



Department
of Energy &
Climate Change



Electricity Settlements Company Ltd

Framework Document

This framework document has been drawn up by the Department of Energy and Climate Change in consultation with the Electricity Settlements Company. It sets out the relationship between the Electricity Settlements Company and its sole shareholder, the Secretary of State for Energy and Climate Change, and the broad framework within which the Electricity Settlements Company will operate. It is signed and dated on behalf of the Secretary of State for Energy and Climate Change and the Electricity Settlements Company. Copies of the document and any subsequent amendments will be placed in the Libraries of both Houses of Parliament and made available to members of the public on the Electricity Settlements Company website.

Contents

A. INTRODUCTION

B. PURPOSE AND REMIT OF THE ELECTRICITY SETTLEMENTS COMPANY

C. ACCOUNTABILITY AND CORPORATE GOVERNANCE

D. OPERATIONAL AND FINANCIAL REPORTING

E. FINANCIAL RESPONSIBILITIES

F. MISCELLANEOUS

ANNEX: MATTERS REQUIRING SHAREHOLDER CONSENT

ELECTRICITY SETTLEMENTS COMPANY LTD: SHAREHOLDER RELATIONSHIP FRAMEWORK DOCUMENT

1 August 2014

A. INTRODUCTION

1. BACKGROUND

- 1.1 This framework document (the “**Framework Document**”) has been drawn up by the Department of Energy and Climate Change (“**DECC**”) in consultation with the Electricity Settlements Company Limited (“**Company**”). It describes:
- (A) certain activities which the Company is required to perform and the guiding principle with which the Company is expected to comply in performing those activities;
 - (B) certain aspects of the relationship between the Secretary of State for Energy and Climate Change as sole shareholder (the “**Shareholder**”) and the Company, and the manner in which it is expected that the Shareholder and the Company will interact with each other; and
 - (C) the intention of the Shareholder to allow day-to-day operational independence of the Company subject to certain limited exceptions provided for in this Framework Document, legislation, and the Company’s constitutional documents.
- 1.2 A key principle in developing this Framework Document has been the creation of a framework within which the Company can fulfil its purpose with appropriate operational independence whilst within certain limitations on that independence which are either (i) common to government-owned entities and necessary to satisfy Government and Parliamentary budgeting and accountability requirements, or (ii) specific to the controls the Shareholder requires over the policy implementation that the Company has been mandated to execute. However, in particular:
- (A) it is recognised that the Company is a separate corporate entity and that the governance, and decision-making processes, of the Company flow through its board, with the executive reporting to that board; and
 - (B) this framework is not intended to replace or duplicate the Company’s own internal corporate governance structure, but instead to enable an effective and clearly defined and aligned Company-shareholder relationship, appropriate to a government-owned company, including facilitating the necessary information and reporting flows and efficient dialogue.
- 1.3 It is agreed that the success of the relationship depends on the nature and quality of the relationship between the Company Board and the Shareholder. The overall responsibility for ensuring that the intentions of the Framework Document are carried out in practice lies ultimately with the Chair and the Secretary of State

acting in his or her capacity as Shareholder. The Chair or relevant Company representatives will maintain regular contact with the Secretary of State or an official nominated by the Secretary of State.

- 1.4 In addition to the regular reporting set out in section 8 (Information Flows) of this Framework Document, there will be quarterly shareholder meetings between the Company and DECC. The purpose of these meetings between relevant Company representatives and senior representatives of DECC is to provide a forum for information exchange and discussion on key aspects relevant to the Company's activities of mutual interest and to ensure alignment between the Company and DECC.
- 1.5 The Company was established on 26 March 2014 as a company limited by shares. It is wholly-owned by the Shareholder as the Capacity Market Settlements Body pursuant to the Energy Act 2013 and related Regulations (the "**Regulations**") (together the "**EA Legislation**").
- 1.6 The Secretary of State for Energy and Climate Change or his relevant successor is the Minister ultimately responsible to Parliament for the Company and will account for the Company's business in Parliament.

B. PURPOSE AND REMIT OF THE ELECTRICITY SETTLEMENTS COMPANY

2. ELECTRICITY SETTLEMENTS COMPANY PURPOSE

- 2.1 The purpose and remit of the Company are set out in the objects clause of the Company's Articles of Association as follows:
 - (A) to act as the settlement body for the capacity market and, in such capacity, to perform the functions, comply with the duties and obligations and exercise the rights, powers and discretions which are set out in, arise out of or in connection with or are provided for pursuant to the capacity market legislation;
 - (B) (without prejudice to the generality of paragraph (A)), to calculate, collect and administer in accordance with the capacity market legislation:
 - (i) capacity market supplier charge and settlement costs levy payments payable by electricity suppliers;
 - (ii) penalties and termination fees payable by capacity providers; and
 - (iii) any other payments payable to the settlement body under capacity market legislation;
 - (C) (without prejudice to the generality of paragraph (A)), to calculate and pay in accordance with the capacity market legislation:
 - (i) capacity payments payable to capacity providers; and

- (ii) any other payments payable by the settlement body under capacity market legislation;
- (D) (without prejudice to the generality of paragraph (A)), to carry out reconciliation of payments in accordance with the capacity market legislation;
- (E) (without prejudice to the generality of paragraph (A)) to calculate, collect and hold credit cover from electricity suppliers, capacity providers and potential participants in capacity market auctions in accordance with the capacity market legislation;
- (F) (without prejudice to the generality of paragraph (A)) to:
 - settle disputes in relation to settlement calculations;
 - settle disputes in relation to non-BSC data provided by a Capacity Provider;
 - conduct metering tests,
 in accordance with the capacity market legislation;
- (G) to undertake such other activities in relation to Electricity Market Reform (“EMR”) as the board considers to be consistent with the company’s functions, duties and obligations which are set out in, arise out of or in connection with or are provided for pursuant to the capacity market legislation;
- (H) to do all other things which the board considers ancillary, incidental or conducive to the attainment or fulfilment by the company of the foregoing objects;
- (I) to provide advice and information to DECC about certain aspects of the workings of the capacity market settlement process.

3. ELECTRICITY SETTLEMENTS COMPANY OPERATIONAL PARAMETERS

3.1 The Company is a company wholly-owned by Government and also has obligations under the EA Legislation and Rules. It will undertake its activities in accordance with:

- (A) its objects as specified in its Articles of Association;
- (B) the terms of any relevant EU state aid approvals;
- (C) all applicable laws and regulations;
- (D) applicable constraints which apply to arm’s length bodies owned by Government where relevant;

- (E) except as otherwise agreed by DECC (in the first instance), and (if required) HM Treasury, the principles, rules, guidance and advice in Managing Public Money;
 - (F) the Guiding Principle as defined in section 4 below (Company Guiding Principle); and
 - (G) the Shareholder Consent Matters as defined in section 5 below (Shareholder Consent Matters).
- 3.2 Subject to section 3.1 above, the Shareholder intends that the Company should operate as a commercially responsive and responsible company, which will include operating efficiently in a commercial timeframe, ensuring it has appropriate resources and personnel to do so.
- 3.3 It is recognised that the company will not initially have its own employees and will be resourced through an agreement with the Low Carbon Contracts Company Limited, whereby the Low Carbon Contracts Company Limited provides the Company with the resources it requires, in return for payment, to enable the Company to perform its activities under and associated with its purpose as set out in Section 2 (Electricity Settlements Company Purpose).

4. COMPANY GUIDING PRINCIPLE

In carrying out activities under and associated with the Company's purpose as set out in section 2 (Electricity Settlements Company Purpose) and within the operational parameters set out in section 3 (Electricity Settlements Company Operational Parameters), the Company shall seek to maintain market participants' confidence in the capacity market settlement process and minimise costs to consumers (the "**Guiding Principle**").

5. OPERATIONAL INDEPENDENCE AND SHAREHOLDER CONSENT MATTERS

The Shareholder intends that the Company should have day-to-day operational independence from Government, however, certain decisions, as set out in the Annex, will require the prior written consent of the Shareholder (the "**Shareholder Consent Matters**").

C. ACCOUNTABILITY AND CORPORATE GOVERNANCE

6. CORPORATE GOVERNANCE

6.1 The Company shall operate a corporate governance framework which, so far as practicable and in the light of the other provisions of this Framework Document or as otherwise may be agreed with the Shareholder, accords with corporate governance best practice. In particular (but without limitation), the Company shall comply with the provisions of the United Kingdom's Corporate Governance Code (the "**Corporate Governance Code**"), other than section E (Relations with Shareholder, as it applies to small quoted companies or specify and explain any non-compliance in its annual report. The Company shall also, as far as it is applicable, comply with the spirit and principles of the Corporate Governance in Central Government Departments Code of Good Practice¹.

6.2 It is agreed that:

- (A) the Company Board is to consist of no fewer than two and no more than twelve directors;
- (B) the senior independent non-executive director and the independent, non-executive directors are to constitute at least half of the Company Board;
- (C) the Shareholder shall appoint the Company's Chair and Senior Independent Director² and shall appoint up to two suitably qualified persons as its representative directors (the "**Shareholder Representative Directors**"), and any other directors to the Company Board in accordance with the Articles;
- (D) subject to the prior written consent of the Shareholder in accordance with the Articles, the Company Board shall appoint the other directors according to the recommendations of the Nominations Committee;
- (E) the Company Board shall regularly ensure that suitably rigorous appraisals are made of the effectiveness of the Chairman and the members of the Company Board;
- (F) non-Executive Company Board members will be subject to re-election every three years;
- (G) the Company Board shall have due regard to the UK Corporate Governance Code's principle that the search for board candidates should be conducted, and

¹ The Shareholder recognises that areas of the Code are not appropriate to a non-government department and expects the Company to exercise its judgement.

² The Chair and Senior Independent Director appointments shall be made by the Shareholder in line with Office of Commissioner of Public Appointments principles.

appointments made, on merit, against objective criteria and with due regard for the benefits of diversity on the board, including gender.

- 6.3 The Company Board should ensure that effective arrangements are in place to provide assurance on risk management, governance and internal control. The Company Board is expected to assure itself of the effectiveness of the internal control and risk management systems.
- 6.4 Individual board members should comply at all times with the Code of Conduct for Board Members of Public Bodies³ and with the rules relating to the use of public funds and to conflicts of interest, including;
- (A) not misusing information gained in the course of their public service for personal gain or for political profit, nor seeking to use the opportunity of public service to promote their private interests or those of connected persons or organisations;
 - (B) complying with the Company Board's rules on the acceptance of gifts and hospitality, and of business appointments.
- 6.5 The Company Board:
- (A) will constitute as a minimum the following committees of the Company Board:
 - (i) Audit and Risk Committee;
 - (ii) Remuneration Committee⁴; and
 - (iii) Nominations Committee;
 - (B) will ensure that one Shareholder Representative Director may always be a member of the Remuneration Committee and of the Audit and Risk Committee;
 - (C) may establish other committees of the Company Board as it determines appropriate.
- 6.6 The Shareholder expects remuneration arrangements for directors and senior management (including any performance related remuneration) to be recommended to the Company Board by the Remuneration Committee and approved by the Company Board, having due regard to the public sector status of the organisation as well as taking account of appropriate benchmarks within the private and public sectors.

³ http://resources.civilservice.gov.uk/wp-content/uploads/2011/09/code-of-conduct_tcm6-38901.pdf

⁴ It is recognised that the Company will not have employees immediately and so the Remuneration Committee will be constituted once it is appropriate and required.

- 6.7 However, the prior written consent of the Shareholder in accordance with the Articles of Association will be required for:
- (A) the approval of or agreement to (or material variation or amendment of) the remuneration, the terms and conditions on which such remuneration is to be paid or granted or the terms of employment or engagement of any director or the remuneration of any executive officer or other employee that is equal to or higher than the threshold outlined in the Cabinet office guidance for approval of senior pay⁵ (or equivalent pro-rata amount). This consent will apply to any new appointment or reappointment to a role regardless of whether this is at the same level as has been previously consented to by the Shareholder; or
 - (B) any pay rise for any director or employee of the Company whose fees or salary has been approved under section 6.7(A), which are material, where a 'material pay rise' is that which is considered to be above the current rate of the Consumer Price Index (CPI).
- 6.8 Gifts to staff must only be made in accordance with policies and processes agreed by the Board or the Remuneration Committee.

7. RISK MANAGEMENT

The Company shall ensure that, except as expressly agreed with the Shareholder, the risks that it faces are dealt with in an appropriate manner, in accordance with relevant aspects of best practice in corporate governance, and develop a risk management strategy. It should adopt and implement policies and practices to safeguard itself against fraud and theft, in line with the Treasury's guidance on tackling fraud⁶. Except in the case of the initial appointment of a subsidiary of ELEXON Ltd as payment and settlement agent, it should also take all reasonable steps to appraise the financial standing of any firm or other organisation with which it intends to enter into a contract.

⁵ The thresholds are currently (as of 1 August 2014) £142,500 for salaries and £17,500 for bonuses. The calculation of whether a salary is equal to or higher than the £142,500 threshold must include any bonus amount that is above £17,500.

⁶ http://webarchive.nationalarchives.gov.uk/20130129110402/http://www.hm-treasury.gov.uk/d/managing_the_risk_fraud_guide_for_managers.pdf.pdf

D. OPERATIONAL AND FINANCIAL REPORTING

8. INFORMATION FLOWS

- 8.1 The following mechanisms will be used to ensure relevant information flows between the Secretary of State for Energy and Climate Change (the 'Shareholder') and the Company:
- (A) a Monthly Financial Report in agreed form. The Shareholder will limit additional reporting requirements on the Company and where possible will rely on reports prepared for the Board;
 - (B) quarterly shareholder meetings as described in section 1.4 (Background) above;
 - (C) the Company will promptly and without delay disclose to the Shareholder any information regarding the Company which is likely to have a material adverse effect on the delivery of the Company's purpose as described in section 2 (Electricity Settlements Company Purpose), or is likely to result in the Company having insufficient funds to meet its operational costs or its obligations under EA Legislation;
 - (D) the Company will provide the Shareholder with copies of Board papers;
 - (E) the Shareholder will be entitled on reasonable notice to such information in relation to the affairs of the Company as it may reasonably require.
- 8.2 Any information provided to the shareholder under section 8.1 above will take into account any BSC⁷ related contractual confidentiality provisions.

9. FINANCIAL REPORTING REQUIREMENTS

- 9.1 The Company will provide DECC and/or HM Treasury with monthly notice (forecast) of its cash requirements as requested by the Shareholder.

⁷ Balancing and Settlement Code

E. FINANCIAL RESPONSIBILITIES

10. DELEGATED FINANCIAL AUTHORITY

Delegated financial authorities will be agreed between the Shareholder and the Company.

11. ELECTRICITY SETTLEMENTS COMPANY BUSINESS PLAN

The Company Board will prepare and maintain a three year Business Plan (setting out the operational delivery plan including capital costs) to be updated annually and agreed with the Shareholder. The first such plan will be prepared in 2015 to support the 2016/17 operational budget.

12. ELECTRICITY SETTLEMENTS COMPANY OPERATIONAL BUDGET

- 12.1 The Company Board will prepare and maintain an operational budget (the “**Budget**”) which is appropriate to ensure the fulfilment by the Company of its purpose as described in Section 2 (Electricity Settlements Company Purpose), and compliance with its associated obligations, as described in this Framework Document.
- 12.2 Every year the Company will submit to the Shareholder its proposed annual operational budget (relating to its next financial year set out in the context of the most recent Business Plan (as defined in section 11 (Electricity Settlements Company Business Plan)) in order to ensure DECC can comply with its obligation to consult on the operating costs of the Company and amend the levy rate in regulations. This must be provided within an agreed format with sufficient time and information to enable the Shareholder to approve it prior to consultation on the operational cost levy rate.
- 12.3 The Shareholder will have regard to the responses from the consultation before final approval of the budget. The Company and DECC shall make best efforts to carry out their respective responsibilities to ensure that the consultation and fixing of the operational cost levy rate in regulation is completed in sufficient time to ensure that Company is able to raise the levy at the times anticipated in order to meet its operating costs. This would also apply to any in year adjustment to the budget.
- 12.4 Any in-year adjustment to the budget will follow the process set out in sections 12.2 and 12.3 above.
- 12.5 Notwithstanding section 12.2 and 12.3 above, the Company’s Accounting Officer is accountable for ensuring that the Budget is prepared and spent in accordance with Managing Public Money as appropriate in accordance with section 3.1 (E) of this document (Electricity Settlements Company Operational Parameters). The Principle Accounting Officer of DECC has designated the Chief Executive as the Electricity Settlements Company’s Accounting Officer. The Principle Accounting

Officer is responsible for ensuring that arrangements are in place to monitor and maintain effective oversight of the Company.

13. REQUIREMENTS FOR DECC BUDGETING: CAPEX

- 13.1 The capital budget for the year ahead and a provisional baseline will be negotiated and agreed annually in accordance with DECC's business planning process. The capital budget will be set for the 12 months ending 31 March each year. The capital budget will be funded by DECC each financial year and if required will be repaid to DECC in subsequent years through depreciation charged in the operational cost levy

14. MANAGEMENT OF OPERATIONAL COSTS AND CAPITAL EXPENDITURE

- 14.1 DECC will provide the Company with a working capital loan facility to support the Company in managing its operational costs and Grants in Aid to finance the agreed capital expenditure, the terms of which are set out in a separate letter between DECC and the Company.

15. ANNUAL ACCOUNTS AND AUDIT

Annual Report and Accounts

- 15.1 The Company must produce an annual report as required under the Regulations together with its audited accounts after the end of each year. The Company annual report and accounts should be made available on the Company's website.
- 15.2 The Company shall provide DECC with audited financial information and supporting narratives by specified dates each year in order for DECC to prepare its consolidated annual report and accounts.

Internal Audit

- 15.3 The Company will establish an appropriate internal audit function which will report to the Company Board's Audit and Risk Committee, and provide to the Shareholder all material reports and findings subject to BSC related contractual confidentiality provisions.

External Audit

- 15.4 The Company will:
- (A) appoint suitably qualified auditors to audit its financial statements with regard to the recommendations of the Audit and Risk Committee. However, DECC's strong assumption is that this will be the NAO;

- (B) produce its accounts in accordance with statutory requirements, apply the requirements of the Companies Act and IFRS⁸;
- (C) provide DECC Finance team when requested with such information as is necessary for DECC to produce its own accounts.

⁸ International Financial Reporting Standards

F. MISCELLANEOUS

16. CONTINUATION OF THE COMPANY

16.1 Subject to section 16.2 below, the Company will continue in existence and for so long as it is required to carry out the Company's purpose as set out in section 2 (Electricity Settlements Company Purpose).

16.2 It is envisaged that the Company will be wound up upon:

- (A) completion of the Company's purpose or remit as set out in section 2 (Electricity Settlements Company Purpose); or
- (B) termination by the Secretary of State of the appointment of the Company as Settlement Body in accordance with EA Legislation.

16.3 DECC shall put in place arrangements to ensure the orderly winding up of the Company⁹.

17. PUBLICATION

17.1 Copies of this Framework Document, and any amendment to it, will be placed in the libraries of the Houses of Parliament and can be obtained from the Company at Fleetbank House, 2-6 Salisbury Square, London, EC4Y 8JX. The Company shall also make this Framework Document (and any amendments to it) available on its website.

18. STATUS AND REVISION OF FRAMEWORK DOCUMENT

18.1 Subject to section 18.2 below, any amendment, update or replacement of any provision of this Framework Document shall be effected by the Shareholder giving notice in writing to the Company Board.

18.2 If the Shareholder proposes to amend, update or replace any element of the Framework Document, it shall consult, and seek to reach agreement with, the Company Board before effecting the relevant amendment, update or replacement.

18.3 This Framework Document should be interpreted in light of the Articles, EA Legislation and English company law and is without prejudice to the statutory and other rights and obligations of the Shareholder or the Company.


⁹ See Managing Public Money Annex 7.2.

19. REVIEW OF THE COMPANY

19.1 The Shareholder expects to conduct a review of the Company as part of an evaluation of EMR within three years.

19.2 The Shareholder shall review the location of the Company within the first 3 years to decide whether to relocate the Company within 5 years of operation.

Signed by authority of the Secretary of State for Energy and Climate Change

 (SIMON V. ALLET)

.....
Dated: 1/8 2014

Signed by authority of the Electricity Settlements Company

 (HELENE TURNER)

.....
Dated: 1/8 2014

ANNEX

MATTERS REQUIRING SHAREHOLDER CONSENT

1. Whilst the Company has day-to-day operational independence as described in section 5 (Operational Independence and Shareholder Consent Matters) of this Framework Document, the Company may make certain decisions only once it has received the prior written consent of the Shareholder (the “**Shareholder Consent Matters**”).
2. The Shareholder Consent Matters are:
 - I. The following commitments with financial or policy impacts for DECC:
 - a. any action which is not contemplated or permitted by this Framework Document or which is contrary to the Guiding Principle;
 - b. any action which will give rise to obligations or liabilities (including contingent liabilities) which are not in the normal course of the Company's business or which are not expected to be affordable in terms of expected levy income (present or future);
 - c. any action which, notwithstanding the levy arrangements, will or is likely to give rise to an additional funding requirement from DECC (including loans for capital expenditure) or other additional financial support being required from, or liabilities or obligations being assumed by DECC (including in the form of an indemnity).
 - II. Management of Operations:
 - a. the approval of or any increase in the Company's Annual Budget in accordance with section 12 (Electricity Settlements Company Operational Budget);
 - b. the approval of financial assistance, subject to section 14 (Management of Operational Costs and Capital Expenditure), which provides for the Company to incur operating costs that are greater than the levy income expected to be received in the same financial year;
 - c. the approval of or material deviation from or any revised version of the Company's Business Plan as defined in section 11 (Electricity Settlements Company Business Plan);
 - d. the approval of any board appointments and related remuneration arrangements in accordance with the Framework Document;
 - e. the approval of any change to the location of the Company;
 - f. the approval of any change to the name of the Company;

- g. the approval of the borrowing of funds from any organisation other than DECC or HM Treasury;
- h. the approval of the establishment of subsidiary companies and the acquiring of any other business/company;
- i. the approval of the depositing of funds in accounts other than within the Government banking service;
- j. the approval of investments not through deposits in interest bearing accounts provided through the Government Banking Service;
- k. the approval of the appointment of any auditors as described in section 15.4 (External Audit);
- l. the approval of any exceptions to Managing Public Money as referred to in section 3.1 (E) (Electricity Settlements Company Operational Parameters) or otherwise agreed by HM Treasury.