



Department
of Energy &
Climate Change

Low Carbon Contracts Company and Electricity Settlements Company operational costs 2016/17

Consultation on the operational cost levies

November 2015



The consultation can be found on the Gov.UK website at:

<https://www.gov.uk/government/consultations/low-carbon-contracts-company-and-electricity-settlements-company-operational-costs-201617>

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General information

Purpose of this consultation:

This consultation document seeks views on the proposed 2016/17¹ operational cost budgets and resulting levies for the Low Carbon Contracts Company and the Electricity Settlements Company.

Issued: 5 November 2015

Respond by: 3 December 2015

This is a short consultation period due to the limited and focussed nature of the material to be reviewed.

Enquiries to:

LCCC/ESC Shareholder Team – Clean Electricity Directorate
Department of Energy & Climate Change,
Fourth Floor Area D,
3 Whitehall Place,
London, SW1A 2AW
Tel: 0300 068 5683

Email: emoperationalcosts@decc.gsi.gov.uk

Consultation reference: URN 15D/491 – Low Carbon Contracts Company and Electricity Settlements Company operational costs 2016/17

Territorial extent:

This consultation applies throughout Great Britain.

How to respond:

You are invited to respond to this consultation either digitally to our official mailbox emoperationalcosts@decc.gsi.gov.uk or by post to:

LCCC/ESC Shareholder Team
Department of Energy & Climate Change,
Fourth Floor Area D,
3 Whitehall Place,
London, SW1A 2AW

If you have any comments on the operational cost budgets and levies as set out in this document it would be helpful if you can also provide supporting analysis to explain your position, where appropriate.

¹ 1 April 2016-31 March 2017.

Additional copies:

You may make copies of this document without seeking permission. An electronic version can be found at <https://www.gov.uk/government/consultations/low-carbon-contracts-company-and-electricity-settlements-company-operational-costs-201617>.

Other versions of the document in Braille, large print or audio-cassette are available on request. This includes a Welsh version. Please contact us under the above details to request alternative versions.

Confidentiality and data protection:

Information provided in response to this consultation, including personal information, may be subject to publication or disclosure in accordance with the access to information legislation (primarily the Freedom of Information Act 2000, the Data Protection Act 1998 and the Environmental Information Regulations 2004).

If you want information that you provide to be treated as confidential, please say so clearly in writing when you send your response to the consultation. It would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded by us as a confidentiality request.

We will summarise responses and confirm the outcome of the consultation in the Government Response which will be published on the [Gov.UK website](#). The Government response will include a list of names or organisations that responded but not people's personal names, addresses or other contact details.

Quality assurance:

This consultation has been carried out in accordance with the [Government's Consultation Principles](#).

If you have any complaints about the consultation process (as opposed to comments about the issues which are the subject of the consultation) please address them to:

DECC Consultation Co-ordinator
3 Whitehall Place
London SW1A 2AW
Email: consultation.coordinator@decc.gsi.gov.uk

Introduction

Budget proposals for the Low Carbon Contracts Company (LCCC) and the Electricity Settlements Company (ESC)

1. This consultation document seeks views on the proposed 2016/17 operational cost budgets and resulting levies for the Low Carbon Contracts Company (LCCC) and the Electricity Settlements Company (ESC).
2. The operational cost levies of LCCC and ESC are set out in legislation (the Regulations^{2,3}). In line with the Energy Act 2013⁴, we are consulting before making any regulations to amend the levies for 2016/17.
3. The levies proposed for 2016/17 are based on estimated operating costs (including applicable depreciation) of £14.216m for LCCC and £4.474m for ESC. The levy rate for the LCCC is proposed to be £0.0503/MWh after taking into account electricity estimated to be supplied over the levy period. The total estimated operational costs for ESC will be collected from electricity suppliers in proportion to the electricity they supply during the relevant period, as per the relevant legislation.
4. We anticipate that the total impact of LCCC and ESC costs on household electricity bills to be around £0.20 in 2016/17 (at 2014 prices)⁵, which equates to around a 0.05% increase in average household electricity bills⁶.
5. A list of consultation questions is set out on page 8 and responses are invited from all interested parties by 3 December 2015. Details on how to respond can be found on page 5. We will analyse responses and address any issues raised in a Government response to the consultation, which we plan to publish in early 2016. If appropriate, we will then amend the relevant legislation to reflect the new levy rates for 2016/17.
6. If there is a material change to the estimated operational costs of LCCC and ESC between the publication of this consultation document and the laying of regulations in Parliament,

² Regulation 23 of the Contracts for Difference (Electricity Supplier Obligations) Regulations 2014 (as amended).

³ Regulation 9 of the Electricity Capacity (Supplier Payment etc.) Regulations 2014 (as amended).

⁴ The Energy Act (2013) http://www.legislation.gov.uk/ukpga/2013/32/pdfs/ukpga_20130032_en.pdf

⁵ The bill impact of LCCC and ESC operational costs are estimated by assuming that such costs faced by electricity suppliers are spread evenly across electricity sales. This provides a £/MWh cost which is multiplied by estimated average household consumption to estimate the bill figure, in this case of around £0.20.

⁶ 'Average household electricity bill' refers to DECC's estimated projections of the level of a household electricity bill after policies, in a central fossil fuel scenario, consistent with those published in the 2014 Prices and Bills report (details available at <https://www.gov.uk/government/publications/estimated-impacts-of-energy-and-climate-change-policies-on-energy-prices-and-bills-2014>).

DECC will publish an amendment to this document. In these circumstances, responses will be required by the latest of either two weeks from publication of the amended consultation, or by the original closure date. Should there be minor adjustments to the budget during consultation or as a result of the consultation process these will be outlined in the Government Response.

7. Part 1 of this consultation document sets out the background to the Government policy of Electricity Market Reform, which LCCC and ESC are helping to deliver. It also describes the functions of LCCC and ESC, their governance structures, the assumptions underlying the operational costs budgets, and the timing for collecting the levies. Part 1 is for information purposes only; it is not subject to this consultation.
8. Part 2 of this document sets out LCCC’s estimated operating costs for 2016/17, and electricity demand in Great Britain over the same period (the levy year). These estimates allow a £/MWh levy rate to be calculated for inclusion in the relevant legislation. Part 2 also sets out ESC’s estimated operating costs for the same period.

Catalogue of consultation questions

Consultation Question	
1.	Do you have any comments on LCCC’s estimated costs as set out in this consultation paper?
Consultation Question	
2.	Do you have any comments on the forecast electricity demand from which the £/MWh levy rate for LCCC is derived?
Consultation Question	
3.	Do you have any comments on ESC’s estimated costs as set out in this consultation paper?

Part 1: Low Carbon Contracts Company and Electricity Settlements Company operational costs - background information

Establishment of the companies

9. Government's Electricity Market Reform was designed to secure significant investment in low-carbon electricity generation. Two key mechanisms of that reform are Contracts for Difference (CFDs) and the Capacity Market. CFDs incentivise investment in low-carbon technologies by removing generators' long-term exposure to electricity price volatility, while the Capacity Market ensures security of supply in accordance with the agreed reliability standard.
10. Government has incorporated two companies, wholly owned by the Secretary of State for Energy and Climate Change, to manage key aspects of CFDs and the Capacity Market: the LCCC and the ESC.

Company functions

11. LCCC, as counterparty to CFDs (including the Investment Contracts which have been transferred to LCCC⁷), manages the contracts and is responsible for payments thereunder. During 2016/17, it will have particular responsibility for:
 - Setting the quarterly supplier obligation interim levy rate and level of total reserve payments;
 - Collecting the operational cost and supplier obligation levies and the reserve fund payments;
 - Dealing with requests for minor and necessary modifications to CFDs pre-allocation;
 - Managing Investment Contracts, and signing and managing CFDs;
 - Metering verification of any private network generators that have been allocated a CFD;
 - Approval and ongoing monitoring of Fuel Monitoring, Sampling and Sustainability proposals for relevant CFD holders;
 - Making payments to generators under CFDs;
 - Implementing the exemptions for Electricity Intensive Industries (EII) and Green Excluded Electricity (GEE) from the Supplier Obligation through changes to the settlement system during 2016/17; and
 - Continuing to provide services to the ESC which will be reimbursed at cost.

⁷ Investment Contracts, which have been transferred to the LCCC, are treated, by virtue of regulation 2(4) of the Contracts for Difference (Electricity Supplier Obligations) Regulations 2014, as CFDs for various purposes. Any reference to a CFD in this document is to be treated as including any such Investment Contracts.

12. ESC is responsible for transactions relating to the Capacity Market, including making capacity payments to capacity providers, controlling collateral and managing auction bid bonds. In 2016/17, it has particular responsibility for:
- Capacity payments to Transitional Arrangement capacity providers throughout the delivery year, from 1st October 2016;
 - Verifying the meters of those providers whose capacity agreement is conditional on the company approving their meter configuration; and
 - Delivering Capacity Market settlement system modules, required to collect and make payments to capacity providers, from Winter 2016 onwards.

Governance

13. Separate Framework Documents⁸ govern the operation of LCCC and ESC. Each document sets out the relationship between the relevant company and its sole shareholder, the Secretary of State for Energy and Climate Change.
14. Both documents also contain a guiding principle. The principle provides that, in carrying out activities, the companies shall seek, in respect of LCCC, to maintain investor confidence in the CFD regime and, in respect of ESC, to maintain market participants' confidence in the capacity market settlement processes, and, in both cases, minimise costs to consumers.
15. As Government-owned companies, LCCC and ESC are subject to the Government's framework for managing public money⁹.
16. The Department of Energy and Climate Change (DECC)'s Accounting Officer (AO) is accountable to Parliament for the performance of the two companies alongside the Chief Executive Officer of LCCC and ESC, who is the AO for these companies. The companies report to DECC on a regular basis to ensure they are run efficiently and continue to provide good value for money.

The Operational Cost Levies

17. The operational cost levies of LCCC and ESC have been designed so that the methodology of payment calculation and the frequency of payment are consistent with the principal supplier obligations for the CFD regime and the Capacity Market.

Low Carbon Contracts Company

18. The operational cost levy rate is calculated by dividing LCCC's proposed annual budget by the total forecast electricity demand for 2016/17, as set out in Part 2 below.
19. The operational cost levy will be collected alongside the principal supplier obligation in the same daily invoice using the same settlement systems. The Settlement Service Provider

⁸ The Framework Documents are published on the companies' websites – see www.lowcarboncontracts.uk and www.electricitysettlementscompany.uk

⁹ Available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/212123/Managing_Public_Money_AA_v2_-_chapters_annex_web.pdf

(EMR Settlements Ltd, a wholly owned subsidiary of Elexon) will administer the collection process on LCCC's behalf.

20. Since the levy rate is based on estimations of LCCC's operating costs and the overall electricity supplied in the corresponding period, the amount collected is unlikely to match actual expenditure. Any surplus recorded at year-end will be reimbursed to suppliers.¹⁰ In the event of a forecast deficit, Government will in the first instance expect LCCC to manage its costs within its own budget, including re-prioritising spend where possible. Government may also increase the levy rate in-year if there is a significant discrepancy between projected levy income and estimated expenditure which LCCC can justify but cannot manage. To do so, it would be necessary first to consult publicly, as any change to the levy rate would require amending legislation. Where appropriate, and solely at its discretion, DECC can provide the company with grant-in-aid to cover any levy deficit or unplanned expenditure.

Electricity Settlements Company

21. The total amount levied on suppliers will be equal to the budget included in the Electricity Capacity (Supplier Payment etc.) Regulations 2014, as amended. Operational costs will be budgeted, and the levy set, for the period April to March even though the principal levy will be based on Capacity Market delivery years, which run from October to September. Initially the amount charged to suppliers will be proportionate to their share of the total electricity supplied during the previous winter's 'period of high demand' (between 4 and 7pm on working days between November and February), reflecting the approach taken for the main Capacity Market Supplier Charge. This levy will then be revised to reflect actual supply data relating to the same 'period of high demand' for the current levy period (in this case November 2016 to February 2017).
22. The Capacity Market operational cost levy will be collected on a monthly basis, with the Settlement Service Provider administering the collection process on behalf of ESC.
23. In the event that the total amount of levy collected exceeds ESC's actual operational costs, the surplus at year-end will be reimbursed to suppliers. As with LCCC, where there is a deficit, Government will in the first instance expect ESC to manage its costs from within its own budget, including re-prioritising spend where necessary. Government may also seek to increase the levy in-year if there is a significant discrepancy between projected levy income and estimated expenditure which ESC can justify but cannot manage. Again, it would be necessary to consult on, and obtain Parliamentary approval for, any change in the levy. Where appropriate, and solely at its discretion, DECC can provide the company with grant-in-aid to cover any levy deficit or unplanned expenditure.

Key assumptions underpinning cost estimates

24. The cost estimates, presented in this consultation document, are underpinned by a number of assumptions, which are subject to some uncertainty. In setting the budget, a balance must be struck between ensuring that the companies have sufficient resources to perform their role effectively, while minimising:
- The risk of over collection (notwithstanding that any surplus will be reimbursed to suppliers); and

¹⁰ Contracts for Difference (Supplier Obligation) Regulations 2014

- The uncertainty that could be caused for suppliers by the need to change the levy rate within year.

LCCC assumptions

25. LCCC will be managing at least 37 CFDs in 2016/17 awarded as a result of auction allocations to date and Investment Contracts transferred to them from DECC. In addition, LCCC will manage two Investment Contracts on behalf of DECC (who is the counterparty) under an Agency Agreement, until they are transferred to LCCC. It is also expected that, if approved, LCCC will sign and manage a Hinkley Point C nuclear CFD which may be agreed later this financial year (2015/16). The proposed budget also includes provision to manage additional CFDs which would result from any Allocation Rounds held in 2015/16 or 2016/17.
26. The Carbon Capture Storage (CCS) Commercialisation Competition opened in April 2012 and makes available £1 billion capital funding, together with additional operational funding through a CFD, to support the design, construction and operation of the UK's first commercial-scale CCS projects. The resources required to manage the CCS CFDs in 2016/17, following completion of the Competition and signature, are currently uncertain as Competition projects will need to be affordable, show value for money and be competitive and Government could support one, two or no projects. The resources needed for CCS CFDs may result in a budget requirement of up to £250k in addition to the budget being consulted on in this document. We therefore propose that, if required, LCCC's budget will be increased by up to £250k to cover management of CCS CFDs. Over the course of the consultation period we will work to refine the estimate of the resources required and will confirm this in the Government Response to the consultation. We would only follow the procedure set out in paragraph 6 if the amount by which the LCCC's budget increases as a result of the inclusion of an amount for CCS work is in excess of £250k.

ESC assumptions

27. ESC will be commencing capacity payments to Demand Side Response bidders following the first Transitional Auction in January 2016; and undertaking meter services and assurance, as well as controlling collateral and managing auction bid bonds.

Part 2: The companies' estimated costs for 2016/17

Low Carbon Contracts Company

The total estimated budget for the Low Carbon Contracts Company for 2016/17 is £14.216m, a breakdown of which is shown in table 1.

Table 1:

Description	Estimated costs – 2016/17 £'000
Premises costs	386
Payroll costs	5,465
Settlement costs	3,023
IT & telephony costs	1,066
Professional and legal fees	3,032
Contractors	475
Insurance	525
Other costs	1,282
Depreciation	669
Recharge to ESC	(1,707)
Total	14,216

Premises costs

28. Government policy is that, where possible, existing Government estate should be used by public sector bodies rather than entering into new leases for property. For this reason, LCCC continues to be based at Fleetbank House, Blackfriars, where it rents accommodation from the Department of Business, Innovation and Skills (BIS)¹¹. The total cost of the rental agreement is £32k per month, which is inclusive of rent, council tax and service charge (which includes heating, water and power supply). Dilapidation costs¹² will be charged to the operational costs levy in the financial year in which they are incurred, which is expected to be 2019/20.

Payroll costs

29. Based on an average of 51 employees plus 7 Board members, estimated payroll costs for 2016/17 are £5.465m. These costs include gross salary payments, National Insurance contributions, pensions, bonuses, payroll outsourcing costs, benefits and recruitment costs, a breakdown of which is included in Table 2. Whilst LCCC is classified as a public sector organisation, its staff are not Civil Servants and so they have separate terms and conditions, pay and benefit packages.
30. The proposed budget anticipates an increase in staff, predominantly to deal with additional contract management activity to support a Hinkley Point C nuclear CFD and maintain the proactive approach to management of renewables contracts, as well as enhanced metering assurance services required for Capacity Market readiness. The organisational structure has been designed to ensure that LCCC has the optimal structure for supporting expected operational activities for the least cost. Senior salaries have been benchmarked against organisations carrying out similar activities and against other relevant Government arm's length bodies. The salaries of senior executives are published in the companies' annual reports and accounts and, where those salaries are £150k and above, they will also be published online by the Cabinet Office¹³ in the interests of transparency. In accordance with Government rules, any pay that is above the Prime Minister's salary is cleared by DECC Ministers and, where such pay relates to Ministerial Board appointments, it is cleared additionally by HM Treasury Ministers.

¹¹ The location of LCCC and ESC will be reviewed within 3 years of becoming operational to decide whether to locate the companies outside London and the South East within 5 years of operation.

¹² Dilapidation costs are the costs that will be incurred at the end of the rental period when moving out of a leased building and are those costs required to restore the rental space back to its original state.

¹³ Salaries of £150k and above will be included in data published by the Cabinet Office on high earning senior officials: <https://www.gov.uk/government/publications/senior-officials-high-earners-salaries>

Table 2:

Description	Estimated costs – 2016/17 £'000s
Gross salary costs ¹⁴	4,075
Employers' National Insurance	503
Employee benefits ¹⁵ , bonus ¹⁶ & pension ¹⁷	693
Recruitment costs	184
Payroll outsourcing	10
Total payroll costs	5,465

Settlement costs

31. The operational costs of the Settlement Service Provider have been estimated at £3.023m for 2016/17 and are set out in Table 3 below. These relate to the daily collection of the operational cost levy and principal Supplier Obligation and making payments to generators under CFDs. Capital expenditure in 2016/17 on the settlement system is described in more detail at paragraph 37.

¹⁴ Includes Board costs.

¹⁵ Includes life assurance, private medical cover, personal accident cover and income protection insurance.

¹⁶ The amount budgeted is based on bonuses of up to 20% salary for 2 senior executives and base bonuses of 5-10% for all other staff, if all staff achieve a bonus. Bonus payments will be subject to staff meeting agreed performance criteria.

¹⁷ The pension employer contribution rate is 10%.

Table 3:

Description	Estimated costs - 2016/17 £'000s
Elexon support staff and related costs	1,639
Business process operational costs	1,126
Audit and assurance ¹⁸	258
Total settlement costs	3,023

IT and telephony costs

32. Total IT and telephony costs for 2016/17 are estimated at £1.066m. Operational IT and telephony costs are incurred for the provision of web hosting, support and maintenance of IT infrastructure and end user equipment, as well as the ongoing running and support costs for fixed and mobile telephony.

Professional and legal fees and contractors

33. The total cost of professional and legal fees, together with contractor costs, has been estimated at £3.507m. Professional fees include those relating to carrying out audit and assurance activities, including fraud prevention activity and generator site audits. They also cover the provision of technical and legal advice required to support the effective management of contracts and other compliance activity, in particular to support the additional requirements surrounding the management of a Hinkley Point C nuclear CFD.

¹⁸ These costs relate to settlement assurance activities undertaken by EMR Settlements Ltd on its own systems and processes.

Table 4:

Description	Estimated costs - 2016/17 £'000s
Professional services	676
Legal fees	1,100
Technical advice ¹⁹	477
Audit, assurance and compliance	450
Fuel monitoring, metering and biomass sustainability.	329
Contractors	475
Total professional fees and contractor costs	3,507

Insurance

34. Insurance is procured on a commercial basis, using an insurance broker engaged under the Crown Procurement framework. The costs reflect the statutory insurances required by the company as well as insurance that any commercial organisation would typically have in place. The level of cover reflects the activity that LCCC expects to be undertaking in 2016/17.

Other costs

35. Other costs include stakeholder engagement and communications, travel and subsistence, training, printing and stationary, and irrecoverable VAT.

36. As LCCC's operational cost levy is based on a £/MWh rate, its levy funding will vary with the amount of electricity actually supplied. A £0.5m contingency is therefore included (under 'other costs') to cover any reduction in volume of electricity supplied (e.g. due to warm weather). This contingency is based on a 4% reduction between forecast and actual supply. The LCCC's requirement to use this contingency will be monitored by DECC. DECC hopes this contingency will avoid any in-year operational cost levy rate increase relating to this specific risk or any other circumstances when an increase would otherwise have been justified.

¹⁹ E.g. engineering advice on whether projects are achieving required construction milestones.

Depreciation

37. DECC will continue to provide grant-in-aid to LCCC to fund capital expenditure planned for 2016/17. Any levy that is subsequently collected in respect of the cost of depreciating these assets will be repaid to DECC in the years it is collected. Capital expenditure planned for 2016/17 is estimated at £0.508m and relates to IT hardware, core operational systems and premises-related costs. The levy proposed in this consultation includes £0.669m for depreciation, of which £0.062m relates to capital in 2016/17 and the remainder to capital expenditure in previous years.

Electricity Settlements Company cost recharge

38. In order to maximise efficiencies in the operation of LCCC and ESC, it was decided that ESC, rather than being developed independently, would contribute at cost for the use of shared facilities, back-office functions and the use of staff it requires for its corporate functions and operational activities. The recharge agreement is explained in more detail under ESC costs.

Low Carbon Contracts Company levy rate

39. LCCC's operational costs are collected on the basis of a gross²⁰ electricity demand projection. For 2016/17, a projected gross demand of 282.85 TWh will be used to calculate the levy rate. The forecast gross electricity demand is based on National Grid's Indicated Out-Turn (INDO) forecast for 2016/17 with adjustments to reflect historic outturn and the exemptions associated with Electricity Intensive Industries (EIIs)²¹.

40. Based on estimated costs of £14.216m and the forecast electricity supply of 282.85 TWh, the operational cost levy rate will be £0.0503/MWh for 2016/17²².

Consultation Question	
1.	Do you have any comments on LCCC's costs as set out in this consultation paper?
Consultation Question	
2.	Do you have any comments on the forecast electricity demand from which the £/MWh levy rate for LCCC is derived?

²⁰ Gross demand is total demand rather than demand net of embedded generation.

²¹ Subject to State Aid, the Department for Business, Innovation and Skills (BIS) intends to introduce EII exemptions from operational cost levy payments in 2016/17. To take account of this, a reduction has been made to the demand forecast based on estimated EII electricity usage in the levy period. BIS currently estimates that 20TWh of electricity per annum will be eligible for exemption at a rate of 85%.

²² The levy rate is calculated by dividing LCCC's proposed annual budget by the total forecast gross electricity demand for 2016/17.

Electricity Settlements Company

The total estimated budget for the Electricity Settlements Company for 2016/17 is £4.474m, a breakdown of which is shown in table 1.

Table 5:

Description	Estimated costs - 2016/17 £'000
Settlement costs	1,485
Low Carbon Contracts Company cost recharge	1,707
Insurance	99
Professional fees	285
Other costs	79
Depreciation	819
Total	4,474

Settlement costs

41. The costs of the Settlement Service Provider, as set out in Table 6, include the costs of administering and monitoring bid bonds and collateral, as well as the payment flows resulting from the Transitional Auction in January 2016; collecting the operational cost levy for 2016/17; and conducting pre and post auction meter checks for Unproven Demand Side Response bidders.
42. The costs of delivering functionality to the settlement system for the Capacity Market will be treated as capital expenditure, which will be funded through a grant in aid, provided by DECC (and repaid through depreciation charges over time). This is covered in paragraph 50.
43. Other costs include metering assurance and operational audit costs.

Table 6:

Description	Estimated costs 2016/17 £'000s
Elexon support staff and related costs	938
Business process operational costs	350
Audit and assurance	197
Total settlement costs	1,485

Low Carbon Contracts Company cost recharge

44. In order to reduce costs as far as possible, ESC will continue to share services and back-office functions with LCCC and so has no employees of its own. Under this arrangement, ESC pays LCCC to provide the functions it requires. This cost is based on an estimate of the time LCCC employees will spend on ESC activities during the levy period, together with an appropriate allocation of overhead costs (including rent, service charges, IT infrastructure and telephony support) as well as a 'use of asset' charge. For core systems which are shared between LCCC and ESC, and where the capital expenditure has been initially funded through LCCC, a charge for the use of these assets will be made to ESC based on a notional depreciation amount. The recharged costs also include a proportion of the salaries of the Board members, who will also be dividing their time between the two companies. LCCC will undertake these activities on behalf of ESC and the ESC Board will retain responsibility and accountability for the quality and cost of services provided by LCCC.
45. This approach avoids ESC replicating functions that LCCC already provides. LCCC must therefore have sufficient capacity in 2016/17 to ensure ESC has the necessary resources to perform all of its functions in relation to the Capacity Market and fulfil its purpose and activities under the shareholder framework document and the relevant legislation.
46. For 2016/17 LCCC and ESC have agreed a recharge of £1.707m, which will be payable by ESC in monthly instalments. In general, this agreed cost for the period shall be fixed and not subject to amendment. If the costs incurred in undertaking the ESC function prove to be materially in excess of the estimated costs, LCCC shall be entitled to amend the level of recharge accordingly. If the costs of undertaking ESC functions prove to be materially less than estimated, resulting in actual cost savings by LCCC, the cost payable by ESC shall be reduced accordingly.

Insurance

47. Insurance is procured on a commercial basis, using an insurance broker engaged under the Crown Procurement framework. The costs reflect the statutory insurances required by the company as well as insurance that any commercial organisation would typically have in

place. The level of cover reflects the activity that ESC expects to be undertaking in 2016/17.

Professional fees

48. The company proposes to undertake a range of fraud prevention activities associated with metering for the Capacity Market, including meter auditing and site visits. These fees relate to the assurance and monitoring costs of undertaking this work.

Other costs

49. In addition to the above, there are a number of other directly incurred costs which ESC will incur. These relate primarily to the annual audit fee for the completion of the statutory annual report and accounts as well as stakeholder management and communications activity.

Depreciation

50. DECC will continue to provide grant-in-aid to ESC to fund capital expenditure planned for 2016/17. Any levy that is subsequently collected in respect of the cost of depreciating these assets will be repaid to DECC in the years it is collected. Capital expenditure planned for 2016/17 is estimated at £1.098m and relates to the implementation of the Capacity Market settlement system. The levy proposed in this consultation includes £0.819m for depreciation, of which £0.15m relates to capital expenditure in 2016/17 and the remainder to previous capital expenditure in previous years.

Consultation Question

3.	Do you have any comments on ESC's costs as set out in this consultation paper?
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