great Britain and Northern Ireland, the national system operator and the Authority before making or amending secondary legislation. The Department of Enterprise, Trade and Investment in Northern Ireland, and Scottish and Welsh Ministers are also required to be consulted.

### ***Section 25: Shadow directors, etc.***

133. This makes it clear that, in exercising their regulatory controls over the CFD counterparty, neither the Secretary of State nor the national system operator could be deemed to be in any way managing or controlling the CFD counterparty in such a way that would class them as, for example, "shadow directors" or principal to the CFDs (in other words that the CFD counterparty is not the agent of either the Secretary of State or the national system operator).

### **Section 26: Licence modifications**

134. This sets out the Secretary of State's power to modify transmission and distribution licences, the standard conditions of such licences and documents maintained in accordance with conditions of such licences (such as industry codes) to allow the CFD counterparty to be provided with services (such as settlement services).
135. The powers will be used to confer consequential functions upon the national system operator to enable it to administer the CFD scheme as well as providing services to the CFD counterparty. It will also be used to make provision about settlement of payment obligations under CFDs and enable licensees to assist with the enforcement of obligations under contracts. Section 64 makes further provision about licence modifications.

### **Chapter 3: Capacity Market**

#### **Section 27: Power to make electricity capacity regulations**

136. This section enables the Secretary of State to make regulations ("electricity capacity regulations") about the provision of capacity to meet the demands of consumers for the supply of electricity in Great Britain. *Subsection (3)* specifies that "providing capacity" means providing electricity or reducing demand for electricity. *Subsection (4)* makes clear that provision made about "reducing demand for electricity" can include provision that reducing the consumption of electricity reduces demand.

#### **Section 28: Capacity agreements**

137. This section provides that electricity capacity regulations may make provision about capacity agreements, and specifies some particular matters relating to capacity agreements about which such provision may be made.
138. *Subsection (2)* states that a capacity agreement is an instrument that can give rise to obligations for the holder of the agreement (a "capacity provider") and for electricity suppliers. It can require a capacity provider to provide capacity (i.e. provide electricity or reduce demand for electricity) and to make payments for the benefit of electricity suppliers ("capacity incentives"). A capacity provider may, for example, be required to pay a capacity incentive if their capacity was not delivering electricity in circumstances defined in or determined in accordance with regulations. In addition, all electricity suppliers may be required to make payments ("capacity payments") for the benefit of capacity providers; it is intended that the revenue payable to capacity providers under capacity agreements will be funded by electricity suppliers in this way.
139. *Subsections (2)(b)* and *(c)* allow capacity agreements to provide for capacity payments and capacity incentives to be paid to an intermediary (a "settlement body") as referred to in *subsection (4)(g)*.
140. *Subsection (3)* enables electricity capacity regulations to make provision regarding the definition of "electricity suppliers" for the purposes of a capacity agreement. For example this may allow a threshold to be put in place to exclude smaller suppliers if the Secretary of State considered that it was not proportionate to require all electricity suppliers to pay for the costs of the Capacity Market.
141. *Subsection (4)* identifies the sort of provision that may be made about capacity agreements in electricity capacity regulations, including: the terms of a capacity agreement; how capacity agreements will be issued; the persons who may be a capacity provider; the circumstances in which capacity must be available; the duration of a capacity agreement; the calculation of payments associated with capacity agreements and the body that will administer those payments; the enforcement of the terms of a capacity agreement; resolution of disputes; and the circumstances in which a capacity agreement may be changed, terminated, assigned or traded.



142. *Subsections (5)(a) and (b)* clarify that such provision can include provision conferring functions on the national system operator to issue capacity agreements, and provision about the outcome of a capacity auction (see section 29). For example this would enable a requirement to be placed on the national system operator to issue a capacity agreement to a person whose bid is successful in a capacity auction. *Paragraphs (c) and (d)* enable electricity capacity regulations to set out the eligibility criteria for persons before they may enter a capacity auction or become a capacity provider. In particular, those persons may be required to meet certain conditions, or to satisfy the national system operator of certain matters, as provided for in electricity capacity regulations.
143. *Subsections (6)(a) and (b)* enable regulations to include provision for the calculation and determination by the settlement body, or by another person specified by the regulations, of the amounts of capacity payments and capacity incentives due from or owed to electricity suppliers or capacity providers.
144. *Subsection (7)* clarifies that regulations may include, in particular, a requirement for a person to consent to an inspection of plant or premises. For example this may be necessary to determine whether the person is capable of providing capacity under a capacity agreement.

### **Section 29: Capacity auctions**

145. This section enables the Secretary of State to make provision in electricity capacity regulations for the determination on a competitive basis (i.e. through capacity auctions run by the national system operator) of who may be a capacity provider.
146. *Subsection (2)* allows the Secretary of State to make provision for the national system operator to run capacity auctions, the circumstances in which a capacity auction is to run, the intervals at which auctions are to take place and the process by which auctions are to be run. For example the Secretary of State may specify the process by which bids into the capacity auction are assessed and how it will be decided which bids are successful. *Subsection (2)(c)* enables regulations to make provision about the amount of capacity in relation to which a determination may be made, for example how the total amount of capacity required from a particular capacity auction is to be determined; *subsection (4)* specifies that the function of determining that amount may be conferred on the Secretary of State or the Authority but not on any other person.
147. *Subsection (3)* provides for electricity capacity regulations to require the national system operator to prepare and publish rules or guidance about capacity auctions, and for the process to be followed in doing so.
148. *Subsection (5)* clarifies that provision made within *subsection (2)(f)*, which relates to the manner in which the Secretary of State exercises any function in relation to capacity auctions, may include provision about the frequency of any decision, the persons who will be consulted and the matters to be taken into account. For example the Secretary of State may take a decision on the amount of capacity which is to be sought through a particular capacity auction, on an annual basis, taking into account information or advice relating to available capacity and consumer demand.

### **Section 30: Settlement body**

149. In the event that a settlement body is appointed to administer capacity payments and capacity incentives, this section enables regulations to require electricity suppliers or capacity providers to make payments to the settlement body for certain ancillary purposes. Under *subsection (1)*, payments may be required to cover the settlement body's administration costs, to enable it to hold sums in reserve, and to mutualise payments across suppliers to cover those not made by an insolvent or defaulting supplier. *Subsection (3)* also enables the regulations to require electricity suppliers or capacity providers to provide collateral. *Subsections (4) and (5)* enable regulations to include provision for the determination by the settlement body or by another person

specified by the regulations, of the amounts of payments due from electricity suppliers or capacity providers, under this section and the form and terms of any collateral.

***Section 31: Functions of the Authority or the national system operator***

150. This section enables the Secretary of State to make provision in electricity capacity regulations to confer functions on the Authority or the national system operator.

***Section 32: Other requirements***

151. This section enables the Secretary of State to make provision to impose other requirements, in addition to those particularly associated with capacity agreements, on licence holders, persons carrying out functions under the capacity market and any other person who is, or has ceased to be, a capacity provider.
152. *Subsection (3)* sets out that such requirements may, in particular, include requirements relating to the manner in which functions are to be exercised, restrictions on the use of generation plant and participation in a capacity auction, and the inspection of plant or property (to supplement the provision in section 28(7)). For example, the Secretary of State may require a person carrying out functions under the capacity market to comply with requirements regarding a particular format, such as to report on its activities, or provide advice. In relation to restrictions on the use of generation plant and participation in a capacity auction, the Secretary of State could, for example, prevent any part of a generating plant to which a capacity agreement does not apply to be used in a way that undermined the efficient operation of the capacity market.

***Section 33: Electricity capacity regulations: information and advice***

153. This section enables the Secretary of State to make provision in electricity capacity regulations for the provision and publication of information including: to require the Authority and the national system operator, or any other person specified in the regulations to provide information or advice; for the Authority and the national system operator to require the provision of information for a purpose specified in the regulations; to require capacity providers and electricity suppliers to share information with one another and with any person named in the regulations; for the publication of information or advice; for the classification and protection of commercial or sensitive information; and for the enforcement of these requirements to provide, publish or protect information or advice.
154. These provisions mean, for example in relation to *subsection (2)(b)*, that the national system operator could require the provision of any information specified in the regulations regarding the operation of the Capacity Market necessary to enable it to administer it, and to report to the Secretary of State on this. In addition, the Secretary of State could for instance, by *subsection (2)(d)*, provide for a body such as the national system operator or an expert group to publish information regarding the operation of the Capacity Market in order to support transparency and accountability of the participants and the administration. Some information, for example relating to forecasts of available capacity some years ahead, may be based upon commercially sensitive or confidential information. *Subsection (2)(e)* enables regulations to include provision about the protection of any such information.

***Section 34: Power to make capacity market rules***

155. This section confers power on the Secretary of State to make capacity market rules, which may contain any provision that may be made by electricity capacity regulations except for the matters referred to in *subsection (2)*. The matters which may not be included in capacity market rules include, in particular, provision about the circumstances in which, and the amount of capacity for which, a capacity auction is to be held, and provision about the calculation and settlement of payments.

156. By virtue of *subsection (3)*, electricity capacity regulations may confer power to make capacity market rules (which includes power to amend, add to or revoke such rules) on the Authority. Thus, the power in this section enables the capacity market to be implemented partly by means of an instrument which the Authority may be given power to add to or amend in future.
157. If electricity capacity regulations give the Authority power to make capacity market rules, *subsection (4)* provides that the regulations must include a condition requiring the Authority to consult before exercising the power.
158. *Subsection (5)* requires such regulations to secure that the Authority must obtain the Secretary of State's consent on each occasion that it seeks to make capacity market rules which confer functions on itself.
159. Supplementary provisions about capacity market rules are contained in sections 41 and 42.

### ***Section 35: Provision about electricity demand reduction***

160. *Subsection (1)* applies this section when electricity capacity regulations made under the power in section 27 relate to the provision of capacity which is created by reducing demand for electricity. Where this is the case, *subsections (2) and (3)* of this section apply.
161. *Subsection (2)* enables the Secretary of State to confer functions on a person or body for the purposes of, for example, administering an electricity demand reduction regime. In relation to the capacity market, section 31 allows the Secretary of State to confer functions on the national system operator (or the Authority). Where provision is made in electricity capacity regulations relating to reducing demand by reducing electricity consumption, it may not be appropriate to confer functions on the national system operator; another person or body may be identified and regarded to be better placed to, for example, administer the electricity demand reduction regime. To cater for this possibility *subsection (2)* enables the Secretary of State to confer functions on a person or body for this purpose and makes clear that the person or body appointed does not have to be the national system operator.
162. *Subsection (3)* ensures that where the power in *subsection (2)* is exercised the references to the national system operator in the provisions listed in *paragraphs (a) to (e)* are construed as references to the person or body appointed under *subsection (2)*. The effect of this provision is to ensure that the powers which might be provided to the national system operator are equally applicable to a person or body appointed under *subsection (2)* for an electricity demand reduction regime.

### ***Section 36: Enforcement and dispute resolution***

163. This section enables the Secretary of State to make provision in electricity capacity regulations and capacity market rules about enforcement and the resolution of disputes, including conferring functions on any public body or any other person.
164. *Subsection (1)* enables electricity capacity regulations to include provision about enforcement of obligations contained either in the regulations or in capacity market rules, while *subsection (2)* only permits capacity market rules to make provision about the enforcement of obligations contained within the rules.
165. *Subsection (4)* clarifies that such provision can include powers to impose financial penalties, provision for requirements imposed by the regulations or rules to be enforceable by the Authority using the enforcement regime set out in the Electricity Act 1989, for reference to arbitration and for appeals.

***Section 37: Licence modifications for the purpose of the capacity market***

166. This section enables the Secretary of State to make licence modifications and to amend electricity industry codes (which are documents maintained under licences), for the purposes of a Capacity Market. Industry codes (such as the Balancing and Settlement Code, made under the standard conditions of the electricity transmission licence) generally contain provisions relating to the functioning of the electricity industry and electricity markets. They also ordinarily contain provision about the procedure for their modification, usually involving the participation of the parties to the code and the Authority.
167. *Subsection (1)* allows the Secretary of State to amend the conditions of generation, transmission, distribution, supply and interconnection licences, electricity industry codes and agreements that give effect to industry codes.
168. *Subsection (2)* allows the Secretary of State to provide for a new document to be required to be prepared and maintained in accordance with the conditions of a licence. This would enable the Secretary of State to create a new industry code rather than modifying an existing one, for example to set out the arrangements governing the settlement of payments relating to capacity agreements. This subsection also enables a licence or code modification to confer functions on the national system operator.
169. *Subsection (3)* enables provisions included in a licence or industry code by a modification made under this section to include any provision of a kind that can be made in electricity capacity regulations, to make different provision for different cases, and confirms that provision need not relate to the activities that the licence authorises. For example modifications to a code may make different provision for different types of capacity (such as electricity generation in contrast to demand side response technologies) or provide for different capacity agreements to apply for different lengths of time.
170. *Subsections (4) and (5)* require the Secretary of State to consult licence holders, the Authority and any other person he or she considers appropriate before making modifications and confirms that consultation that occurs before the passing of the Act will satisfy this requirement.
171. *Section 64* makes further provision about licence modifications.

***Section 38: Amendment of enactments***

172. This section enables the Secretary of State to: amend or repeal section 47ZA of the Electricity Act 1989 regarding the annual report by the Authority on security of electricity supply; amend section 172 of the Energy Act 2004 regarding the annual report on security of energy supplies; amend section 25 of, and Schedule 6A to, the Electricity Act 1989 regarding enforcement of obligations of regulated persons (i.e. to supplement section 36)); and to make consequential amendments to any other enactment as the Secretary of State considers appropriate as a consequence of provision made under this Chapter, including to repeal or revoke such enactments.

***Section 39: Principal objective and general duties***

173. This section provides that sections 3A to 3D of the Electricity Act 1989, which set out the principal objective and general duties of the Secretary of State and the Authority, apply to the functions of the Authority under or by virtue of this Chapter.

***Section 40: Regulations under Chapter 3***

174. This section sets out how the Secretary of State can use the powers to make regulations under this Chapter and the process that must be followed.

175. *Subsection (1)* enables the Secretary of State to make different provisions in regulations for different cases or circumstances. For example, this power might be used to apply different eligibility criteria to capacity provided using different technologies. It also enables the Secretary of State to make regulations including provisions of an incidental, supplementary, consequential or transitional nature.
176. *Subsections (2) and (3)* require that the Secretary of State must consult the Authority, any person who is a holder of a licence to supply electricity under section 6(1)(d) of the Electricity Act 1989 and other persons that he or she considers it appropriate to consult before making any regulations under this Chapter and confirms that this requirement can be satisfied by consultation before the passing of the Act.
177. *Subsections (4) to (7)* provide that regulations must be made by statutory instrument and that, subject to two exceptions, any regulations made under Chapter 3 must be laid in draft before, and approved by affirmative resolution of, each House of Parliament.. Exceptions are made for electricity capacity regulations which only make provision about information and advice (other than the first regulations making such provision), and regulations under section 38 which do not amend primary legislation; these are subject to negative resolution.
178. *Subsection (8)* sets out that the regulations relating to the Capacity Market should not be treated as a hybrid instrument.

#### ***Section 41: Capacity market rules: procedure***

179. This section describes the procedures which must be followed in making capacity market rules. *Subsections (1) to (6)* specify that the first set of rules must be laid in draft before both Houses of Parliament for 40 days, and is subject to the negative procedure. *Subsection (9)* specifies that subsequent capacity market rules or amendments must be laid before Parliament and published as soon as is reasonably practicable after they are made.
180. *Subsection (7)* specifies that the Secretary of State must consult certain persons prior to making capacity market rules: the Authority; any licence holder under section 6(1)(d) of the Electricity Act 1989; any capacity provider; and any other person the Secretary of State considers it appropriate to consult. *Subsection (8)* allows consultation undertaken before or after the passing of the Energy Act 2013, to count towards the duty in *subsection (7)* when making capacity market rules.

#### ***Section 42: Capacity market rules: further provision***

181. This section confers powers for capacity market rules to make the additional changes required to enable them to function. In particular *subsection (1)* allows for: incidental, supplementary and consequential provision; transitory or transitional provision or savings' provision for different cases, circumstances or purposes; and to make provision subject to exceptions.
182. *Subsections (2) and (3)* have the effect that, if electricity capacity regulations give the Authority power to make capacity market rules, that includes power to amend, add to or remove capacity market rules made by the Secretary of State, subject to any provision made by the regulations.

#### ***Section 43: Pilot scheme for electricity demand reduction***

183. *Subsection (1)* of this section enables the Secretary of State to spend money on an electricity demand reduction pilot programme. Before proposing a particular design for an electricity demand reduction regime, the Secretary of State may wish to explore particular design options by running a pilot programme to test different options. This spending power enables the Secretary of State to spend money for these purposes.



184. *Subsections (2) to (4)* of this section add a statutory reporting requirement for any pilot schemes. *Subsection (2)* sets out a duty to review the operation and effectiveness of any pilot scheme, while *subsection (3)* requires the results of that review to be reported to Parliament. This can be done through a written report laid in both Houses, or, if the Secretary of State thinks it should be done orally, by making a statement. *Subsection (4)* specifies that this should be done as soon as reasonably practicable after the conclusion of any pilot.

#### **Chapter 4: Investment contracts**

##### **Section 44: Investment contracts**

185. In keeping with fact that investment contracts are intended to be entered into during a relatively short period of time and are therefore a transitional measure before the enduring regime is fully implemented, the detailed provisions relating to them are contained in Schedule 2 to the Act. This section gives effect to this Schedule.

##### **Schedule 2, Part 1**

###### **Paragraph 1: Meaning of “investment contract”**

186. This paragraph defines what an “investment contract” must be for the purposes of this Schedule. It does this by laying down, for example, requirements about who the parties are to be to such contracts, about the content of contracts, and requirements about being laid before Parliament. The restrictions here are important because Parts 2 to 4 of the Schedule contain a number of regulation-making powers that may be exercised only in relation to contracts that meet the defining characteristics of “investment contracts”, and Part 5 of the Schedule provides for the Secretary of State to incur expenditure in connection with “investment contracts”.
187. Specifically, in terms of their contents and nature, an investment contract is a contract with an electricity generator (as defined in *sub-paragraph (3)*) which:
- is entered into by the Secretary of State before the 31<sup>st</sup> December 2015 or if earlier, the date on which regulations are first made under section 10(3) defining an “eligible generator”. An “eligible generator” is the type of person who may benefit from a CFD under the regulations relating to the enduring regime;
  - has been entered into with the consent of the (Northern Ireland) Department of Enterprise, Trade and Investment if it relates to an electricity generating station in Northern Ireland (which is defined to include territorial waters – see *sub-paragraph (3)*, as well as *sub-paragraph (1)(b)*);
  - contains an obligation for the parties to make payments to each other based on the difference between a strike price and a reference price in relation to electricity generated (see *sub-paragraph (1)(c)* and, for a definition of these prices, *sub-paragraph (3)*). Where the investment contract is entered into before the coming into force of Schedule 2, this payment obligation must be expressed to be conditional on Schedule 2 being in force (see *sub-paragraph (2)*).
188. It is worth noting here that an electricity generator is defined in *sub-paragraph (3)* in a way to cover not simply someone who is directly involved in the generation of electricity, but also and more broadly speaking (for example) a person intending, at the time the contract is entered in to, to establish, or participate in the operation of a new or altered electricity generating station, and any person who has an interest in a company consisting of these aforementioned persons. Under Schedule 1 to the Interpretation Act 1978, “person” is defined to include persons corporate, such as companies. If an investment contract is entered into with more than one person, the payment obligation referred to in *sub-paragraph (1)(c)* must be an obligation on a party

that is an electricity generator as defined in *sub-paragraph (3)* and the Secretary of State (see *sub-paragraph (4)*).

189. A contract is only an “investment contract” if it has been laid before Parliament, accompanied by a statement meeting the requirements in *sub-paragraph (6)* (see *sub-paragraphs (1)(d)* and *(5)(a)*). However, it is not necessarily the case that the whole contract must have been laid before Parliament in order for it to constitute “an investment contract”. *Sub-paragraph (5)(b)* means that certain confidential or commercially sensitive information which is contained in the contract may be omitted from it when it is laid before Parliament (see also *paragraph 3* of the Schedule for the definition of “confidential information”).
190. The statement that must be laid in Parliament together with the contract needs to cover various matters, to provide a measure of transparency about the decision-making process. For example, the statement will need to specify that the Secretary of State considers that payments which would be made under the investment contract which is being laid before Parliament would encourage low carbon electricity generation and that without the contract there is a significant risk of this electricity generation being delayed, or of it not occurring at all. Low carbon electricity generation is defined in *sub-paragraph (7)* to mean electricity generation which in the opinion of the Secretary of State will contribute to a reduction in emissions of greenhouse gases, as defined in section 92(1) of the Climate Change Act 2008. “Greenhouse gases” includes, for example, carbon dioxide and methane.
191. In addition, the Secretary of State must summarise in any statement the regard he or she has had in deciding to enter into a contract to the matters set out in section 5(2) of the Act (see *sub-paragraph (6)(c)*) – namely, the likely costs to consumers of ensuring security of supply to consumers in the United Kingdom, certain statutory targets relating to greenhouse gas emissions contained in the Climate Change Act 2008 and the target relating to the use of renewable energy set out in Article 3(1) and Annex 1 to “the renewable directives” (see the definition in section 5(3)).
192. Finally (though publication here is not a defining characteristic of an investment contract), the Secretary of State is obliged to publish any investment contracts in the form in which they have been laid before Parliament (see *sub-paragraph (8)*).

### ***Paragraph 2: Varied investment contract***

193. Since investment contracts are contracts, they may be varied by agreement of the parties to them (though regulations under *paragraphs 14(2)* and *(3)* may impose restrictions on a counterparty to agree variations). The effect of the paragraph here is to ensure that if an investment contract is amended by the parties, and the amendment will (in the Secretary of State’s opinion) result in a material increase in the likely costs to electricity consumers, the amended contract must be laid before Parliament in order to constitute an “investment contract” for the purposes of Schedule 2. In addition, when a varied contract is laid before Parliament, it must also be accompanied by a statement as to why the Secretary of State considers the amendment is appropriate, having regard to the likely costs to such consumers.
194. *Sub-paragraph (4)* should be noted because it means that where an investment contract is amended in accordance with its terms, there is no need to lay the amended contract before Parliament. For example, if the strike price were to be increased in accordance with a procedure set out in the contract following a change of law, then there would be no need to follow the procedures required under this paragraph.
195. As with the case of an original investment contract, an amended contract must be published (see *sub-paragraph (3)*), once confidential information has been redacted from it (as well as in the case of when an amended contract is laid before Parliament – see *paragraph 2(2)(b)* and *(3)*).

196. The purpose of the provision here is to ensure that Parliament is informed of any changes outside the terms of an investment contract that are likely to adversely impact on consumers.

### ***Paragraph 3: Confidential information***

197. This paragraph defines the “confidential information” which may be removed from an investment contract or varied investment contract before it is laid before Parliament and published in accordance with [paragraph 1](#) or [2](#).
198. “Confidential information” is defined by reference to the terms of an investment contract. Where an investment contract contains a term that information in the contract should not be disclosed, that information is to be excluded from publication provided that in agreeing this term against disclosure the Secretary of State considered that the information in question either constituted a trade secret, or that the disclosure of the information would be likely to prejudice the commercial interests of any person or constitute an actionable breach of confidence. However, it is not possible (given [paragraph 3\(3\)\(a\)](#)) for the investment contract to cover non-disclosure of the strike price or reference price.
199. In effect what this paragraph means, in conjunction with [paragraph 1\(5\)\(b\)](#) is that, where it comes to laying an investment contract before Parliament, any confidential information (as covered by the contract) must be excluded from publication.
200. It is anticipated that the vast majority of information within an investment contract will be included in the contract that is laid in Parliament and published. However, it is possible that some investment contracts may incorporate information that is commercially sensitive, such as detailed financial information belonging to the electricity generator, the disclosure of which could prejudice their commercial interests. This paragraph therefore allows for such information to be excluded from contracts that are laid in Parliament or published.

### ***Paragraph 4: Interpretation for the purposes of this Schedule***

201. This paragraph sets out how certain terms are to be interpreted in this Schedule. For example, it states that “CFD” and “CFD counterparty” should be construed in accordance with provisions in Chapter 2 of Part 2 of the Act (sections 6(2) and 7(2) respectively), and that “electricity supplier” means a person who is a holder of a licence to supply electricity in either Great Britain or Northern Ireland. Definitions for other terms used in the Schedule (and elsewhere in the Act) are to be found in section 151.
202. The paragraph also specifies that references to a CFD counterparty in the Schedule (apart from references in [paragraphs 9\(1\)\(c\)](#), [9\(1\)\(d\)](#), and [16](#)) only apply when the CFD counterparty is acting as a counterparty in relation to an investment contract – in other words, where any property, rights or liabilities under a contract have been transferred to the CFD counterparty by a scheme under [paragraph 16](#).

### ***Paragraph 5: Investment contract counterparty***

203. This paragraph sets out a power allowing the Secretary of State to designate (by order) a registered company or a public authority, with their consent, to act as the counterparty for an investment contract (an “investment contract counterparty”). Whilst it is expected that the counterparty will be owned by Government, any designated investment contract counterparty would have access to the same rights (such as to the supplier obligation) and be bound by the same duties under the legislation, regardless of whether it was a company and / or public authority, or whom it was owned by.
204. The property, rights and liabilities under an investment contract entered into by the Secretary of State can be transferred to a person designated as an investment contract counterparty through a scheme under [paragraph 16](#).

205. The designation of a company as an investment contract counterparty can be revoked by the Secretary of State by order, or if the investment contract counterparty elects to withdraw its consent to being designated by giving 3 month's notice. *Sub-paragraph (6)* provides that, as soon as reasonably practicable after a designation ceases to have effect, the Secretary of State must make a transfer scheme under *paragraph 16* to transfer the rights and liabilities of any investment contracts to which the person was a party to another counterparty. Additionally, under *sub-paragraph (8)* regulations made under *paragraph 6* may specify a period of time for which a person who has ceased to be an investment contract counterparty must continue to be treated as a counterparty for the purpose of regulations under this Schedule. The underlying purpose in the case of *sub-paragraphs (6) and (8)* is to have provision in place to minimise any disruption to obligations under investment contracts, including payments, in the event of a designation of an investment contract counterparty being revoked.
206. As explained in the 'Summary and background' section of the Explanatory Notes to Chapter 4, there will be a duty to transfer investment contracts to a CFD counterparty once one has been designated and certain other conditions have been met. However, in the event that a CFD counterparty is not designated, this paragraph enables another company or public authority to be designated to act as a counterparty for investment contracts.

### ***Schedule 2, Part 2***

207. *Part 2* principally provides the Secretary of State with regulation-making powers in connection with investment contracts. These powers are very similar to those in Chapter 2 relating to contracts for difference. A general regulation-making power is provided by *paragraph 6*, with that power being further particularised in other paragraphs in *Part 2* and in *paragraph 14(3) and (4) and 16(2)* (as well as *paragraph 5(8)* and in the definition of "electricity supplier" in *paragraph 4*). The requirements about who must be consulted before regulations are made are set out in *paragraph 13*. Regulations are to be made either under the affirmative resolution procedure if they are the first regulations which make provision falling within *paragraph 10 or 11*, or any other regulations which make provision falling within other paragraphs of Parts 1 to 3 of Schedule 2; see *sub-paragraph (5)*), or the negative resolution procedure for all other regulations (see *sub-paragraph (6)*). *Paragraph 6(7)* provides that regulations relating to investment contracts should not be treated as a hybrid instrument.

### ***Paragraph 7 – Supplier obligation***

208. *Paragraph 7* expressly provides regulation-making powers to impose financial obligations on licensed electricity suppliers – supplier obligation(s). Under *sub-paragraph (1)*, regulations may impose obligations on licensed electricity suppliers in GB and Northern Ireland (see the definition of "electricity supplier" in *paragraph 4(1)*) to make payments to the Secretary of State to meet obligations under investment contracts. *Sub-paragraph (2)* requires that regulations impose obligations on licensed suppliers to make payments to an investment contract counterparty, or a CFD counterparty (see *paragraph 4(1)* for definitions of these counterparties – hereafter referred to as "counterparties") to meet obligations under investment contracts. Licensed suppliers may also be obliged to make payments for certain other purposes under regulations – for example, to cover costs associated with administering investment contracts, and to enable the Secretary of State or a counterparty to hold sums in reserve (see *sub-paragraph (3)*), or to mutualise costs across (other) licensed suppliers where another becomes insolvent or defaults. *Sub-paragraph (6)* requires that any regulations under *sub-paragraphs (1) or (2)* must include a duty in relation to the collection of payments.
209. Other regulation-making powers expressly include imposing requirements on suppliers to provide collateral to the Secretary of State or to a counterparty (*sub-paragraph (5)*). They also cover powers for regulations to set out how the Secretary of State or a

counterparty is to calculate or determine the amounts owed under regulations or the financial collateral to be provided by electricity suppliers (see *sub-paragraphs (7)(b)* and *(8)*). For example, regulations might provide powers to the counterparty to require collateral from suppliers according to such amounts as the counterparty calculates, but to require the counterparty to make its calculation of the amount of collateral required by reference to the size of a supplier or the amount of electricity it provides to certain consumers.

210. *Sub-paragraphs (7)(c)* and *(d)* expressly provide regulation-making powers to make provision about the issuing and enforcement of notices (issued by the Secretary of State or a counterparty) which require the payment of amounts owed under regulations here or the provision of collateral. *Sub-paragraph (9)* covers regulations making connected provision, for example, on dispute resolution about notices and the payment of interest for late payment. Note that the powers in *paragraph 12* of this Schedule would allow regulations to make provision for the requirements of notices here to be enforced by the Authority or the Northern Ireland Authority for Utility Regulations as if the requirements were relevant requirements on a regulated person. See the text below for explanation of *paragraph 12*.
211. *Sub-paragraph (10)* clarifies that any sum which the supplier is required to pay the Secretary of State, the investment contract counterparty or the CFD counterparty by virtue of the supplier obligation regulations, and which is not paid when it is due under the regulations, is recoverable as a civil debt.

#### ***Paragraph 8: Payments to electricity suppliers***

212. This paragraph expressly enables regulations to require the Secretary of State, an investment contract counterparty, or a CFD counterparty to make payments to licensed electricity suppliers. The underlying purpose of the power is to ensure that regulations can require that payments are made to licensed suppliers (where for example the reference price is higher than the strike price) and in circumstances where regulations are made imposing the supplier obligation under *paragraphs 7(1)* or *7(2)*.

#### ***Paragraph 9: Application of sums***

213. *Paragraph 9* is concerned with providing regulation-making powers to cover two broad areas. First, to ensure that regulations may make provision about the apportioning of money between generators by the Secretary of State or a counterparty where the amount collected from licensed suppliers is insufficient to collectively meet the liabilities under investment contracts or CFDs in full. In making these regulations, the Secretary of State must have regard to the principle that sums should be apportioned in proportion to the amounts which are owed, i.e. that they are pro-rated.
214. Secondly, *sub-paragraphs (4)* and *(5)* are concerned about conferring regulation-making powers to control how monies received by a counterparty or by the Secretary of State are used – specifically, whether or not they need to be paid into the Consolidated Fund.

#### ***Paragraph 10: Information and advice***

215. This paragraph allows for regulations to be made imposing requirements about providing information or publishing it, as well as about how information is to be protected (see *sub-paragraphs (1)* and *(2)(f)*). The paragraph is intended, in part, to ensure that provision can be made in regulations so that there is a sufficient flow of information and advice for the purposes of administering and managing investment contracts. Therefore, for example, the regulations can require information to be provided to the Secretary of State or a counterparty from suppliers or generators (see *paragraph 10(2)(c)* and *(e)*). In addition the powers will allow provision to be made in regulations to permit the Secretary of State and the regulators in Great Britain and



Northern Ireland to gather information together about investment contracts, in order to monitor their use and inform their wider decision-making.

### ***Paragraph 11: Functions of the Authority***

216. This paragraph provides an express power for regulations to confer functions, for two purposes, on the Authority (see the definition of “Authority” in section 151). The Authority is the regulator for the electricity markets in Great Britain. However, as a statutory body, it only has power to do those things which legislation confers a power on it to do.
217. The two purposes are to provide advice to, and to make determinations for, the parties to investment contracts. Therefore, for example, regulations could empower the Authority to monitor the performance of obligations under an investment contract relating to biomass sustainability (such as the type or mix of fuels used in an electricity generating station) and to determine for the parties whether such obligations have been met.

### ***Paragraph 12: Enforcement***

218. This paragraph provides an express regulation-making power in relation to the enforcement of obligations in regulations made under Schedule 2. Specifically, regulations may permit requirements imposed on suppliers to be enforced by the Authority in GB, or the Northern Ireland Authority for Utility Regulations in Northern Ireland, as if they are relevant requirements imposed on a regulated person.
219. What this means, in effect, is that regulations may treat a breach of a requirement imposed under them as akin to a breach of a licence condition in relation to certain enforcement powers. For example, sections 25 to 27A of the Electricity Act 1989 permit the Authority to make orders to secure compliance with licence conditions, and/or to impose financial penalties for their breach. Regulations could apply these enforcement powers in relation to breaches of requirements imposed under them as if they were breaches of licence conditions.

### ***Paragraph 13: Consultation***

220. *Paragraph 13* imposes requirements on the Secretary of State about who he or she must consult before making regulations under Schedule 2 – with *sub-paragraph (8)* expressly providing that any required consultation may take place before or after enactment of the Act.
221. As a broad rule, the Secretary of State is required to consult those persons who will be affected by specific regulations, as well as the devolved administrations in Northern Ireland, Scotland and Wales. For example, electricity suppliers are required to be consulted on regulations under *paragraphs 7, 8, 9 or 14(3)*.

### ***Schedule 2, Part 3***

#### ***Paragraph 14: Duties and liabilities of an investment contract counterparty and a CFD counterparty***

222. This paragraph allows for regulations to tightly define and limit the scope of the behaviour of an investment contract counterparty, or a CFD counterparty which is acting as a counterparty in relation to an investment contract.
223. The regulation-making power is designed to ensure that controls can be imposed on counterparties to ensure that suppliers are properly protected from potential for increased costs due to variation of contracts, whilst still enabling decisions to be made by the Secretary of State to permit variation where it is appropriate to do so. This paragraph only covers regulation of the behaviour of the counterparty and does not

enable the Secretary of State, through regulations, to vary any investment contract without the consent of the generator in question.

224. *Sub-paragraph (2)* places a duty on an investment contract counterparty or CFD counterparty to exercise its functions to ensure that it can meet its liabilities under an investment contract. Those functions are principally those conferred under or by virtue of *paragraph 7* (supplier obligation) in relation to the ability of the CFD counterparty or investment contract counterparty to recover sums from licenced electricity suppliers. “Liabilities” in this context includes all liabilities under an investment contract. For these purposes, liabilities will exist in respect of any sums that are owed at a particular time by the counterparty under the investment contract, irrespective of whether they have yet become payable in accordance with any payment provisions it contains.
225. *Sub-paragraph (3)(c)* enables regulations to make provision about the making of directions to an investment contract counterparty or CFD counterparty. This will enable specific directions to be given in relation to particular contracts or matters (such as where a generator has proposed a variation to the contract and the Secretary of State wishes to require the counterparty to agree to it).
226. *Sub-paragraph (5)* places a duty on the Secretary of State. The regulations that he or she makes must include such provision as he or she considers necessary to ensure that the investment contract counterparty or CFD counterparty can meet its liabilities under investment contracts. As set out in relation to *sub-paragraph (2)* above the reference to liabilities means all sums which are owed under an investment contract.

#### ***Paragraph 15: Shadow directors***

227. This paragraph makes it clear that, as a result of exercising any powers conferred by or under Schedule 2 (such as those given by regulations under *paragraph 14(3)*) over an investment contract counterparty or CFD counterparty, the Secretary of State is not to be regarded as, for example, a director or shadow director of these bodies or an agent of them or their principal.
228. The purpose of this provision is to limit the potential liabilities and duties that could otherwise accrue to the Secretary of State (such as under the Companies Acts or the Insolvency Act 1986) were he or she to be treated, for example, as shadow director of these bodies. This is considered to be appropriate since the powers the Secretary of State will be exercising under the regulations will be exercisable in the public interest.

#### ***Schedule 2: Part 4***

##### ***Paragraphs 16-18: Transfers***

229. The above paragraphs provide powers to the Secretary of State, by transfer scheme, to transfer the property, rights and liabilities under an investment contract from the Secretary of State to an investment contract counterparty or a CFD counterparty, and from one counterparty to another.
230. *Paragraph 16* sets out the broad power to make one or more transfer schemes and contains provision on how schemes are to take effect. This paragraph also introduces a duty to make a transfer scheme to transfer investment contracts from the Secretary of State or an investment contract counterparty to the CfD counterparty once three conditions are satisfied: that the CfD counterparty has been designated, the investment contract provisions in the Act have expired (31 December 2015 or earlier if an eligible generator has been defined under section 10(3)), and supplier obligation regulations under section 9 are in place to collect payments from suppliers. The duty does not apply to the extent that the Secretary of State considers it is appropriate in all circumstances to dis-apply it.

231. *Paragraph 17* particularises the powers to make transfer schemes – for example, a scheme could make provision that in the case of any legal proceedings concerning an investment contract that is transferred, that the new counterparty body is to be substituted as a party (see *paragraph 17(1)(c)*). *Paragraph 18* gives the Secretary of State the power to pay compensation to persons whose interests are adversely affected by a transfer scheme.
232. Supplementary provision is made in section 153 which relates to the powers to make schemes here. For example, powers are conferred to modify schemes.
233. The powers ensure that over the lifetime of an investment contract there is a mechanism in place to ensure that if an existing counterparty ceases to be suitable or willing to act as such, the investment contract can be transferred to another person designated as a counterparty. The Secretary of State is under a duty, by virtue of *paragraph 5(6)* and section 7, to ensure that where a counterparty ceases to be a counterparty, the property, rights and liabilities under any investment contracts are transferred to a new counterparty as soon as reasonably practicable.

### **Schedule 3: Part 5**

#### **Paragraph 19: Licence modifications**

234. *Paragraph 19* provides the Secretary of State with powers to modify generation, transmission and distribution licences, the standard conditions of such licences and documents maintained in accordance with conditions of such licences (such as industry codes). There are two purposes for which the powers are exercisable (see *sub-paragraph (2)*) – which relate to the provision of services or enforcement. For example, the powers may be used to make amendments to the Balancing and Settlement Code (BSC) (which is a document falling within *sub-paragraph (1)(c)*) to enable the BSC company to provide settlement services to the Secretary of State, an investment contract counterparty or a CFD counterparty. Or new licence conditions could be imposed to assist in the enforcement of obligations under investment contracts where contractual remedies thought insufficient to provide protection against abuse.
235. The powers to make licence modification here are supplemented by section 64, which also contains requirements of the procedures that need to be followed in connection with modifications.

#### **Paragraph 20: Expenditure**

236. *Paragraph 20* provides Parliamentary authorisation for certain items of expenditure by the Secretary of State in connection with investments contracts. The expenditure covered includes expenditure incurred for the purposes of obtaining advice and assistance in relation to investment contracts (for example, to engage technical advisers to assess a generator’s construction costs). The paragraph would also authorise, for example, financial assistance given to an investment contract counterparty to assist with set-up costs or costs which the Secretary of State might incur in establishing one.

### **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.

## ***Chapter 6: Access to markets etc***

### ***Section 49: Power to modify licence conditions etc: market participation and liquidity***

257. This section enables the Secretary of State to modify electricity generation and supply licences and to amend electricity industry codes to facilitate participation and promote liquidity in the wholesale electricity market.
258. *Subsection (1)* allows the Secretary of State to modify the conditions of particular electricity generation and supply licences and the standard conditions contained in such licences and to amend electricity industry codes (such as the Balancing and Settlement Code), which are documents maintained in accordance with the conditions of such licences, and agreements that give effect to industry codes.
259. *Subsection (2)* sets out the purposes for which the Secretary of State may use the modification power, these being to:
- facilitate participation in the wholesale electricity market in Great Britain, both by licence holders and others (such as exempt suppliers and generators); and
  - promote liquidity in that market.
260. *Subsection (3)* sets out a non-exhaustive list of the types of licence modification that the Secretary of State may choose to make when exercising the powers in *subsection (1)*. These include:
- imposing obligations on electricity generators or suppliers to either sell or purchase electricity, including obligations to sell or purchase electricity on certain terms or in particular circumstances (such as a requirement to sell a proportion of electricity on a particular exchange or to sell particular products at particular times);
  - restrictions on generators and suppliers selling or purchasing electricity to or from their group undertakings; and
  - imposing obligations to disclose or publish information (such as information about transactions in the wholesale electricity market).
261. *Subsection (4)* provides additional clarification on the types of transactions that may be subject to the restrictions referred to in *subsection (3)(b)*.

### ***Section 50: Power to modify licence conditions etc to facilitate investment in electricity generation***

262. This section enables the Secretary of State to modify the conditions of electricity supply licences and related industry codes for the purpose of facilitating investment in electricity generation by means of a Power Purchase Agreement (PPA) scheme.
263. *Subsection (1)* allows the Secretary of State to modify the conditions of particular supply licences and the standard conditions incorporated in such licences and also to

amend electricity industry codes, being documents maintained in accordance with the conditions of such supply licences, and agreements that give effect to industry codes.

264. *Subsection (2)* sets out the purpose for which the Secretary of State may use the modification power. This is limited to facilitating investment in electricity generation by means of a power purchase agreement scheme.
265. *Subsection (3)* explains that
- a PPA scheme is a scheme established by supply licence conditions and regulations for promoting the availability to electricity generators of power purchase agreements;
  - a PPA is an arrangement under which a licensed supplier agrees to purchase electricity generated by an electricity generator at a discount to a prevailing market price.
266. *Subsection (4)* sets out the nature of provisions that may be made in licence or code modifications under this section, which include:
- the eligibility of an electricity generator to enter into a PPA under the scheme;
  - the terms of any PPA to be entered into under the scheme, including provision for determining the price at which electricity is to be purchased under the agreement and the duration of any such agreement;
  - the circumstances in which a licensed supplier is or may be required or permitted to enter, or offer to enter, into a PPA under the scheme;
  - the provision of information in connection with the scheme.
267. *Subsections (5) and (6)* set out further details about the process for determining which licensed supplier or suppliers is or are required or permitted to enter, or offer to enter, into a PPA agreement with an electricity generator in any particular case and for this determination to be made by one or more of the Secretary of State, the Authority, and the electricity generator or by auction or other competitive process.
268. *Subsection (7)* sets out that a licenced supplier under section 50 and 51 means the holder of a licence under Section 6(1)(d) of the Electricity Act 1989.

### ***Section 51: Power purchase agreement scheme: regulations***

269. This section enables the Secretary of State to make regulations in connection with any modifications made under section 50 for or in connection with a PPA scheme.
270. *Subsection (2)* sets out that such regulations may include provision for:
- apportioning amongst licensed suppliers the costs or benefits of any licensed supplier in connection with the scheme;
  - conferring functions on the Secretary of State or the Authority;
  - the delegation of functions conferred on the Secretary of State or the Authority by the regulations or by virtue of section 50;
  - obligations imposed by the regulations on licensed suppliers to be enforceable as if they were relevant requirements on a regulated person under section 25 of the Electricity Act 1989;
  - requiring the provision of information in connection with the scheme.
271. *Subsection (3)* explains that provision may be included in regulations for requiring licensed suppliers to pay a levy to the Authority or conferring an entitlement on them to receive a payment from it.

*These notes refer to the Energy Act 2013 (c.32)  
which received Royal Assent on 18 December 2013*

272. *Subsection (4)* sets out that regulations may include provision for the Secretary of State or the Authority to determine what is to be taken into account as a cost or benefit of any licensed supplier in connection with the scheme.
273. *Subsection (5)* enables the Secretary of State to make different provisions in regulations for different cases or circumstances. It also enables the Secretary of State to include in regulations provisions of an incidental, supplementary, consequential or transitional nature.
274. *Subsections (6) and (7)* require that the Secretary of State must consult relevant persons, including licensed suppliers and the Authority, before making any regulations in connection with any modifications made under section 50 and confirms that this requirement can be satisfied by consultation before the passing of the Act.
275. *Subsections (8) and (9)* provide that regulations must be made by statutory instrument and are subject to the negative parliamentary procedure.

### ***Section 52: Power Purchase agreement scheme: disclosure of information***

276. This section extends section 105 of the Utilities Act 2000 to include sections 50 and 51 of the Energy Act 2013 in relation to general restrictions on disclosure of information, by inserting references to these sections into *subsections (1)(a) and (3)(a)* of the Act.

### ***Section 53: Principal objective and general duties: power purchase agreement scheme***

277. This section requires the Secretary of State and the Authority to apply the principal objective and comply with the general duties laid out under sections 3A to 3D of the Electricity Act 1989, when exercising functions so far as they relate to a power purchase agreement scheme.

### ***Section 54: Licence modifications under sections 49 and 50: further provisions***

278. This section sets out additional provisions that apply to both sections 49 and 50 and clarifies how these licence modification powers may be exercised.
279. *Subsection (1)* allows the Secretary of State to provide for a new document to be required to be prepared and maintained in accordance with the conditions of a licence. This would enable the Secretary of State to create a new industry code, for example to set out the detailed arrangements of an auction in which suppliers or generators are obliged, by the conditions of their licences, to participate.
280. *Subsection (2)* requires the Secretary of State to consult affected licensees, the Authority, and other relevant persons, before making modifications under section 49 or 50.
281. See also section 64, which sets out other general provision on licence and code modification powers.

## ***Chapter 7: The renewables obligation: transitional arrangements.***

### ***Section 55: Closure of support under the renewables obligation***

282. *Subsection (1)* inserts new sections 32LA and 32LB to the Electricity Act 1989 to confer a power on the Secretary of State to make a renewables obligation closure order. The closure order will prevent renewables obligation certificates from being issued under any renewables obligation order (whether made by the Secretary of State or by the Scottish Ministers) in respect of electricity generated after a specified date (section 32LA(2)). Different closure dates may be specified for different cases or circumstances (section 32LA(3)). The powers in sections 32 to 32M of the Electricity Act 1989 (renewables obligation) will be subject to any provisions contained in a

closure order (section 32LA(7)). The closure order may make provision as to the functions of the Authority in relation to the closure of the renewables obligation and may make transitional provision and savings (section 32LA(8)). *Subsections (2) and (3)* make consequential amendments to sections 32M (interpretation) and section 106 (regulations and orders) of the Electricity Act 1989. Subsection (4) provides the Department for Enterprise, Trade and Investment in Northern Ireland with the power to amend corresponding legislation in relation to the Northern Ireland renewables obligation to take account of the amendments made by *subsection (1)*.

### ***Section 56: Transition to certificate purchase scheme***

283. The section inserts new sections 32N to 32Z2 to the Electricity Act 1989 to enable the Secretary of State to make an order which imposes an obligation on the Authority, the Secretary of State or a CFD counterparty to purchase GB certificates which have been issued to generators in respect of renewable electricity (section 32N). The body on which this certificate purchase obligation is placed is referred to in the sections as the purchasing body of GB certificates (section 32N(2)(a)).
284. With the consent of the Northern Ireland Department for Enterprise, Trade and Investment (DETI), the Secretary of State may also make an order which imposes an obligation on the Northern Ireland Authority for Utility Regulation (the Northern Ireland authority) or a CFD counterparty to purchase NI certificates which have been issued to generators in Northern Ireland in respect of renewable electricity. The body on which this certificate purchase obligation is placed is referred to in the sections as the purchasing body of NI certificates (section 32N(2)(b)).
285. The GB and NI certificates are intended to be issued in place of renewables obligation certificates and to be issued in similar circumstances. The price at which the certificates are to be purchased by the purchasing body will be fixed and different purchase prices may be set for different periods of time (section 32O(2)(a) and (b)). Adjustments to the purchase price may also be made for inflation (section 32O(2)(c)).
286. The order may provide for the manner in which a GB or NI certificate is to be presented for payment and may set deadlines and other conditions that must be met before the purchasing body is required to purchase the certificate (section 32O(2)(e) and (h)). The person presenting the certificate for payment may also be required to provide information in a particular form and within deadlines set by the purchasing body (section 32O(4)). The order may authorise certain fees or charges incurred in making the payment for the certificates to be deducted from the payment for the certificate (section 32O(2)(1)).
287. The new section 32P makes provision for an order to impose a levy charged in respect of supplies of electricity. In Great Britain, the levy would be administered by the Authority, by the Secretary of State or by a CFD counterparty body (section 32P(7)). In Northern Ireland, the levy would be administered by the Northern Ireland authority, DETI or a CFD counterparty body (section 32P(8)).
288. The new section 32Q sets out how the amounts raised by the levy are to be used to meet the cost of purchasing certificates (section 32Q(3)) or paid into the Consolidated Fund or the Consolidated Fund of Northern Ireland in respect of costs incurred by the administrator of the levy, the purchasing body, the Authority and the Northern Ireland authority. The Secretary of State may also direct sums held by the purchasing body to be paid into the relevant Consolidated Fund (section 32Q(9) and (10)).
289. The order may provide for different levy rates for different periods or different cases or circumstances (section 32P(3)) and may make exemptions from the levy (section 32P(4)). The order may impose deadlines for payment of the levy, with interest for late payment (section 32P(6)(e)) and may provide for enforcement measures if the requirements in respect of the levy are not complied with (section 32P(6)(i)).

290. In the case of overpayment or underpayment of the levy, the order may require the amount to be set off against or added to the liability of the person to pay the levy for future periods (section 32P(11)). The order may provide for further payments to be made by electricity suppliers if there is a shortfall in the amounts raised by the levy due to missed or late payments or insolvency (section 32P(12)).
291. The CFD counterparty can be designated as the purchasing body or as the administrator of the levy only with the consent of the CFD counterparty (section 32R(2)). The Secretary of State may make an order revoking the designation at any time and the CFD counterparty may withdraw its consent by giving 3 months notice (section 32R(4)). The Secretary of State may also make an order dealing with the transition upon a change in the identity of the purchasing body or administrator when the designation of the CFD counterparty as the purchasing body or administrator ceases to have effect (section 32R(5) and (6)).
292. A certificate purchase order may provide for the Authority to issue a GB certificate to the operator of a generating station or to such other person specified in the order (section 32S(1)). A GB certificate must certify that it has been issued in respect of electricity generated from renewable sources, by the generating station or stations specified in the certificate, and supplied to customers in the United Kingdom or used in a permitted way (as defined in section 32S(10)). A GB certificate cannot be issued if a renewables obligation order is in force and a renewables obligation certificate could be issued for the electricity (section 32S(3)).
293. A certificate purchase order may provide for the Northern Ireland Authority to issue a NI certificate to the operator of a generating station in Northern Ireland (section 32T(1)). A NI certificate must certify the same matters as a renewables obligation certificate issued under article 52 of the Energy (Northern Ireland) Order 2003 (see article 54 of that order). A NI certificate cannot be issued if a Northern Ireland renewables obligation order is in force and a Northern Ireland renewables obligation certificate could be issued for the same electricity (section 32T(3)).
294. Article 54(10) of the Energy (Northern Ireland) Order 2003 prevents the issue of a Northern Ireland renewables obligation certificate in respect of electricity generated by a generating station situated in the territorial sea. A similar restriction applies to the issue of NI certificates by the Northern Ireland authority, as for the purposes of section 32N to 32Z2, Northern Ireland does not include any part of the territorial sea adjacent to Northern Ireland, unless a certificate purchase order provides otherwise (section 32Z2(5) and (6)).
295. The new sections 32U to 32X and 32Z to 32Z2 mirror many of the provisions in sections 32C to 32E and 32J to 32M of the Electricity Act 1989 to enable equivalent provision to be made under the certificate purchase scheme as may currently be made under the renewables obligation. In particular, this will enable many of the same rules to apply in connection with the issue of GB and NI certificates as currently apply, or as may in the future apply, to the issue of renewables obligation certificates. In some cases, the powers for the certificate purchase scheme differ from the existing powers for the renewables obligation to reflect the different features of the certificate purchase scheme.
296. Section 32U makes supplemental provision relating to the issue of GB or NI certificates. A certificate purchase order may specify cases or circumstances in which certificates cannot be issued or can be issued in respect of a proportion only of the electricity generated (s32U(1)). Only the proportion attributable to renewable sources is to be treated as generated from such sources where the generating station is fuelled partly by renewables sources and partly by fossil fuel (section 32U(4)). A certificate purchase order can specify how that proportion is to be determined and the consequences where more than the specified proportion of fossil fuel is used (section 32U(5)).
297. A certificate purchase order may impose restrictions on the transfer of GB and NI certificates (section 32U(7)). The order can specify circumstances where the



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Authority or Northern Ireland authority may revoke certificates (section 32U(8)). The order may provide for sums to be repaid to the Authority or the Northern Ireland authority if the purchasing body has purchased a GB or NI certificate that should not have been issued, and if it is not possible to refuse the issue of another certificate in its place (section 32U(10)) and provide for enforcement and appeals where repayment is required (section 32U(11)).

298. A certificate purchase order may provide for different numbers of certificates to be issued for electricity generated from different renewable sources or in other different cases or circumstances (section 32V). This is known as “banding provision”. Before making a banding provision, the Secretary of State must have regard to the matters listed in section 32V(4).
299. A certificate purchase order may provide for banding provision made in a renewables obligation order to apply in relation to GB and NI certificates as it applied in relation to renewables obligation certificates (section 32W(3)). The requirement to hold a banding review and the requirement to have regard to the matters listed in section 32V(4) does not apply where the effect of earlier banding provisions is being preserved (section 32W(4)).
300. A certificate purchase order may provide for the number of certificates issued in respect of the generation of electricity by a generating station to be conditional upon the repayment or cancellation of the whole or part of a statutory grant (section 32W(5) to (9)). In the case of repayment of a grant, the repayment must be made to the person who made the grant (section 32W(7)(a)). The order may also require interest to be paid, and may leave the interest rate and period to be determined by a person, such as the person who made the grant (section 32W(7)(b)).
301. A certificate purchase order may provide for the Authority and the Northern Ireland authority to require information which is relevant to whether a GB or NI certificate should be issued (section 32X(1)). The order may also require information to be provided about biomass used to generate electricity (section 32X(3)).
302. Section 32Y places a duty on the Secretary of State, when exercising a number of powers listed for the certificate purchase order, to exercise those powers in the way that the Secretary of State considers will replicate the effect of a provision made by virtue of an equivalent power for the renewables obligation order in England and Wales or in Scotland. The powers to which this duty applies are listed in section 32Y(4) together with the equivalent power for the renewables obligation order.
303. Where a listed power is exercised in relation to Northern Ireland, the power is to be exercised in the way that the Secretary of State considers will replicate the effect of a provision made by virtue of an equivalent power for the Northern Ireland renewables obligation (section 32Y(2)(b)).
304. The duty in section 32Y applies only to the extent that it appears reasonably practicable to exercise the listed power in that way and only to the extent that the duty is not inconsistent with other duties on the Secretary of State (section 32Y(3)).
305. A certificate purchase order may provide for renewables obligation certificates to be treated as if they were GB or NI certificates (section 32Z(2)) and may make different provision for different parts of the United Kingdom or for different localities (section 32Z(3)).
306. The Authority may act on behalf of the Northern Ireland Authority by arrangement (section 32Z(5)). Similar arrangements have been made in respect of the renewables obligation by virtue of section 121 of the Energy Act 2004.
307. Section 32Z2 provides definitions for various terms used in the sections 32N to 32Z2.

## **Chapter 8: Emissions performance standard**

### **Section 57: Duty not to exceed annual carbon dioxide emissions limit**

308. This section places a limit on the amount of carbon dioxide that a “fossil fuel plant” may emit within a year. Those operating a “fossil fuel plant” are placed under a duty not to exceed the emissions limit. The limit is calculated using the formula in *subsection (1)* by reference to an individual plant’s installed generating capacity (of the electricity generating station), a statutory rate of emissions and a load factor of 85%, (expressed in the formula as 7.446, see further below for an explanation for how this is derived).
309. To calculate the limit, a plant’s capacity in Mega Watts (MW) is multiplied by the statutory rate of emissions expressed in g/kWh (grams per kilo watt hour) and 7.446. The figure of 7.446 represents 85% of the total operating hours available in a year (8760) divided by 1000, which provides that the annual limit is expressed in tonnes of carbon dioxide.
310. By virtue of *subsection (2)* the statutory limit is set at 450g/kWh until the start of 2045. This “grandfathering” of the emissions limit under which a new plant is consented provides regulatory certainty for investors about the regime under which their assets will operate, consistent with the time needed to achieve a return on an investment in a new plant.
311. The emissions limit duty is applicable to a “fossil fuel plant” that is built pursuant to a “relevant consent” provided on or after the date that *subsection (1)* comes into force. *Subsection (3)* defines a “fossil fuel plant” whilst “relevant consent” is defined in section *61(1)* as one which is granted under the Planning Act 2008, section 36 of the Electricity Act 1989 or Article 39 of the Electricity (Northern Ireland) Order 1992. This means that the emissions limit duty will only apply to plant at or over 50MW electrical capacity that are given development consent by the Secretary of State (in England and Wales), Scottish Ministers (in Scotland) or the Department of Enterprise, Trade and Investment (in Northern Ireland).
312. “Fossil fuel plant” is defined in *subsections (3) and (4)*. *Subsection (3)* makes clear that a fossil fuel plant includes any associated gasification plant or Carbon Capture and Storage plant and which satisfies the conditions in *subsection (4)*. The conditions in *subsection (4)* are that the plant is constructed pursuant to a “relevant consent”, see previous paragraph, and uses fossil fuels or fuel produced by gasification plant.
313. *Subsection (5)* subjects the emissions limit duty in *subsection (1)* to any regulations which the Secretary of State makes under *subsection (6)*. Under *subsection (6)* the Secretary of State may make regulations regarding interpretation of the emissions limit duty (under *subsection (1)*) and for extending the application of the emissions limit duty or modifying it in respect of the types of case mentioned in Schedule 4.
314. *Paragraph 1* of Schedule 4 allows the Secretary of State, when making regulations under section 57(6)(b), to bring existing fossil fuel plant consented prior to this legislation into the regime where that plant replaces a main boiler or installs an additional main boiler. This sort of provision may be necessary in order to prevent existing fossil fuel plants from being refurbished with replacement boilers, effectively extending a plant’s technical lifetime consistent with that of a new plant, thereby circumventing the emissions limit duty.
315. *Paragraph 2* of Schedule 4 allows the Secretary of State to modify the emissions limit duty such that it does not apply to facilities that generate electricity solely for the purposes of self-supply. *Paragraph 3* allows the Secretary of State to apply the emissions limit with modifications where gasification or CCS plant is “associated” with more than one generating station at a fossil fuel plant. *Paragraph 4* allows the Secretary of State to provide different limits to generation plant which enters, or ends, commercial operation part way through a calendar year.

316. *Subsection (7)* illustrates the type of further provision which the Secretary of State may make in regulations under *subsection (6)(a)*. *Subsection (7)(a)* taken together with Schedule 5 *Paragraph 3* allows the Secretary of State to make provision in respect of “associated gasification plant<sup>1</sup>” for the purpose of ensuring that the emissions limit regime can be suitably applied in circumstances where a generating station uses fuel produced by a gasification plant that is either integral to, or remote from, the generating station, as well as where the gasification plant provides fuel to more than one generating station.
317. *Subsection (7)(c)(ii)* makes provision for application of the emissions limit duty in respect of electricity generating stations that only make incidental use of fossil fuel for safety, start-up or stabilisation purposes (such as biomass plants).
318. Regulations under *subsection (7)* can also include provisions to determine the emissions from fossil fuel plant, to include or exclude emissions by reference to regulations implementing the EU Emissions Trading System (*subsection (7)(g)*); and to exclude emissions associated with the supply of heat to customers from combined heat and power plants (*subsection (8)*).

***Section 58: Introduction of carbon capture and storage: exemption from emissions limit***

319. This section provides that a fossil-fuel plant that is equipped with carbon capture and storage (CCS) will be exempt from the emissions limit duty for a period of 3 years starting from the date when a complete CCS system (capture, transport and storage) is ready for use. The exemption is time-limited and available until the end of 2027.
320. *Paragraph 4* of Schedule 4 allows the Secretary of State, when making regulations under section 57(6)(b) to be apply the exemption with modifications such that it can be applied to only those parts of a fossil fuel plant that are fitted with a complete CCS system.

***Section 59: Suspension etc of emissions limit in exceptional circumstances***

321. *Subsection (2)* provides the Secretary of State with a power to suspend or modify the emissions limit duty on fossil fuel plant located in Great Britain (GB). *Subsection (1)* sets out the circumstances in which the power to suspend or modify the emissions limit duty will arise. It will arise, for example, if the Secretary of State believes there is a risk of a shortfall in electricity supplies and that suspending the emissions limit duty will prevent or reduce a shortfall.
322. *Subsection (3)* defines “electricity shortfall” so that shortfalls in GB and Northern Ireland (NI) can be taken into account to determine whether the power should be exercised. Thus, the Secretary of State may exercise this power where there is a risk to security of electricity supplies in GB or NI. The provisions also enable the Department of Enterprise Trade and Investment (DETI) in Northern Ireland to suspend or modify the emissions limit in respect of fossil fuel plant located in NI (see definition of “appropriate authority” and “relevant plant” in *subsection (12)*).
323. *Subsection (2)* provides for the Secretary of State to direct that the emissions limit duty in respect of a plant in GB be suspended or modified for such period as is specified in that direction. *Subsection (5)* requires the Secretary of State to consult Scottish and Welsh Ministers before giving a direction under *subsection (2)*.
324. A suspension or modification of the emissions limit duty will be effected by way of a direction to the relevant enforcing authorities who will be appointed pursuant to powers in section 60 and Schedule 5.

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<sup>1</sup> gasification plant can extract combustible gases e.g. hydrogen, from fossil fuels, which when burnt do not produce CO<sub>2</sub>.

325. *Subsection (6)* requires the Secretary of State to lay before Parliament a copy of any direction together with a statement of the reasons for making the direction as soon as is practicable after giving a direction. A similar requirement applies to DETI, which is responsible for suspending or modifying the emissions limit in Northern Ireland, see *subsection (8)*.
326. *Subsection (9)* provides that a direction must be made in writing and that a direction may be varied or revoked by a further direction.
327. *Subsection (11)* requires the Secretary of State and DETI to issue, and have regard to, a statement of his or her policy in relation to making directions to suspend or modify the emissions limit duty.

### **Section 60: Monitoring and enforcement**

328. *Subsection (1)* places a duty on the “appropriate national authority” to make arrangements for monitoring compliance with, and enforcement of, the emissions limit duty. The “appropriate national authority” is the Secretary of State in England, Scottish Ministers in Scotland, Welsh Ministers in Wales and the Department of the Environment in Northern Ireland (DoE) (see *subsection (4)*).
329. *Subsection (2)* enables the “appropriate national authority” to make regulations for the purpose of implementing the arrangements which are necessary for the purpose of monitoring and enforcing the emissions limit duty.
330. *Subsection (3)* requires that arrangements must also be made in the enforcement regulations for an enforcing authority to comply with a direction made under section 59 to suspend or modify the emissions limit duty.
331. *Schedule 5* details the measures that may be included in the regulations made under section 60 about monitoring and enforcement of compliance with the emissions limit. These include the relevant national authority determining which body will be the enforcing authority, expected to be the Environment Agency in England, the Scottish Environmental Protection Agency, the Northern Ireland Environment Agency and the new Natural Resources Body for Wales.
332. *Paragraph 1* of Schedule 5 details the matters that can be dealt with in the enforcement regulations. Among other things, they make provision for publication of information on compliance with the emissions limit; authorise the national authority to set up a charging regime; provide for enforcement of the duty through enforcement notices; and confer a right of appeal against decisions made by the enforcing body.
333. Away from enabling the enforcement regulations to contain provision which will facilitate an enforcing authority to perform its enforcement activities in *paragraph 1*, *paragraph 2* describes the provision that can be made in relation to enforcement notices and the possible effect that enforcement notices can have. *Paragraph 3* enables provision to be included dealing with the imposition of financial penalties in cases of a breach. *Paragraph 4* provides that the enforcement regulations may contain consequential amendments to other legislation when such amendments are necessary to implement an emissions limit duty enforcement regime.

### **Section 61: Interpretation of Chapter 8**

334. This section defines terms used in this Chapter. For example, the section defines “fossil fuel” as coal, lignite, peat, natural gas, crude liquid petroleum, bitumen or any substance which is produced directly or indirectly from these products for use as fuel and, when burnt, produces carbon dioxide.

## **Section 62: Regulations under Chapter 8**

335. *Subsection (1)* provides that any orders or regulations made under this Chapter must be made by statutory instrument. *Subsection (2)* makes a similar provision in respect of regulations made by DETI and requires these regulations to be made by way of statutory rule.
336. *Subsection (3)* applies the affirmative resolution procedure to any regulations made under section 57. *Subsection (4)* subjects any enforcement regulations to the negative resolution procedure. Therefore, regulations containing provision for monitoring and enforcement are subject to the negative procedure. Where any regulations seek to make consequential amendments to primary legislation the regulations are subject to the affirmative resolution procedure. Equivalent procedures apply in respect of regulations or statutory rules made by the devolved administrations, see *subsections (6), (7) and (8)*.
337. *Subsection (10)* respects the Northern Ireland devolution settlement and the fact that the policy in this Chapter relates to a matter within the legislative competence of the Assembly in Northern Ireland. Accordingly, the Secretary of State must obtain the consent of DETI before making provision under section 57 which will apply in Northern Ireland.
338. *Subsection (11)* requires the Secretary of State to consult Scottish and Welsh Ministers and such persons as Secretary of State thinks appropriate before making regulations under section 57(6) (interpretation of duty or applying duty with modifications to additional cases) or section 60(2) (monitoring and enforcement). *Subsection (12)* requires Scottish Ministers and Welsh Ministers to consult such persons as they think appropriate before making regulations under section 60 (monitoring and enforcement).

## **Chapter 9: Miscellaneous**

### **Section 63: Exemption from liability in damages**

339. This section gives the Secretary of State the power to make provision in contracts for difference (CFD) regulations (see section 6), capacity market regulations (see section 27) or regulations relating to investment contracts (see [paragraph 6](#) of Schedule 2) to limit the national system operator's liability to pay damages if a civil claim was brought against it in respect of its role, or a particular element of its role, as the delivery body for the CFD and capacity market schemes and in relation to investment contracts. A limit on liability in damages could extend to the acts or omissions of the national system operator, its directors, employees, officers or agents.
340. This section does not allow the Secretary of State to limit liability in cases where an act or omission is in bad faith, where the act or omission would be unlawful under section 6 of the Human Rights Act 1998, or where the national system operator has breached an order for securing compliance issued by the Authority under the enforcement powers in the Electricity Act 1989.
341. *Subsection (4)* places a reporting duty on the Secretary of State. If the Secretary of State confers a CFD, capacity market or investment contracts delivery function on the national system operator and does not limit the national system operator's liability in damages in respect of that function, the Secretary of State must publish a statement setting out the reasons why.

### **Section 64: Licence modifications: general**

342. This section provides more detail about the licence and industry code modification powers in sections 26 (contracts for difference), 37 (capacity market), 45 (conflicts of interest), 49 and 50 (access to markets etc) and [paragraph 19](#) of Schedule 2 (investment contracts). It describes the parliamentary scrutiny procedure, the full scope of the powers, duties to publish modifications and other technical requirements.



343. *Subsections (2) to (7)* set out the parliamentary scrutiny procedure, which is a variation of the “draft negative” procedure used for some statutory instruments. *Subsections (2) and (3)* provide that before making modifications, the Secretary of State must lay a draft before Parliament for a period of 40 days, during which either House of Parliament may reject the draft modifications. If the modifications are not rejected during the 40-day period the Secretary of State can bring them into effect (*subsection (4)*). *Subsections (6) and (7)* explain how the 40-day period is calculated.
344. *Subsections (8) and (9)* set out the full scope of the licence modification powers:
- *subsection (8)* allows the Secretary of State to use the licence modification powers to make modifications which are general (i.e. applicable to all licence holders) or specific (for example, to make different provision for small suppliers or generators). It also allows the Secretary of State to make different modifications of different licences and to make incidental, supplemental, consequential or transitional modifications;
  - *subsection (9)* enables provisions included in a licence or industry code by a modification made under these powers to make different provision for different cases (i.e. it allows a licence to be modified in a way that requires or allows the licence holder to deal with other people in different ways). It also makes it clear that any provisions imposed by such a modification need not relate to the activities (e.g. generation, supply) that the licence authorises. *Subsection (9)(c)* enables a licence condition which is imposed under these powers to confer certain functions on the Secretary of State or the Authority, to the same extent as section 7(2A), (3) or (4) of the Electricity Act 1989. For example, this could require a licence holder to comply with a direction given by the Authority or the Secretary of State.
345. *Subsection (10)* requires the Secretary of State to publish the details of any modifications as soon as reasonably practicable after he or she brings them into effect.
346. *Subsections (11) and (12)* make provision about the relationship between licence modifications made under the power and standard conditions:
- *subsection (11)* requires the Authority to incorporate modifications to standard conditions of licences in future licences and to publish the modifications. The standard conditions of electricity licences are governed by section 33 of the Utilities Act 2000 (in relation to generation, distribution and supply licences), section 137(3) of the Energy Act 2004 (electricity transmission licences) and section 146 of the Energy Act 2004 (electricity interconnector licences). Section 8A of the Electricity Act 1989 provides that the conditions which, by virtue of those enactments, are standard conditions for a particular type of licence are incorporated by reference in all licences of a particular type;
  - *subsection (12)* states that a modification to a part of a standard condition of a licence does not prevent any other part of the condition from continuing to be regarded as a standard condition for these purposes.
347. *Subsection (13)* explains that a power to modify a licence or code is a continuing power, like a power to make statutory instruments. Modifications made at a later date could amend, add to or remove earlier modifications, or make completely new modifications.

### ***Section 65: Consequential amendments***

348. This section makes minor amendments to other legislation to ensure the coherence of electricity law. *Subsection (1)* has the effect of requiring the Secretary of State and the Authority, whenever they apply the “principal objective” under section 3A of the Electricity Act 1989 (the principal objective is to protect the interests of present and future consumers), to have regard to the need to secure that licensees are able to finance their obligations under the Energy Act 2013.

*These notes refer to the Energy Act 2013 (c.32)  
which received Royal Assent on 18 December 2013*

349. *Subsections (2) to (4)* add the Energy Act 2013 to three lists of legislation; where an Act is on the list, licence modification powers contained in the Act can be used modify the standard conditions of electricity licences.

***Section 66: Review of certain provisions of Part 2***

350. This section requires the Secretary of State to carry out a review of much of Part 2, as soon as is reasonably practicable five years after Royal Assent, and report the conclusions to Parliament. In the report, the Secretary of State must set out the objectives of the provisions which are under review, the extent to which the objectives have been achieved, whether the objectives are still appropriate and, if they are, whether there might be other ways of achieving them which impose less regulation.