ANNEX 11

SZC ECONOMIC LICENCE

This Annex sets out the Board's understanding of certain key provisions of the SZC Economic Licence as they relate to the Operator's ability to meet FDP Payments when due in accordance with the FAP.

1. BACKGROUND

1.1 A nuclear plant operator's electricity generation licence is granted by the Authority pursuant to the 1989 Act. In relation to Sizewell C, the generation licence will then be modified by the Secretary of State in accordance with the powers under Section 6 of the 2022 Act by the introduction of "special conditions for nuclear generator" (the electricity generation licence, as modified by the nuclear generator special conditions, together comprising the SZC Economic Licence).

1.2 The 2022 Act introduced the RAB funding model for new nuclear power generation projects based on the principles of certain regimes previously implemented in the United Kingdom (such as the Thames Tideway Tunnel), as further described in paragraph 5 of Annex 10 (*Legislative Background*). The SZC Economic Licence will commence on the Licence Modification Date and continue until the end of the Regulatory Period, being sixty (60) years from the Scheduled COD date of the Plant (unless extended or revoked pursuant to the terms of the SZC Economic Licence). This 60-year period aligns with the expected life of the Plant, noting the Funding Path in the FAP is also for 60 years.[1]

1.3 The SZC Economic Licence employs a "building blocks" approach to the calculation of Allowed Revenue, with the aggregate amount of the Allowed Revenue being constructed from various component blocks based on the detailed formulae set out in the SZC Economic Licence.

1.4 The Allowed Revenue component of central importance for the purposes of the FDP Implementation Company is the FDP Allowance Building Block, which is variably sized to cover (i) the amount of Contributions to Fund Assets in accordance with the FAP and (ii) operating expenses payable by the Operator to the FDP Implementation Company under the terms of the FDP Budget and Services Agreement. The FDP Allowance Building Block will be active from the time of First Criticality; prior to First Criticality, the initial costs of the FDP Implementation Company will be provided for under the Opex Building Block.

1.5 The FDP Allowance Building Block for each Financial Period will reflect the amount contained in the corresponding Draft Contributions Notice issued in accordance with clause 4.4 (*Contributions Notices will be produced annually up to the First Decommissioning Period*) of the FAP (in addition to the FDP Implementation Company's operating costs). It is therefore structured to mirror the Operator's funding obligations under the FAP, as adjusted from time to time by the Annual Review and Quinquennial Review process, in normal circumstances.

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[1] **Note**: The Funding Path in the FAP will respond to the extent that there is a delay to First Criticality such that the FDP Allowance Building Block under the SZC Economic Licence will be scheduled to be in effect for less than 60 years. See paragraph 6 of Part A (*Factual Background*) of Annex 7 (*Funded Decommissioning Programme*).

1.6 The Funding Path used to determine Base Case Contribution levels is recalibrated every five years pursuant to each Quinquennial Review. This five-yearly recalibration will in turn be reflected in the FDP Allowance Building Block as noted above. The Quinquennial Review process continues into the Disbursement Period; however, such Quinquennial Review in the Disbursement Period no longer recalibrates the Funding Path since the Operator's funding obligations under the FAP, and the term of the Regulatory Period under the SZC Economic Licence, are no longer extant in the Disbursement Period.

1.7 If, at the time that an Approved Contributions Notice is required to be provided under the SZC Economic Licence (1 November of each Charging Year), there is either:

(i) a dispute between the Operator and the FDP Implementation Company in relation to the quantum of a Draft Contributions Notice under the FAP; or

(ii) the Contributions Notice is unavailable due to an ongoing Quinquennial Review,

then, in the case of (i), the FDP Allowance Building Block shall be based provisionally on the undisputed portion of the Draft Contributions Notice, and, in the case of (ii), the FDP Allowance Building Block shall be based provisionally on the Approved Contributions Notice for the previous Charging Year. In each case, any resulting discrepancy from the finally agreed-upon Contributions Notice under the FAP will be reconciled by an adjustment to the Allowed Revenue on a two-year lagging basis pursuant to Part B (*K-factor true up*) of Special Conditions 30 (*Allowed Revenue during the Pre-PCR Phase*) and 48 (*Allowed Revenue during the Operations Phase*) of the SZC Economic Licence.

2. CHANGE IN LAW RELIEF

2.1 A key risk to the sufficiency of the Fund Assets identified by the Board in row B.8 of Annex 5 (*Risk Matrix Identifying Key Potential Risks to Shortfall in Funding the Cost of FDP Liabilities*) is a potential change to the regulatory environment that reduces the likelihood of the Operator receiving sufficient income to make the Contributions, and possible relief available under the SZC Economic Licence in these circumstances.

2.2 A Qualifying Change in Law (being: (a) a Discriminatory Change in Law, (b) a Specific Change in Law or (c) change in law or regulation which involves additional capital expenditure, operational costs (or savings) or results in a delay or impediment to reaching the Commercial Operations Date, which, in each case, was not foreseeable at or prior to the Licence Modification Date) will not be a Relevant Change of Circumstance where the change of law arises as the direct and proportionate result of: (a) the Authority exercising its discretion to amend the SZC Economic Licence conditions in accordance with its statutory powers; (b) the Authority exercising its powers under the SZC Economic Licence; (c) non-compliance with / breach of a related legal requirement by the Operator which is not remedied within a reasonable timeframe; (d) a failure by the Operator to act in accordance with Good Industry Practice; or (e) the Operator acting in a manner that may reasonably be considered as subverting the clear and objective intent of related legal requirements, such intent to be assessed by reference to publicly available information. A Qualifying Change in Law excludes changes in corporation tax law. An RCC Trigger Event also includes an unforeseen pandemic. In respect of either a Qualifying Change in Law or an unforeseen pandemic, to be an RCC Trigger Event it must result in an increase or decrease to Allowable Capital Spend or Allowable Operational Spend (above a *de minimis* amount).

2.3 The Authority pursuant to Part B (*Determination of a Relevant Change of Circumstance*) of Special Condition 44 (*Relevant Change of Circumstance during the Pre-PCR Phase*) of the SZC Economic Licence will then determine whether the RCC Trigger Event constitutes a Relevant Change of Circumstance and whether the Operator is eligible for an RCC Adjustment.

2.4 In the Operations Phase, change in law protection is provided by way of a CiL Adjustment where there is an Operations Phase QCiL (pursuant to Special Condition 61 (*Qualifying Change in Law or Regulation during the Operations Phase*)). The same exclusions specified in paragraph 2.3 above apply in respect of an Operations Phase QCiL, and the change in law must be either (a) a Discriminatory Change in Law, (b) a Specific Change in Law or (c) change that comes into effect during the Control Period which requires additional capital expenditure or operational costs (or savings). A CiL Adjustment will not be available where the change in law was foreseeable at the immediately preceding PCR or PR Determination and excludes changes in corporation tax law.

3. LIQUIDITY AND REVENUE SUPPORT

3.1 The Board has identified revenue and liquidity support mechanisms available under the SZC Economic Licence as an important mitigant to the risks of a temporary extended Plant outage as described in row B.9 of Annex 5 (*Risk Matrix Identifying Key Potential Risks to Shortfall in Funding for the Cost of FDP Liabilities*).

3.2 There are three (3) revenue and liquidity support mechanisms available to the Operator under the SZC Economic Licence:

(A) Significant Unavailability Event Revenue Support;

(B) Buyback of Power Revenue Support; and

(C) the Operational Incentives Adjustment.

3.3 **Significant Unavailability Revenue Support**

(A) If a Significant Unavailability Event is forecast to occur during a Charging Year, the Operator may submit an application to the Authority to request Significant Unavailability Revenue Support in accordance with Special Condition 58 (*Revenue Support*) of the SZC Economic Licence.

(B) Significant Unavailability Revenue Support is intended to provide an interim revenue top up where the Plant is unable to earn (as Recovered Revenue) at least 80% of the Allowed Revenue (disregarding incentives and adjustments) due to the occurrence of a Significant Unavailability Event.

(C) The support operates by way of an in-year exceptional adjustment to the Difference Payment, in circumstances where the Recovered Revenue earned would otherwise fall below 80% of the Allowed Revenue (disregarding incentives and adjustments), rather than requiring the Operator to await K-factor reconciliation to true up the discrepancy in the Charging Year$_{t+2}$. This enhances the liquidity position of the Operator considering that Differences Payments are otherwise fixed based on forecast electricity revenue in the Charging Year$_{t-1}$ and would only be reconciled in the Charging Year$_{t+2}$ pursuant to the K-factor mechanism.

(D) This effectively provides a floor in respect of the proportion of the Allowed Revenue that will actually be received by the Operator at 80% of the Allowed Revenue (disregarding incentives and adjustments) in a given Charging Year.

(E) Significant Unavailability Revenue Support is paid via the Revenue Collection Counterparty by way of an exceptional adjustment to the Difference Payments in accordance with Part F (*In-Year adjustment to Difference Payments*) of Special Condition 58 (*Revenue Support*) of the SZC Economic Licence.

(F) There is no clawback or repayment mechanism in respect of Significant Unavailability Revenue Support amounts, as these are essentially bringing forward Difference Payments to which the Operator would have been entitled in any case (by way of a K-factor adjustment in the Charging Year $_{t+2}$) and it would still suffer financial penalties through the Availability Incentive in Charging Year$_{t+2}$.

3.4 **Buyback of Power Revenue Support**

(A) If a Significant Unavailability Event occurs or is forecast to occur during a Charging Year that would require the Operator to purchase power from the electricity market in order to meet forward trades it has entered into in respect of electricity that was expected to be generated by the Plant, then it may submit an application to the Authority to request Buyback of Power Revenue Support in accordance with Special Condition 58 (*Revenue Support*) of the SZC Economic Licence (either in the year in which the Significant Unavailability Event takes place for an in-year adjustment to the Revenue Amount before Power, or in year t+1 for an adjustment to the Allowed Revenue in year $_{t+2}$).

(B) Buyback of Power Revenue Support is support provided to the Operator to help finance the cost of purchasing power to meet such forward trades and is calculated on the basis of the volume of energy sold forward and the discrepancy between the price achieved in the forward trades and the market price at the time of buyback.

(C) An in-year application for Buyback of Power Revenue Support is paid via the Revenue Collection Counterparty by way of an exceptional adjustment to the Difference Payments in accordance with Part F (*In-Year adjustment to Difference Payments*) of Special Condition 58 (*Revenue Support*) of the SZC Economic Licence.

(D) An application in respect of a Significant Unavailability Event that occurred in year t-2 will be included in the Allowed Revenue calculation for year t via the Buyback of Power

Revenue Support Building Block, in accordance with Part C (*Buyback of Power Revenue Support amount*) of Special Condition 58 (*Revenue Support*) of the SZC Economic Licence.

(E) Buyback of Power Revenue Support is aggregated together with any support provided pursuant to the Operational Incentives Adjustment (see paragraph 3.5 below) to calculate the Liquidity Support Amount.

(F) The Liquidity Support Amount is limited to 50% of the previous three (3) years' worth of Allowed Revenue, disregarding incentives and any revenue support amounts (being the Revenue Support Cap). Therefore, the amount of Buyback of Power Revenue Support is limited to the Revenue Support Cap, less any Liquidity Support Amount outstanding for repayment at the time of the calculation.

(G) The Liquidity Support Amount (being the aggregate amount of any Buyback of Power Revenue Support and/or Operational Incentives Adjustment amounts) will be repayable by the Operator to the Revenue Collection Counterparty in subsequent Charging Years in accordance with the Liquidity Support Repayment Building Block set out in Part E (*Liquidity Support Repayments*) of Special Condition 58 (*Revenue Support*) of the SZC Economic Licence.

(H) The Liquidity Support Repayment Building Block is a repayment block that calculates the clawback of payments in respect of the Liquidity Support Amount (rather than amounts due to the Operator as Allowed Revenue). While there is any Liquidity Support Amount outstanding, the repayment building block requires an amount equal to the lesser of: (i) the outstanding Liquidity Support Amount, and (ii) 25% of the Allowed Revenue (disregarding incentives and any revenue support amounts) to be deducted from the Allowed Revenue, subject to the OIA Floor as set out in paragraph 3.5 below.

3.5 **Operational Incentives Adjustment**

(A) Under Special Condition 59 (*Operational Incentives Adjustment*) of the SZC Economic Licence, the Operator is provided with liquidity support through the Operational Incentives Adjustment. This is a top up adjustment made to the Allowed Revenue during the Operations Phase to ensure that the Operator always receives revenue equal to 75% of the Allowed Revenue (disregarding any incentive adjustments and revenue support amounts), being the OIA Floor in any Charging Year.

(B) The Operational Incentives Adjustment is automatically engaged where the Allowed Revenue would otherwise fall below the OIA Floor as a result of the aggregate of the incentives adjustments and/or the Liquidity Support Repayment Building Block.

(C) The top up amount provided pursuant to the Operational Incentives Adjustment counts towards the Liquidity Support Amount and is therefore: (i) capped by reference to the Revenue Support Cap (in aggregate with Buyback of Power Revenue Support) as described in paragraphs 3.4(E) and 3.4(F) above; and (ii) repayable in accordance with the Liquidity Support Repayment Building Block as described in paragraph 3.4(G) above.

3.6 **Acceleration of Liquidity Support**

(A) If the Liquidity Support Amount is accelerated as per Special Condition 58 (*Revenue Support*) of the SZC Economic Licence (due to the Operator's insolvency or an issuance of a Discontinuation Notice by the Secretary of State), this amount will become immediately due and payable by the Operator to the Revenue Collection Counterparty.

(B) This accelerated Liquidity Support Amount may be deducted from the Allowed Revenue. While the OIA Floor provides some mitigation, if the Revenue Support Cap is exceeded, there is no specific provision in the SZC Economic Licence that would ring-fence or protect the FDP Allowance Building Block. Notwithstanding the foregoing, in the event of a nuclear insolvency the Allowed Revenue would continue to be paid in full (see Annex 12 (*Nuclear Administration and Nuclear Transfer Scheme*)) and, in any event, the SZC Economic Licence cannot be revoked while an FDP Shortfall is outstanding as described in paragraph 4 (*Revocation of the SZC Economic Licence*) below.

4. REVOCATION OF THE SZC ECONOMIC LICENCE

4.1 A critical mitigation to various scenarios identified in Annex 5 (*Risk Matrix Identifying Key Potential Risks to Shortfall in Funding the Cost of FDP Liabilities*) which would otherwise give rise to a revocation of the SZC Economic Licence (and thereby remove the regulatory funding source for payment of Contributions under the FAP) is the Partial Revocation regime set out in Special Condition 12 (*Revocation*) of the SZC Economic Licence. As explained further below, this regime prohibits the Authority from revoking the special conditions in relation to the payment of the FDP Allowance Building Block while any FDP Shortfall is outstanding.

4.2 The Authority will be *prima facie* entitled to revoke the SZC Economic Licence in the circumstances listed under paragraph 4 (*Revocation events*) of Special Condition 12 (*Revocation*) of the SZC Economic Licence, which includes Discontinuation, Permanent Early Closure and the enactment of a Nuclear Transfer Scheme, in addition to revocation rights under the standard electricity generation licence conditions (such as licensee insolvency). However, the SZC Economic Licence provides at paragraph 5 (*Revocation events*) of Special Condition 12 (*Revocation*) that at any time when there is an FDP Shortfall outstanding, the Authority's right to revoke the Special Conditions during the Regulatory Period will be limited to a Partial Revocation (i.e., excluding the Special Conditions relating to the Operator's entitlement to receive the FDP Allowance Building Block), unless the Secretary of State otherwise directs (and the right to revoke such standard conditions will be suspended).

4.3 The Authority will, having regard to the provisional values of the FDP Shortfall and FDP Final Amount provided by the Operator pursuant to Special Conditions 12 (*Revocation*) and 13 (*Funded Decommissioning Programme*) of the SZC Economic Licence, determine the Partial Revocation Period (which, pursuant to the SZC Economic Licence, is capped at ten (10) years).

4.4 Once the Partial Revocation Period is determined, Part E (*FDP Shortfall*) of Special Condition 13 (*Funded Decommissioning Programme*) of the SZC Economic Licence requires the Operator to propose modifications to the FDP, including the Funding Path in the FAP to ensure that there is no FDP Shortfall at the end of the Partial Revocation Period. The Partial Revocation Period may only take effect once the FDP modification has taken place pursuant to paragraph 8(a) (*Revocation events*) of Special Condition 12 (*Revocation*) of the SZC Economic Licence.

4.5 The Operator will have a significant role in this Partial Revocation process, in that it will be notifying the Authority of the FDP Shortfall and the FDP Final Amount and proposing modifications to the Funding Path in the FAP to ensure that there is no FDP Shortfall at the end of the Partial Revocation Period. There is accordingly a risk that the Operator's determination of these amounts and/or Funding Path turns out to be incorrect and that results in a Funding Shortfall at the end of the Partial Revocation Period. The mitigants against this risk include the following:

(A) the Operator is required to engage with the FDP Implementation Company and the Secretary of State under clause 33.1.1 (*Early Permanent Shutdown Decision and Partial Revocation*) of the FAP following an Early Permanent Shutdown Decision, providing both the FDP Implementation Company and the Secretary of State with the opportunity to provide their input; and

(B) the determination of the FDP Final Amount will be subject to approval of a modified FDP by the Secretary of State pursuant to Section 49 of the 2008 Act, rendering this ultimately a risk within the control of the Secretary of State.[2]

Ultimately, if there remains a Funding Shortfall at the end of the Partial Revocation Period, clause 5.6 (*Nuclear Administration*) of the NASTA would apply, such that the Secretary of State will be required to fund the Funding Shortfall. As such, the Board considers this risk to be well-mitigated, with any residual risk being within the control of the Secretary of State.

4.6 The Partial Revocation regime is subject to the Secretary of State's right to elect for the FDP Shortfall and any of the FDP Implementation Company's costs to be funded by taxpayers pursuant to the NASTA.

4.7 The Board notes that the FDP Final Amount is calculated based on nominal values (i.e., the year at the start of the Partial Revocation Period), whereas FDP Allowance Building Blocks will be calculated in money values of the Charging Year during the Partial Revocation Period. These are ultimately aligned because, pursuant to Special Condition 48(5) (*Allowed Revenue during the Operations Phase*), the FDP Allowance Building Block is adjusted by the Applicable CPIH Price Index Adjustment Factor. Special Condition 51(4) (*FDP Allowance Building Block during the Operations Phase*) also goes on to provide that the aggregate of the FDP Allowance

[2] **Note**: However, the Board notes that the calculation of the FDP Final Amount is not required to entail the level of financial audit and expert verification set out in the Quinquennial Review process in relation to the Funding Path (prior to revocation), and the FDP Final Amount is not subject to ongoing review and course corrections under the Quinquennial Review regime. The Board also refers to paragraph 9.3 of the Main Report – as discussed therein, the Board considers that it would have been helpful to have the Funding Outcomes Report regime apply in an early closure scenario to inform the FAP modification.

Building Blocks for the Charging Years during a Partial Revocation Period may not exceed the FDP Final Amount.

4.8 The FDP Final Amount does not expressly contemplate that any Emergency DTM Payments which may have been drawn (i.e., amounts required to be disbursed by the FDP Implementation Company to the Operator prior to the commencement of the Disbursement Period in order to meet unforeseen emergency costs) would be included in this amount. In a Partial Revocation scenario, if the Fund had been drawn prior to the FAP being modified to cover Emergency DTM Payments, this would be recognised when the FAP is modified ahead of the FDP Final Amount being set (and therefore captured by the FDP Final Amount). This is discussed further in row B.1 of Annex 5 (*Risk Matrix Identifying Key Potential Risks to Shortfall in Funding for the Cost of FDP Liabilities*) and paragraph 3 of Annex 16 (*Safety Critical Expenditure*).

4.9 The Partial Revocation process applies during the term of the SZC Economic Licence, which cannot be revoked or otherwise expire while an FDP Shortfall is outstanding. This will entitle the Operator to continued receipt of the FDP Allowance Building Block until any FDP Shortfall has been reduced to zero. Therefore, if there is an FDP Shortfall at the end of the Regulatory Period, such as: (i) where the Authority is continuing to make payment of FDP Final Amount instalments under a ten-year Partial Revocation Period commencing after year 50; or (ii) if significant unforeseen costs arise in the final year of operation, the SZC Economic Licence will continue to remain in place to provide the funding of such amounts.

4.10 The Secretary of State also has the option under paragraph 12(b) (*Revocation and transfer*) of Special Condition 12 (*Revocation*) of the SZC Economic Licence to extend the Regulatory Period.

5. FORCE MAJEURE

5.1 The Board has considered the operation of the force majeure regime under the SZC Economic Licence and has concluded that it does not have a material impact on the ability of the Operator to meet its payment obligations in respect of FDP Secured Liabilities under the FAP. For completeness, a summary of the mechanics is set out below.

5.2 Where there is a Force Majeure Event that results in a Delay Event to the Scheduled COD, the Operator may submit a Scheduled COD Extension Application or apply to extend the Longstop Date (a failure to achieve the Commercial Operations Date would otherwise incur financial penalties under the SZC Economic Licence). If the Authority determines such a Delay Event is a Qualifying Scheduled COD Delay Event or a Qualifying LSD Delay Event (as applicable), the Authority may amend the Scheduled COD or Longstop Date (as applicable) to such later date as it may specify in any direction (Parts B (*Scheduled COD Extension Application*), C (*Extension of Scheduled COD*) and D (*LSD Extension Application*) of Special Condition 42 *(Extensions to Scheduled COD or the Longstop Date*) of the SZC Economic Licence). If the Commercial Operations Date is not achieved by the Scheduled COD, there is a downward ratchet on the Return on Capital Building Block that the Authority can impose.

5.3 The Operator must achieve the Commercial Operations Date by the Longstop Date, otherwise they are in breach of paragraph 7 (*Timely delivery*) of Special Condition 2 (*General Provisions*) of the SZC Economic Licence. There is no entitlement for the Authority to revoke the SZC Economic Licence for a failure to achieve the Longstop Date. However, the Authority may take enforcement action, including by levying fines of up to 10% of annual turnover on the Operator.

6. RESTRICTIONS ON PERMITTED ACTIVITIES

6.1 The SZC Economic Licence includes certain restrictions on the activities of the Operator intended to limit the scope for it to incur additional liabilities that may lead to insolvency, and therefore provide an additional layer of mitigation (in addition to the protections under the Nuclear Administration regime described in Annex 12 (*Nuclear Administration and Nuclear Transfer Schemes*) and the insolvency remoteness of the FDP Implementation Company analysed in Annex 13 (*Insolvency Remoteness Analysis*)) in terms of any risk to the Fund Assets following Operator insolvency.[3]

6.2 Paragraph 3 (*Restriction on activities*) of Special Condition 5 (*Ringfencing)* of the SZC Economic Licence states that (unless a carve out applies) "*the licensee must not conduct any business or carry on any activity other than the Regulated Activities and/or the Regulated Business*". Further, paragraph 9 (*Availability of resources*) of Special Condition 5 (*Ringfencing*) of the SZC Economic Licence requires the Operator to have sufficient resources (including financial resources) to carry on the Regulated Business and Regulated Activities and comply with its obligations under the SZC Economic Licence and legal requirements.

6.3 Special Condition 10 (*Indebtedness*) of the SZC Economic Licence sets out certain restrictions on incurring Indebtedness. In particular, unless a carve out applies, the Operator must not undertake any Indebtedness without the consent of the Authority that is otherwise than: (i) on arm's length basis; (ii) on commercial terms; (iii) for a Permitted Purpose; and (iv) where such transaction also constitutes a Disposal of, or a Relinquishment of Operational Control over, any Relevant Asset or the grant of any mortgage, charge, or other form of security over any Receivable, or class or classes of Receivables, such transactions comply with the requirements of Special Condition 9 (*Disposals*) of the SZC Economic Licence.

[3] **Note**: The Board notes that these restrictions are not mirrored to the same degree in the FAP. See paragraph 3.5 of Part B (*Operator Insolvency*) of Annex 13 (*Insolvency Remoteness Analysis*) and row C.2 of Annex 5 (*Risk Matrix Identifying Key Potential Risks to Shortfall in Funding the Cost of FDP Liabilities*).