



Department for
Business, Energy
& Industrial Strategy

Low Carbon Contracts Company and Electricity Settlements Company Operational Costs 2021/22

Consultation on the Operational Cost Levies

Closing date: 14 December 2020



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Any enquiries regarding this publication should be sent to us at: LCCC-ESOperationalcosts@beis.gov.uk

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General information

Why we are consulting

This consultation document seeks views on the proposed 2021/22¹ operational cost budgets, resulting levies for the Low Carbon Contracts Company (LCCC) and the Electricity Settlements Company (ESC), and changes to legislation.

Consultation details

Issued: 16 November 2020

Respond by: 14 December 2020

Enquiries to:

Email: LCCC-ESCOperationalcosts@beis.gov.uk

Consultation reference: Consultation on the Operational Cost Levies

Audiences:

The Government welcomes views from anyone with an interest in the policy area. We envisage that the consultation will be of interest to licensed electricity suppliers in Great Britain; generators; consumer groups; CfD delivery bodies and other stakeholders with an interest in the energy sector.

Territorial extent:

The CfD scheme applies in the UK but does not currently operate in Northern Ireland. This consultation therefore applies to Great Britain only.

¹ The financial year runs from 1 April – 31 March.

How to respond

Respond online at: <https://beisgovuk.citizenspace.com/clean-electricity/operational-cost-budgets-levy-rates-lccc-esc-21-22>

or

Email to: LCCC-ESCOperationalcosts@beis.gov.uk

When responding, please state whether you are responding as an individual or representing the views of an organisation. If you wish to respond but are unable to do so online because of difficulties with accessibility, please contact us on 020 7215 5000.

Your response will be most useful if it is framed in direct response to the questions posed, though further comments and evidence are also welcome.

Confidentiality and data protection

Information you provide in response to this consultation, including personal information, may be disclosed in accordance with UK legislation (the Freedom of Information Act 2000, the Data Protection Act 2018 and the Environmental Information Regulations 2004).

If you want the information that you provide to be treated as confidential please tell us, but be aware that we cannot guarantee confidentiality in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not be regarded by us as a confidentiality request.

We will process your personal data in accordance with all applicable data protection laws. See our [privacy policy](#).

We will summarise all responses and publish this summary on [GOV.UK](#). The summary 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 way this consultation has been conducted, please email: beis.bru@beis.gov.uk.

List of acronyms

Acronym	
AO	Accounting Officer
BEIS	Department for Business, Energy and Industrial Strategy
CfD	Contract for Difference
CM	Capacity Market
CCUS	Carbon Capture Use and Storage
ESC	Electricity Settlements Company
GPA	Government Property Agency
HMRC	HM Revenue & Customs
LCCC	Low Carbon Contracts Company
MWh	Megawatt-hour
10 SC	10 South Colonnade
TWh	Terawatt-hour

Introduction

Budget proposals for the Low Carbon Contracts Company and Electricity Settlements Company

1. The operational costs of the Low Carbon Contracts Company (LCCC) and the Electricity Settlements Company (ESC) are recovered through levies on electricity suppliers as set out in legislation ('the regulations'^{2,3}). The Energy Act 2013 requires that we consult before making any regulations to amend the levies. In legislation, the levy relating to ESC is called the 'settlement costs levy', and the levy relating to LCCC is called the 'operational costs levy'. The references in this consultation to 'operational costs levy' cover both levies for simplicity.
2. Prior to 2017/18, we consulted on and amended the levies on an annual basis for the following financial year. However, in order to offer stakeholders and parliament greater visibility of the estimated operational costs, to reduce the administrative burden on LCCC and ESC, and to save Parliamentary time, in 2017 we consulted on changes to the regulations that would enable levies to be set for the financial years: 2018/19, 2019/20 and 2020/21. Parliament approved these changes in 2018.
3. However, this consultation seeks views on the proposed operational costs for LCCC and ESC and resulting levies for the 2021/22 financial year only.
4. We would prefer to consult on the proposed budget and associated levies for more than the next financial year due to the benefits outlined at paragraph 2. However, electricity demand has reduced significantly during the Covid-19 pandemic and increased uncertainty with regards to a number of factors that are used to forecast electricity demand. The possibility of further lockdowns or other actions the Government may have to take to control further outbreaks could also impact on future electricity demand levels and make it difficult to forecast beyond the 2021/22 financial year.
5. The operational costs levy is calculated by dividing LCCC's proposed annual budget by the total forecast electricity demand for the corresponding financial year. If demand is lower than forecast, LCCC will not be able to raise enough income from the levy to meet their budgeted costs. Therefore, a robust forecast of electricity demand is needed for each financial year in order to set LCCC's levy rate accurately.
6. The period for which the levy can be set for LCCC has knock-on impacts for ESC's levy setting. A significant part of ESC's cost is the recharge from LCCC, which cannot be budgeted for in isolation from LCCC (see paragraphs 82-84 for an explanation of the

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).

recharge). As we believe it is prudent to set the LCCC budget for 2021/22 only, due to current difficulties in accurately forecasting electricity demand beyond this financial year, it is only possible to set ESC's operational cost levy for the same period.

7. We anticipate we will next need to consult on LCCC and ESC's operational costs in 2021. When we do so we intend to set out a budget and associated levy costs for the financial years: 2022/23, 2023/24 and 2024/25, provided we are confident that we can forecast electricity demand for these years with sufficient robustness and it is otherwise appropriate to consider operational costs for all of these years.
8. For LCCC, operational costs are £20.847m and for ESC £7.472m for ESC based on estimated costs (including applicable depreciation) for 2021/22. We estimate that the total impact of LCCC and ESC operational costs on household electricity bills over 2021/22 will be around £0.40 (at 2020 prices⁴).
9. The consultation document is split into the following sections:
 - Part 1 sets out LCCC's and ESC's functions and describes their governance structures, the assumptions underlying the operational costs, and the timing for collecting the levies.
 - Part 2 sets out LCCC's estimated operating costs for 2021/22 and electricity demand in Great Britain over the associated levy year. These estimates allow a £/MWh levy rate to be calculated for inclusion in the amending regulations. It also sets out ESC's estimated operating costs for 2021/22 for inclusion in the amending regulations.
10. A list of consultation questions is set out below and responses are invited from all interested parties by 14 December 2020. Details on how to respond can be found on page 5.

⁴ The bill impact of LCCC and ESC operational costs is 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 calculate the bill figure, in this case, of around £0.40.

Consultation questions

Consultation questions	
1.	Do you have any comments on LCCC's estimated operational costs set out in this consultation document?
2.	Do you have any comments on the forecast electricity demand from which the £/MWh levy rates for LCCC are derived?
3.	Do you have any comments on ESC's estimated operational costs set out in this consultation document?

What happens next?

11. We will analyse responses and produce a Government response to this consultation, which we plan to publish in early 2021. Subject to the outcome of this consultation and Parliamentary approval, we will amend the relevant legislation to enable levies to be set for 2021/22.
12. If there is a material increase to the total estimated operational costs of LCCC or ESC between the publication of this consultation document and the laying of the amending regulations in Parliament, we will publish an amendment to this document. In such circumstances, responses will be required to the amended document by the latest of 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 to this document.
13. We intend that, subject to the will of Parliament, the amending regulations will come into force before the beginning of the 2021/22 financial year. However, if it is not possible to complete the parliamentary process within this time period the existing levies will continue to apply until such time as the regulations are amended.
14. If the amending regulations are delayed, we would need to consider making an adjustment to the 2021/22 levy rate as set out in this consultation in order that the estimated operational costs of LCCC can be collected in full. Any necessary revision to the rate would be communicated in the Government response to this consultation. In the case of the ESC operational costs levy, we would expect to collect the difference between the 2020/21 levy and the 2021/22 levy amount as part of the March 2022 reconciliation (as part of the revised settlement cost levy calculations set out in paragraph 8, Schedule 1 of the Electricity Capacity (Supplier Payment etc.) Regulations 2014 (as amended)).

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

Overview

15. LCCC and ESC are responsible for delivering key elements of Contracts for Difference (CfDs) and the Capacity Market (CM) schemes respectively.
16. LCCC enters into and manages CfDs (including the Investment Contracts which have been transferred to it⁵) with low carbon generators, awarding top-up payments for qualifying generation. During 2021/22 it will have particular responsibility for:
 - managing the CfD portfolio, including the Hinkley Point C nuclear CfD, to ensure all pre-generation contractual milestones (Milestone Delivery Dates, Operational and Further Conditions Precedent) are met. Ensuring that generators are fulfilling their compliance and reporting obligations, including those relating to post-commissioning fuel monitoring, sampling and sustainability, and where appropriate, handling any disputes that may arise;
 - entering into new CfDs, which involves industry engagement and coordination with National Grid-ESO ahead of allocation rounds, dealing with requests for minor and necessary modifications to CfDs pre-allocation, signing and managing initial conditions precedent with successful applicants;
 - collecting from electricity suppliers the operational costs and the CfD Supplier Obligation (the levy on electricity suppliers to pay for the cost of low-carbon generation under the CfD scheme), which will involve:
 - setting the quarterly supplier obligation interim levy rate and total reserve amount;
 - collecting the supplier obligation levies, the total reserve amount and the suppliers' collateral payments;
 - providing projections for future quarterly supplier obligation interim levy rates and total reserve amounts and cash utilisation via online Levy Dashboards⁶;
 - making payments to generators as required under CfDs;

⁵ Investment Contracts, which have been transferred to 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.

⁶ <https://www.lowcarboncontracts.uk/dashboards/cfd/levy-dashboards>

- managing payments under the supplier obligation reconciliation process; and
 - metering verification of any private network generators that have been allocated a CfD.
 - contributing to CfD and policy development:
 - supporting the ongoing review and development of existing and future CfD standard terms and conditions;
 - feeding into CfD consultations concerning potential changes to CfD structures, settlement activities, and any other related regulations;
 - delivering revisions to the CfD settlement system to reflect policy changes, ensuring continued correct processing of transactions; and
 - subject to Government confirmation of support for Carbon Capture Usage and Storage (CCUS) power projects under the Energy Act 2013, supporting the drafting of the contract and preparing to manage and settle these contracts.
 - providing supporting services to ESC, which will be reimbursed at cost.
17. ESC is responsible for all financial transactions relating to the Capacity Market, including making capacity payments to capacity providers, managing supplier credit cover and capacity providers' auction credit cover. During 2021/22, it will have particular responsibility for:
- collecting from electricity suppliers the operational costs levy, and the Capacity Market Supplier Charge which funds capacity payments;
 - making payments to capacity providers successful in the 2020/2021 T-1 capacity auctions and the 2017/18 T-4 capacity auction which are expected to secure over 50GW of capacity for delivery in 2021/22;
 - managing the collection, holding, monitoring and, where appropriate, refund of credit cover collected from auction applicants; and
 - verifying the meter arrangements of those providers whose capacity agreement is conditional on ESC approving their meter configuration.
- contributing to Capacity Market development:
 - delivering revisions to the Capacity Market settlement system to reflect policy and rule changes, ensuring continued correct processing of transactions;
 - implementing changes to the Capacity Market settlement system arising out of the five-year review of the capacity market⁷; and

⁷ These changes include, but are not limited to, lowering of the minimum capacity threshold for participating in auctions; direct participation of foreign capacity; the participating rules for new types of capacity; the access to long-term contracts; the volume in the year-ahead auction and compliance with the new Electricity Regulation.

- feeding into Capacity Market consultations from Government and Ofgem concerning potential changes to settlement activities and any other related regulations.

Governance

18. LCCC and ESC are private limited Companies wholly-owned by the Secretary of State for Business, Energy and Industrial Strategy. The Companies have day-to-day operational independence, subject to certain limited exceptions which require shareholder consent. The relationship between the Companies and the shareholder is set out in separate Framework Documents⁸.
19. Both documents contain a guiding principle. This requires that, in carrying out its activities, LCCC should seek to maintain investor confidence in the CfD regime and ESC should seek to maintain market participants' confidence in the Capacity Market settlement processes. The guiding principle also requires both Companies to minimise costs to consumers.
20. As Government-owned Companies, LCCC and ESC are subject to the Government's framework for managing public money⁹.
21. The Accounting Officer (AO) of the Department for Business, Energy and Industrial Strategy (BEIS) 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. Two Shareholder Representative Directors sit on the Board of both Companies.

The Operational Cost Levies

22. 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.

⁸ The Framework Documents are published on the Companies' website – see <https://lowcarboncontracts.uk/corporate-governance>. The LCCC document is available at: <https://lowcarboncontracts.uk/sites/default/files/publications/Low%20Carbon%20Contracts%20Company%20Framework%20Document%20-%20August%202014%20-%20Signed.pdf> and the ESC document is available at: <https://lowcarboncontracts.uk/sites/default/files/publications/Electricity%20Settlements%20Company%20Framework%20Document%20-%20August%202014%20-%20Signe....pdf>

⁹ Available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/454191/Managing_Public_Money_AA_v2_-jan15.pdf

Low Carbon Contracts Company

23. The operational cost levy rate is calculated by dividing LCCC's proposed annual budget by the total forecast electricity demand for the corresponding financial year, as set out in Part 2 below.
24. The operational cost levy will be collected alongside the principal supplier obligation (the interim levy) in the same daily invoice using the same settlement system. The Settlement Service Provider (EMR Settlements Ltd, a wholly-owned subsidiary of Elexon) administers the collection process on LCCC's behalf.
25. Since the levy rate is based on estimates 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 in accordance with the Regulations¹⁰. In the event of a forecast deficit, Government will in the first instance require LCCC to manage its costs within its available 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, BEIS can provide the Company with budget and grant-in-aid to cover any levy deficit or justifiable unplanned expenditure.

Electricity Settlements Company

26. The total amount levied on suppliers will be equal to the budget included under Regulation 9 in the Electricity Capacity (Supplier Payment etc.) Regulations 2014, as amended. Operational costs will be budgeted, and the levy set, for the financial year. The initial monthly amount charged to suppliers will be proportionate to their share of the total electricity supplied during the previous winter's 'period of high demand' (4 to 7pm on working days between November and February inclusive). Suppliers' shares of the levy are then revised after 16 March to reflect actual supply data relating to the 'period of high demand' for the current levy period (for example, for the 2021/22 levy, demand 4 to 7pm on working days between November 2021 to February 2022).
27. The Settlement Service Provider administers the collection process on behalf of ESC.
28. 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 require 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

¹⁰ Contracts for Difference (Supplier Obligation) Regulations 2014

for, any change in the levy. Where appropriate, and solely at its discretion, BEIS can provide the Company with budget and grant-in-aid to cover any levy deficit or justifiable unplanned expenditure.

29. Details of the operational expenditure for both LCCC and ESC are published in their annual report and accounts, which are audited by the National Audit Office and made available on the Companies' website¹¹.

Key assumptions underpinning cost estimates

30. 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
 - the uncertainty that could be caused for suppliers by the need to change the levy rate in-year.

LCCC key assumptions

31. LCCC currently manages 73 CfDs to which it is a direct counterparty (including the nuclear CfD for Hinkley Point C).
32. The proposed budget includes some provision to manage potential additional CfDs that would result from CfD allocation round 4.

ESC key assumptions

33. ESC manages credit cover pre-and post-auctions and capacity payments commencing 1 October every year resulting from two annual auctions a year (a T-1 auction one year ahead of delivery and a T-4 auction four years ahead of delivery). As the number of applicants for the two annual auctions carries on increasing, there will be increasing meter assurance activity required for those providers whose capacity agreement is conditional on ESC approving their meter configuration.

¹¹ The 2019/20 Annual Report and Accounts are available at: <https://www.lowcarboncontracts.uk/annual-reports>

Part 2: The Companies' estimated costs for 2021/22

Low Carbon Contracts Company

34. The total estimated budget for the Low Carbon Contracts Company for 2021/22 is £20.847m, representing a £3.362m increase on the £17.485m budget for 2020/21.
35. LCCC's budget has not increased significantly since 2018/19, with the budget increasing by 3% in 2019/20 and 3% in 2020/21. The larger increase in budget for 2021/22 reflects a number of factors, including LCCC's growing role in helping to meet our legally binding net zero target, increased uncertainty in energy demand arising out of the Covid-19 pandemic and other cost increases beyond LCCC's control, such as insurance premiums and new premises costs.
36. If the UK is to meet its net zero target, further deployment of low carbon electricity generation will be required. Despite a growing portfolio, CfD operational costs are falling both per contract and by overall generation capacity. The increase in the LCCC budget in 2021/22 across payroll and settlement services reflects the estimated increase in the number of contractual events from existing CfD projects, the engagement with applicants and onboarding of new CfD projects from the Allocation Round 4 process and implementation of the projected pipeline of policy and regulatory change.
37. Where it is possible to reduce operational costs without compromising scheme delivery, LCCC has taken steps to do so. LCCC has invested in bringing certain skills in-house to reduce professional fees. Professional fees (excluding the legal dispute contingency) across ESC and LCCC are broadly in line with 2020/21, despite increased contractual events. IT costs have been kept level by moving to the cloud and bringing key skills in-house. By moving to a hybrid model of working that sees staff working from home more often, LCCC will reduce the number of desks they require when they move to new offices in June 2021, saving £184k on initial relocation plans.
38. An indicative breakdown of the total estimated operational costs for 2021/22 is provided in Table 1, together with comparative figures for the 2020/21 budget.
39. Further information can be found below on the areas of spend.

Table 1:

Description	Budgeted costs – 2020/21 £000s	Estimated costs – 2020/21 £000s
Payroll Costs	7,342	7,678
Professional and Legal Fees *	6,157	7,515
Settlement Service	3,309	3,503
IT Costs	715	716
Depreciation	580	391
Premises Costs	434	715
Contractor Costs	108	198
Other Costs **	1,633	2,924
Recharge	(2,793)	(2,793)
Total	17,485	20,847

*includes a ring-fenced contingency for legal disputes. This was £2.1m in 2020/21 and is £3m in 2021/22 (see paragraphs 64-65 for further details).

**includes a contingency for any reduction in volume of electricity supplied. This was £0.75m in 2020/21 and is £1.5m in 2021/22 (see paragraphs 62-63 for further details).

Payroll costs

40. Based on an average of 83 employees plus 6 Board members, estimated payroll costs for 2021/22 are £7.678m. A breakdown of the costs is included in Table 2. Estimated payroll costs are £0.336m higher than those budgeted for in 2020/21. This is due to four new roles and the full year impact of staff recruited part way through financial year 2020/21. Where LCCC staff perform functions on behalf of ESC, payroll costs will be recharged to ESC accordingly.
41. LCCC has budgeted for four additional staff, including 3 apprentices, taking overall headcount to 83 employees by 2021/22. These new apprentices will provide support for

LCCC's IT, HR and Forecasting team. An additional Contract Manager will provide additional resource for allocation round 4.

42. 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.
43. The Company's organisational structure has been designed to ensure that LCCC has the optimal structure for undertaking expected operational activities in an efficient way. 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 LCCC's annual report and accounts and, where those salaries are £150k and above, they will also be published online by the Cabinet Office in the interests of transparency. In accordance with Government rules, any pay that is above the Prime Minister's salary is cleared by BEIS Ministers and, where such pay relates to Ministerial Board appointments, it is cleared additionally by HM Treasury Ministers.

Table 2:

Description	Estimated costs – 2020/21 £000s
Gross salary costs ¹²	5,798
Employers' National Insurance	759
Employee benefits ¹³ , bonus ¹⁴ and pension ¹⁵	1,121
Total	7,678

Professional and legal fees

44. The total cost of professional and legal fees has been estimated at £4.515m (excluding disputes) for 2021/22. Costs associated with professional services and legal fees are incurred to support effective management of CfDs and other compliance activity (see Table 3).
45. Changes in professional fees over the 2021/22 financial year reflect the existing portfolio of CfDs and the potential increase in the number of CfDs under management over the

¹² Includes Board costs.

¹³ Includes life assurance, private medical cover, personal accident and income protection insurance.

¹⁴ The amount budgeted is based on bonuses of up to 20% salary for Executive Directors, up to 12% for senior managers and up to 6% for other staff, if all staff achieve a bonus. Bonus payments will be subject to staff meeting agreed performance criteria.

¹⁵ The pension employer contribution rate is 10% for Executive Directors and 8% for other staff.

period, following Allocation Round 4. Events requiring professional fees include planned events such as facilities reaching contractual milestones, and generator driven events such as approvals of changes to Fuel Monitoring Sampling and Sustainability plans from thermal generators, or handling force majeure or qualifying change in law claims. The cost per contract under management is projected to fall by around 13% over 2021/22. This reflects the Company’s aim to carry out routine work in-house and to use outside resource efficiently when required to provide additional capability.

46. The “Professional and Legal Fees” line item also includes the ringfenced legal dispute contingency budget, which is discussed in detail at paragraphs 64-65.

Table 3:

Description	Estimated costs – 2020/21 £000s
Professional services and legal fees	2,761
Technical advice	670
Audit, assurance and compliance	880
Fuel monitoring, sustainability, metering	204
Disputes	3,000
Total	7,515

Settlement Service

47. Estimated total operational costs related to the settlement system, including the costs of the Settlement Service Provider and software upgrades are set out in Table 4 below. These costs relate to the daily collection of the operational cost levy and principal supplier obligation and making payments to generators under CfDs. The audit and assurance costs include the costs for the provision of meter verification services for any private network generators that may be offered a CfD. Meter assurance services will be undertaken by the Settlement Services Provider as Metering Agent using a sub-contractor (which is currently Siemens).
48. There is a continued requirement for changes to the settlement system which includes changes associated with CfD allocation rounds, the impact of code changes on the settlement system and operational improvements. The Company has budgeted around £1.950m split between resource and other third party spend for this in 2021/22.

Table 4:

Description	Estimated costs – 2020/21 £000s
Resource and sub-contractors	1,937
Other third party and Assurance costs	1,566
Total	3,503

IT costs

49. Total IT costs have remained flat compared to the 2020/21 budget and are estimated at £0.716m for 2021/22. This has been achieved by bringing key skills in-house in parallel with moving to cloud-based applications.

Depreciation

50. These charges relate to the assets LCCC has purchased using loan funding initially provided by BEIS, such as the IT hardware and the development and build of the settlement system for CfDs. The cash collected through the levy for depreciation will be repaid to the Department in accordance with the loan agreements in place.

51. Expected annual depreciation charges of £0.45m in 2021/22 are included in the operational cost budget. This is a reduction of £0.13m compared to the 2020/21 budget, reflecting the fact that costs associated with the settlement systems will be fully depreciated between quarter 4 2020/21 and quarter 4 2021/22.

Premises Costs

52. LCCC will continue to be based at Fleetbank House, Blackfriars, where it rents accommodation from the Government Property Agency (GPA), until June 2021. The total premises cost of the rental agreement is expected to remain at £36k per month until June 2021, which is inclusive of rent, council tax and service charge (which includes heating, water and power supply).

53. LCCC will vacate Fleetbank house in June 2021 as the building is being demolished. The GPA requires LCCC to relocate to 10 South Colonnade (10 SC), Canary Wharf, which also houses other government departments and public sector organisations such as Ofgem and HM Revenue & Customs (HMRC). The facilities at 10 SC are more modern compared to those at Fleetbank House and the rental charge is more reflective of latest rates. The total premises costs of the rental agreement at 10 SC is £43.75k per month, which is inclusive of rent, council tax and service charge (which includes heating, water and power supply).

54. In light of the increase in overall premises costs due to the move to 10 SC, LCCC has sought to reduce other related costs where possible. Work patterns have shifted to a hybrid model during lockdown, with a greater number of staff working from home for a greater number of days per week. This new work pattern is expected to continue after the Covid-19 pandemic has passed. Consequently, LCCC has reduced the number of desks it requires at 10 SC, resulting in a budget saving of £184k.

Contractor Costs

55. LCCC has sought to keep costs to a minimum by only employing contractors where doing so is more economical than employing full or part time staff. Contractors are expected to be needed in 2021/22 to provide peaks in workload for the legal team, to facilitate IT cloud migration and to provide cover for maternity leave, shared parental leave and for unforeseen events.

Other Costs

56. Other costs include stakeholder engagement and communications, training, travel and subsistence, printing and stationery, recruitment fees, insurance, bank charges, and subscriptions.
57. Insurance is procured on a commercial basis, using an insurance broker engaged under the Crown Procurement framework. The level of cover reflects the activity that LCCC expects to be undertaking in the next financial year.
58. The insurance market has hardened over the course of 2019 and 2020 as the market reacted to risks such as the Covid-19 pandemic. On the advice of its insurance broker, LCCC has reduced its level of cover in order to reduce the level of premium it has to pay for insurance. However, despite taking this step to reduce costs, LCCC still expects to pay a greater premium for its insurance cover in 2021 than it has in 2020 as the market is expected to remain challenging going forward. The level of cover LCCC requires will be kept under review in case further savings can be found.
59. LCCC has successfully used online events to maintain communications with stakeholders during the Covid-19 pandemic, which have proven popular and allowed for savings on costs associated with hiring buildings for face to face meetings. As the pandemic passes, LCCC intends to make use of face-to-face events again but will in parallel increase spend to improve its online offering on items such as website maintenance, portal development and more regular online events and workshops. There will also be increased demand on LCCC's stakeholder engagement function in the run-up to Allocation Round 4 – a large number of bidders is anticipated with the re-opening of Pot 1. LCCC takes a lead on this engagement and will need to invest in educational materials for new bidders and engaging with potential bidders throughout the year.
60. The "Other costs" line item also includes the MWh contingency budget, which is discussed in detail at paragraphs 62-63.

Electricity Settlements Company cost recharge

61. To maximise efficiencies in the operation of LCCC and ESC, ESC contributes at cost for its use of shared facilities, back-office functions and the staff it requires for its corporate functions and operational activities. The contribution that LCCC expects to apportion to ESC is netted off against LCCC's estimated budget, see Table 1. The recharge agreement is explained in more detail under ESC costs (see paragraphs 82-84).

Contingencies

62. 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 £0.75m contingency was therefore included in its 2020/21 budget (under 'other costs') to cover any reduction in volume of electricity supplied (e.g. due to warm weather).
63. The Covid-19 pandemic has resulted in a reduction in electricity demand. LCCC's forecasts predict reduced electricity demand will continue into 2021/22. To mitigate the risk of having to rely on BEIS for cash flow, a contingency of £1.5m has been included in the budget for 2021/22 and is classified within the other costs category.
64. A ring-fenced contingency of £2.1m was included in the 2020/21 budget to cover legal disputes. As LCCC signs more CfDs and projects with signed agreements start to build out, there is an increased risk of legal dispute. Taking into account costs of previous disputes and the increased risk of a dispute(s) arising in the future, a ring-fenced contingency of £3m has been included in the 2021/22 budget and is classified within the professional and legal fees category.
65. In the event that electricity demand is higher than expected, or in the event that a legal dispute(s) does not arise, the funds levied to cover these contingencies will be returned to suppliers at the end of the financial year.

Carbon Capture Use and Storage

66. As a part of Government's drive to deliver a Net Zero economy in 2050, BEIS consulted on business models for the support of CCUS power stations. One of the options is to use a form of the CfD under the powers taken in the Energy Act 2013, tailored to the sector. Were Government to move forward with this option, some preparatory work would be required on the part of LCCC in 2021/22, the cost of which would be a legitimate use of Operational Cost Levy income as the CCUS support would be via a CfD.
67. The work involved would include supporting BEIS in developing the contract and LCCC designing changes to their settlement system, activities that would be ancillary to LCCC's role as CfD Counterparty. LCCC estimates that this would add £0.2m to the operational budget for 2021/22. This contingent figure has been included in the budget above under "Professional services and legal fees". Were it to be needed, however, it would be spread over a number of line items, such as payroll and contractor costs as well as fees.

Low Carbon Contracts Company Levy rate

68. LCCC's operational cost levy is calculated on the basis of a gross electricity demand projection. For 2021/22, LCCC expects to use a projected gross demand of 273.63 TWh to calculate the levy rate. This forecast of gross electricity demand is based on a dedicated forecast model developed by LCCC. The model uses statistical techniques taking into account trends in electricity demand and embedded generation¹⁶; it also considers the long-term variability of weather.
69. A breakdown of the estimated operating costs, forecast electricity demand and corresponding operational cost levy rate for 2021/22 is provided in Table 5.

Table 5:

Year	Estimated costs £000s	Forecast Electricity Demand (TWh)	Levy rate (if applied from 1 April 2021) (£/MWh)
2021/22	20,847	273.63	0.0762

70. As set out previously, if it is not possible to complete the parliamentary process in time for the levy for 2021/22 to come into force by 1 April 2021, the current rate will continue to apply until such time as the regulations are amended.
71. If the amending regulations are delayed, in order that the estimated operational costs of LCCC can be collected in full, we would need to consider making an adjustment to the 2021/22 levy rate. Any necessary revision would be communicated in the Government response to this consultation.

Consultation questions	
1.	Do you have any comments on LCCC's estimated operational costs set out in this consultation document?
2.	Do you have any comments on the forecast electricity demand from which the £/MWh levy rates for LCCC are derived?

¹⁶ Embedded generation is generation that is connected to the distribution network rather than the transmission grid.

Electricity Settlements Company

72. The total estimated budget for the Electricity Settlements Company for 2021/22 is £7.472m, representing a £0.003m decrease on the £7.502m budget for 2020/21.
73. ESC has responded well to a number of challenges over the course of the last three years, in particular restarting the full range of its functions after the 11 month “standstill period” following the 2018 judgment of the General Court of the Court of Justice of the European Union regarding the state aid approval for the Capacity Market. During this standstill period, the UK Government was unable to award capacity agreements or make capacity payments. Following an in-depth investigation by the European Commission, the standstill period ended and by 20 January 2020 ESC had paid over £1bn to capacity providers in settlement of their deferred payments.
74. Over 2021/22 it is anticipated that ESC will take forward continuous improvements, including controls and automation in relation to settlement services, which were delayed in 2020/21 due to resource being allocated to restarting the Capacity Market. ESC is also expected to take forward work arising out of the 5 year review of the Capacity Market and at the same time work arising from regulatory change, such as market-wide half hourly settlement.
75. The Capacity Market has grown considerably since it was established, both in size and complexity. ESC currently manages 513 Capacity Market Units and this is expected to grow by 30% over 2021/22. The amount of capacity managed by ESC has grown from 0.6GW in 2016/17 to 54.5GW in 2020/21. Despite this growth, and further operational complexity arising out of a significant increase in the number of energy suppliers in recent years, costs have been held relatively steady to date. This reflects the fact that ESC is becoming more efficient as the number of agreement holders increases in the Capacity Market.
76. A breakdown of the estimated operational costs for 2021/22 is provided in Table 6, together with comparative figures for the 2020/21 budget. The subsequent paragraphs provide an explanation for each row of Table 6.

Table 6:

Description	Budgeted costs – 2020/21 £000s	Estimated costs – 2021/22 £000s
Professional fees	450	64
Metering and Settlement Services	3,620	4,242
Insurance	85	123
Depreciation	509	250
Low Carbon Contracts Company cost recharge	2,793	2,793
Other costs	45	
Total	7,502	7,472

Professional fees

77. The budget is required for external audit fees and ad-hoc consultancy.

Metering and Settlement Services

78. The costs of providing the metering and settlement services, as set out in Table 7, include the estimated cost of:

- administering and monitoring bid bonds and collateral;
- making payments in respect of Capacity Market auctions;
- collecting ESC's operational costs levy for 2021/22; and
- audit and assurance, including the verification of meter arrangements for providers whose capacity agreements are conditional on ESC approving their metering configuration and external audit costs for the operational settlement services.

79. The increase on the 2020/21 budget is mainly driven by a greater proportion of changes in the pipeline relating the capacity market. The Company has budgeted around £2.254m split between resource and other third party spend for this in 2021/22.

80. The increase on the 2020/21 budget is mainly driven by a greater proportion of changes to the settlement system in the pipeline relating to the Capacity Market. The Company has budgeted around £2.254m for this in 2021/22, split between resource and other third party spend.

Table 7:

Description	Estimated costs – 2020/21 £000s
Resource and subcontractors	2,876
Other third party and Assurance costs	1,366
Total	4,242

Depreciation

81. Expected annual depreciation charges of £0.250m in 2021/22 are included in the operational cost budget. These charges relate to the development and build of the Capacity Market settlement system funded by BEIS in previous years. The charges that are collected to cover depreciation costs will be paid to BEIS in the year that it is collected.

Low Carbon Contracts Company cost recharge

82. 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 year, together with an appropriate allocation of overhead costs (including rent, service charges, IT infrastructure, telephony support and other non-core assets). 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 charge. The recharged costs also include a proportion of corporate service costs, legal and professional fees, and the salaries of the ESC Board members. Although LCCC undertakes corporate activities on behalf of ESC, the ESC Board retains responsibility and accountability for the quality and cost of services provided.
83. This approach avoids ESC replicating functions that LCCC already has in place. LCCC must therefore have sufficient capacity in 2021/22 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.

84. For 2021/22 LCCC and ESC have agreed a recharge of £2.793m, which will be payable by ESC in monthly instalments. In general, this amount will remain fixed and will not be subject to amendment. However, if actual costs prove to be materially in excess of the estimated costs, LCCC will be entitled to amend the level of recharge accordingly. If costs prove to be materially less than estimated, resulting in actual cost savings to LCCC, the amount payable by ESC would be reduced accordingly.

Other costs

85. In addition to the above, there are a number of other directly charged costs which ESC will incur. These relate primarily to the annual audit fee for the completion of the statutory annual report, stakeholder management and ESC-specific assurance activity. The 2020/21 external audit fee was allocated to other costs, however, this has been moved to professional fees for 2021/22 to be consistent with LCCC.

Consultation questions

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|----------|------------------------------------------------------------------------------------------------------|
| 3 | Do you have any comments on ESC's estimated operational costs set out in this consultation document? |
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This consultation is available from: www.gov.uk/government/consultations/low-carbon-contracts-company-and-electricity-settlements-company-operational-costs-2021-to-2022

If you need a version of this document in a more accessible format, please email enquiries@beis.gov.uk. Please tell us what format you need. It will help us if you say what assistive technology you use.