
EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations impose a number of obligations on persons who supply electricity in Great Britain pursuant to an electricity supply licence (granted by the Gas and Electricity Markets Authority under section 6 of the Electricity Act 1989). Those obligations principally consist of requirements to make payments to the CFD counterparty, a person who is designated as such under section 7 of the Energy Act 2013. The payments are made to enable the CFD counterparty to meet its costs, and these include the costs it incurs in meeting obligations it has under CFDs. CFDs are contracts which the CFD counterparty must enter into by virtue of section 10 or 14 of the Energy Act 2013 with eligible generators (see the Contracts for Difference (Definition of Eligible Generator) Regulations 2014 which defines that term).

A CFD (or Contract for Difference) will set out circumstances when the CFD counterparty will have to make payments to the eligible generator who is a party to that contract, and for circumstances when that eligible generator will have to make payments to that CFD counterparty. It is therefore possible that there will be times when CFDs will not operate as a cost to the CFD counterparty, but instead will provide a benefit to it. In those circumstances that benefit will be passed on to electricity suppliers through a reduction in the payments they must make, or through payments these Regulations require the CFD counterparty to make to those suppliers.

Part 1

Regulation 2 contains definitions used in these Regulations. There are terms used in these Regulations which are defined in the Balancing and Settlement Code (as that code was in force on 1st April 2014). A copy of that code may be requested from Elexon Limited (4th Floor, 350 Euston Road London NW1 3AW). The Balancing and Settlement Code Company makes determinations under that code about the amount of electricity supplied in Great Britain, and these determinations are relied upon for various purposes in these Regulations. Every licensed electricity supplier is a party to that code.

Part 2

Regulation 3 sets out the obligation of electricity suppliers to contribute towards the costs of CFDs and connected agreements (which are contracts entered into pursuant to CFDs – this will include, for example arrangements with a financial institution who has an interest in a generating station which is the subject of a CFD) in respect of a quarterly obligation period. There are 4 such periods a year each lasting 3 months, the first such period commencing on 1st April 2015. The regulation also provides the obligation of the CFD counterparty to make payments to suppliers where a supplier's contribution in respect of a period is calculated as being a negative number.

Whilst this regulation sets out the principal obligation to make such payments, the obligation will actually be made by the making of interim payments and reconciliation payments. The final amount may not be known until 28 months after the period in respect of which they are due. This is because the amount of the payments are calculated by reference to the supply of electricity which may take up to 28 months after such supply occurred to be finally determined.

The contribution for a period is composed of contributions calculated in respect of each day in the period, and an additional contribution for the entire period.

Regulation 4 sets out the calculation for an electricity supplier's contribution in respect of a day in a quarterly obligation period. This is calculated on the basis of the payments the CFD counterparty must make under CFDs and connected agreements and the payments the CFD

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counterparty receives under those agreements where those payments are dependent upon the amount of electricity generated on that day.

Regulation 5 sets out the calculation for an electricity supplier's additional contribution for the period which is calculated on the basis of all payments the CFD counterparty must make and receives under CFDs and connected agreements which are paid during that period and which are not dependent upon the amount of electricity generated on a particular day.

Regulation 6 requires the CFD counterparty to determine a rate which applies to a quarterly obligation period. That rate will be the basis on which electricity suppliers make interim daily payments to that CFD counterparty during that period. The rate is set on the basis of the amount of money which the CFD counterparty believes it will need to make payments under CFDs during that period less the amount of money which it believes it will be paid under CFDs during that period. The rate is then arrived at by dividing that amount by the amount of electricity which the CFD counterparty estimates will be supplied during that period.

Regulation 7 sets out the basis on which the CFD counterparty must estimate the matters referred to in regulation 6 (such as the amount of money which it believes it will need).

Regulation 8 requires an electricity supplier who supplies electricity on a day in a quarterly obligation period to make a payment in respect of that day (an interim rate payment). The payment is calculated by multiplying the rate determined by the CFD counterparty by the amount of electricity supplied by that supplier on that day. The CFD counterparty must issue a notice to that supplier once the first information about electricity supply on that day is available (this will be available once the Balancing and Settlement Code Company has carried out the Interim Information Volume Allocation Run in relation to that day). The supplier must then pay the amount within 5 working days after the day that notice was issued. As a consequence the payments are likely to be daily payments (subject to how working days fall). The regulation also provides that interest must be paid on amounts which are not paid on time.

Regulation 9 provides for payments to be made by a supplier to that CFD counterparty, or by the CFD counterparty to that supplier where the Balancing and Settlement Code Company revises its determination of an amount of electricity supplied following the carrying out of an Initial Volume Allocation Run or Reconciliation Volume Allocation Run. The payments are made for the purpose of ensuring that the amount paid by a supplier as an interim rate payment reflects, as much as possible, the amount of electricity actually supplied. These payments will not be made after the conclusion of a quarterly obligation period as amounts will be subsequently reconciled once every quarter.

Regulation 10 requires the CFD counterparty to calculate a "total reserve amount" to be paid to it in respect of a quarterly obligation period and the share of that amount which each supplier must pay (that supplier's reserve payment). The counterparty must make those determinations at least 3 months before that period.

The CFD counterparty will determine the total reserve amount by modelling how much money it would need to have during a period to meet all payments it might have to make under CFDs. Unlike its determination of the interim rate, which is done on the basis of its best (or central) estimate, this determination is based upon a probabilistic assessment of the amount it would need in 95% of possible cases. This therefore covers the amount that would be needed in many extreme scenarios, but not the most extreme scenarios.

Regulation 11 sets out the time by which a reserve payment must be made, which is either the 7th working day after the commencement of the period to which the payment relates, or where a reconciliation payment is to be made in that period, at the same time as that supplier must make a reconciliation payment. This is so that the amounts can be offset against one another so a supplier only has to make a single payment (or may receive a single payment).

Regulation 12 allows the CFD counterparty to vary an interim levy rate, and/or require a further reserve payment from suppliers where, after setting the rate and determining the total reserve amount, it later appears that it will not receive enough money to make all the CFD payments it must make during that period. The regulation also allows the CFD counterparty to reduce the

interim levy rate if it appears that it will receive significantly more than enough money to make CFD payments during that period.

Regulation 13 sets out the means for determining an adjusted interim rate. The rate is arrived at in the same manner as the rate determined under regulation 6, but taking into account such payments as have already been made and may be made before the coming into effect of the adjusted rate. An adjusted rate will not have effect before at least 30 days after that rate has been determined.

Regulation 14 sets out the means for determining an additional total reserve amount for a quarterly obligation period, and the share of that amount which each supplier must pay. An additional total reserve amount is arrived at in a similar manner to the total reserve amount. The same probabilistic assessment is made in respect of the payments which must be made by the CFD counterparty for as much of the that period as remains after the making of the determination. The determination should also take into account any payments which the CFD counterparty has failed to make during the period. A supplier will have to pay its share of the amount no earlier than 30 days after it has been notified of the amount it has to pay.

Regulation 15 makes provision for the CFD counterparty to calculate reconciliation payments which must be made by it to a supplier, or by that supplier to it. Reconciliation payments must be determined in respect of a quarterly obligation period once in every subsequent quarterly obligation and paid 90 days after the CFD counterparty has issued a notice which sets out the amount of that payment. This will happen 10 times, by which point the Balancing and Settlement Code Company will have carried out all reconciliation volume allocation runs in respect of every day in a quarterly obligation period.

Regulation 16 sets out the means for calculating a reconciliation payment. To calculate such a payment the CFD counterparty must calculate the CFD period contribution of a supplier using the latest data available. This is then compared against the total amount of payments under Chapter 2 and 3 which that supplier was required to pay to the CFD counterparty, and which were required to be paid by the CFD counterparty to that supplier. The difference between the two determines the amount and direction of a reconciliation payment.

Regulation 17 makes provision for the circumstances in which an electricity supplier defaults on a payment it was required to make. In those circumstances other electricity suppliers can be required to pay further amounts to cover the amount of that default (a mutualisation of that default).

Regulation 18 makes provision for the circumstances where, following a mutualisation of a default, the CFD counterparty is able to recover amounts from the supplier who defaulted in respect of that default. In those circumstances, suppliers who were subject to the obligation to pay in respect of that default must be paid a share of the amount recovered, and a share of any default interest which was paid in respect of that default.

Regulation 19 imposes a requirement on electricity suppliers to provide collateral in respect of their obligations under this Part. The amount of collateral which must be provided by a supplier is calculated by reference to the amount of electricity supply for a recent period of 21 days. A supplier may choose to provide collateral as cash or as letters of credit. As that requirement is calculated daily the requirement may fluctuate and electricity suppliers may have to provide additional collateral. Suppliers will also have to provide additional collateral where their collateral is used (“called”) by the CFD counterparty.

Regulation 20 makes provision about the terms of letters of credit which may be provided by electricity suppliers to meet their collateral requirement. The CFD counterparty may determine whether the terms of a letter of credit are appropriate. The regulation also makes provision about the required credit rating of a person issuing such a letter.

Regulation 21 contains provision about how collateral is called by the CFD counterparty. It may be called by the CFD counterparty when an electricity supplier fails to make a payment it is required to make under this Part. The CFD counterparty may then issues a notice to that supplier informing it that an amount of that supplier's collateral is called. This may trigger the requirement to provide further collateral. Where collateral was provided as cash this cash is treated as having been paid to the CFD counterparty and will discharge that supplier's obligations as a payment would have done. Where collateral was provided as a letter of credit, the obligations of a supplier

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will only be discharged where the person issuing the letter of credit has paid the CFD counterparty under it.

Regulation 22 allows an electricity supplier to request the return of collateral where the amount provided exceeds the amount of that supplier's collateral requirement at that time. The regulation also provides that any interest which has been earned on the holding of cash collateral by the CFD counterparty must be paid to the supplier who provided that collateral.

Part 3

Regulation 23 requires electricity suppliers to make operational cost payments to the CFD counterparty for the purpose of allowing it to meet its costs (apart from making payments under CFDs which are dealt with in Part 2). The payments are calculated by reference to the amount of electricity supplied on a day, and a rate specified in this regulation. The rate specified in this regulation was arrived at by dividing the anticipated annual budget of the counterparty and dividing by the expected amount of electricity to be supplied in the first operational cost period. This number was then rounded to 4 decimal places. This gives £0.0790 per megawatt hour. Payments must be made daily, except in relation to the first operational costs period (which runs from 1st January 2015 until 31st March 2015 – every subsequent period will last a year) where the sum of the payments for that period must be made after the CFD counterparty has given notice of the amounts of all the payments which are due in respect of that period, so they are, in effect, required to be paid by the same date which will be after the conclusion of that period.

It is anticipated that this regulation will be amended annually to vary the rate.

Regulation 24 makes provision about the circumstances where the CFD counterparty has received more in operational cost payments than the amount of its costs. In those circumstances the CFD counterparty must pay electricity suppliers any excess based on the amount of electricity supplied over the operational cost period.

Part 4

Regulation 25 makes provision about enforcement of the requirements of electricity suppliers under these Regulations. It enables the Gas and Electricity Markets Authority to deal with any breach of such requirements as if those requirements were, in effect, requirements under an electricity supply licence. It also provides for notices to be issued by the CFD counterparty where a supplier has breached a requirement to make a payment, or a requirement to provide collateral. In the case of a breach of a collateral requirement, a supplier will then have to provide that collateral as cash.

Regulation 26 enables an electricity supplier to dispute any determination made by the CFD counterparty. Determinations about an amount of electricity supplied which is determined by the BSCCo are excluded from this provision, as there are processes in the BSC for determining such disputes and once those disputes are determined, the results would flow through reconciliation.

Regulation 27 sets out the duties of the CFD counterparty in relation to the determination of disputes including the steps it must take if it accepts a dispute. It also makes provision dealing with the effect of determinations made following the determination of a dispute.

Regulation 28 imposes some general duties of the CFD counterparty including a duty in relation to the collection of sums to be paid under these Regulations, and duties to keep electricity suppliers informed of their liabilities under these Regulations.

Regulation 29 makes provision about the issuing of notices by the CFD counterparty under these Regulations and the giving of notices by electricity suppliers, including provision about the giving and issuing of notices electronically.

Regulation 30 is provision enabling the CFD counterparty to set off amounts it has to pay to a supplier against amounts that supplier must pay.

Regulation 31 deals with the circumstances where an electricity supplier makes a partial payment such that not all of its liabilities at that time will be discharged by the making of that payment. In those circumstances that payment will be allocated to the outstanding debts of that supplier

in an order determined partially by this regulation and partially by the CFD counterparty in its discretion.

Regulation 32 prohibits the CFD counterparty from using payments from suppliers except for the purpose for which they were raised – either to make payments under CFDs (or connected agreements) or to pay for the costs of the CFD counterparty.

Regulation 33 deals with the circumstances where the CFD counterparty does not hold enough money to make all payments it is required to make under CFDs (or connected agreements). In those circumstances the amount that the CFD counterparty holds will be divided between the CFDs (and connected agreements) such that a proportional share of the total available may be paid under each CFD (and connected agreement).

Regulation 34 contains provision designed to have effect in relation to the terms of CFDs and connected agreements. The terms of CFDs and connected agreements are likely to include limited recourse provisions which prevent a party to those agreements from taking steps to recover more from the CFD counterparty than it has raised under these Regulations (or is available from other sources). Regulation 34 applies the apportionment provision in regulation 33 to such CFDs (or connected agreements) in accordance with those terms.

Regulation 35 sets out the rate of interest which applies to a requirement of a supplier to pay interest under these Regulations.

Schedule

The Schedule sets out the way the provisions of these Regulations will operate when there is more than one CFD counterparty designated. The Energy Act 2013 limits the circumstances when this may occur but these provisions are required if it was ever necessary for the Secretary to designate additional CFD counterparties. In those circumstances electricity suppliers would be required to contribute separately to the costs of CFDs in relation to each CFD counterparty.

The operational costs provisions in Part 3 would only apply in those circumstances to the CFD counterparty which was designated first however, as the rate for the levy under that Part is set out in these Regulations at the level it has been set at in order to recover the anticipated costs of that person and other arrangements would have to made to fund the costs of additional CFD counterparties until such time as these Regulations may be amended to provide for a levy for those costs.

A full impact assessment of the effect that this instrument will have on the costs of business and the voluntary sector is available from the Department of Energy and Climate Change at 3 Whitehall Place, London, SW1A 2AW and is published with the Explanatory Memorandum alongside this instrument on www.legislation.gov.uk.

Changes to legislation:

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