

ENERGY ACT 2013

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 2: Electricity Market Reform

Chapter 4: Investment contracts

Schedule 2, Part 1

Paragraph 1: Meaning of “investment contract”

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

payment obligation referred to in *sub-paragraph (1)(c)* must be an obligation on a party that is an electricity generator as defined in *sub-paragraph (3)* and the Secretary of State (see *sub-paragraph (4)*).

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

Paragraph 2: Varied investment contract

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

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

Paragraph 3: Confidential information

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

Paragraph 4: Interpretation for the purposes of this Schedule

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

Paragraph 5: Investment contract counterparty

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

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