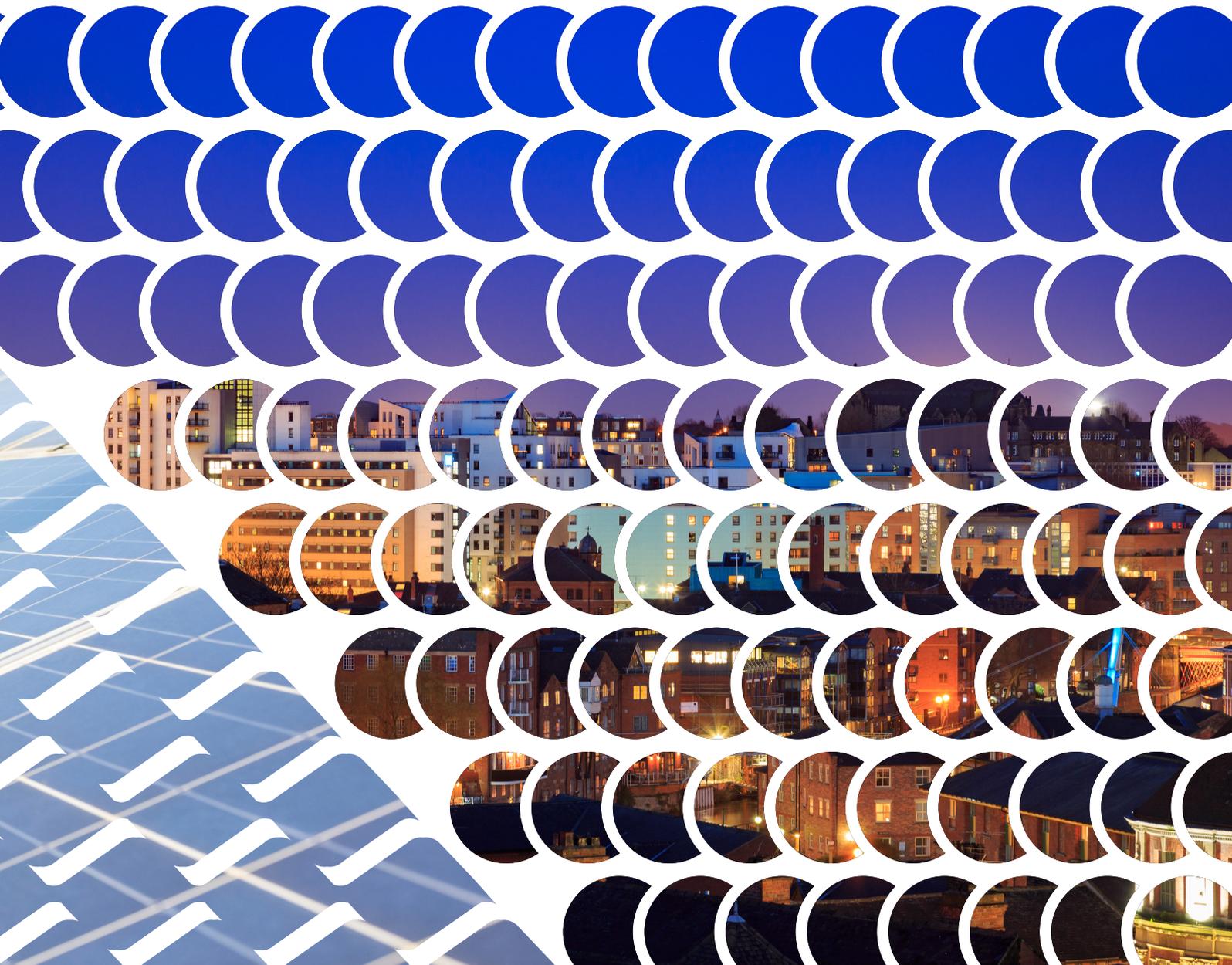


PROVIDING A RELIABLE, LOW COST AND **CLEAN ENERGY** **SYSTEM** TO THE CONSUMER

Annual Report and Accounts
for Electricity Settlements Company Ltd
2022/23



OUR VISION

is to accelerate the delivery of net zero.

The Electricity Settlements Company (ESC) is an operationally independent, not-for-profit private company wholly owned by the Secretary of State for Energy Security and Net Zero. The company carries out the key role of Capacity Market Settlement Body, supporting the delivery of the Government's objective of "ensuring that the country can deliver its goal to provide a reliable, low cost and clean energy system".²

OUR MISSION

is to shape and implement schemes which enable low-carbon investment at least cost to the consumer.

As Capacity Market Settlement Body, ESC is responsible for managing all financial transactions and associated assurances under the Capacity Market (CM) scheme, such as: credit cover; meter assurance; penalties; and payments to Capacity Providers.

ESC'S GUIDING PRINCIPLE

is to maintain market participants' confidence in the Capacity Market settlement process and minimise costs to consumers.¹

With effect from 7 February 2023, the name of our parent entity was changed from Department for Business, Energy & Industrial Strategy (BEIS) to Department for Energy Security and Net Zero (DESNZ). HM Treasury has specified for simple arrangements to still refer to BEIS in the 2022-23 financial statements, but for the rest of this report our parent department will be referred to as DESNZ.



¹ ESC Framework Document available at <https://lowcarboncontracts.uk/corporate-governance>

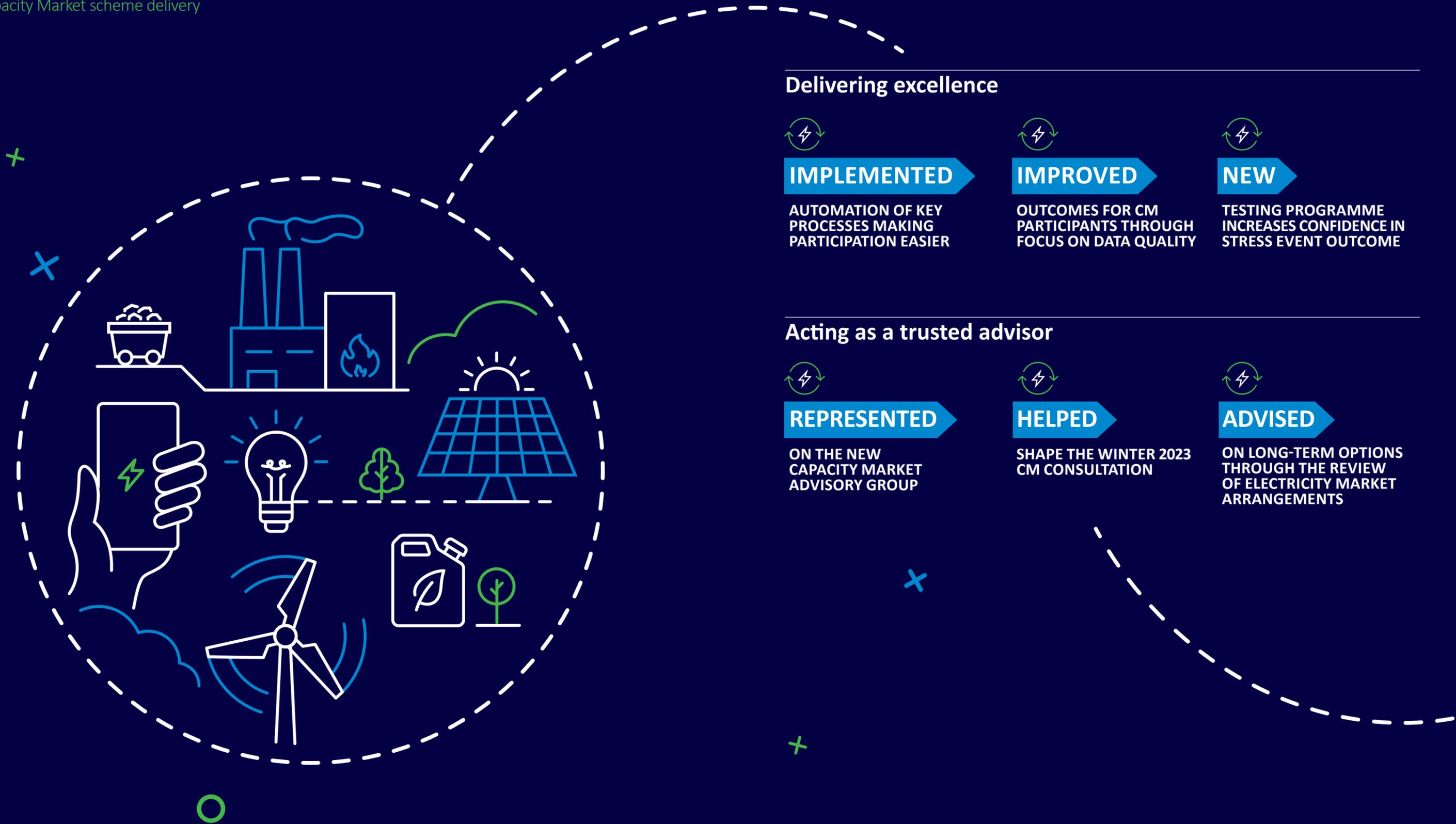
² BEIS Single Departmental Plan, updated 27 June 2019: [Withdrawn] Department for Business, Energy and Industrial Strategy single departmental plan, June 2019 - GOV.UK (www.gov.uk)

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Highlights for 2022/23

Capacity Market scheme delivery



Delivering excellence



IMPLEMENTED

AUTOMATION OF KEY PROCESSES MAKING PARTICIPATION EASIER



IMPROVED

OUTCOMES FOR CM PARTICIPANTS THROUGH FOCUS ON DATA QUALITY



NEW

TESTING PROGRAMME INCREASES CONFIDENCE IN STRESS EVENT OUTCOME

Acting as a trusted advisor



REPRESENTED

ON THE NEW CAPACITY MARKET ADVISORY GROUP



HELPED

SHAPE THE WINTER 2023 CM CONSULTATION



ADVISED

ON LONG-TERM OPTIONS THROUGH THE REVIEW OF ELECTRICITY MARKET ARRANGEMENTS

Chair's foreword

OUR DELIVERY EXPERIENCE IS KEY TO MAKING THE CM MORE WELCOMING TO NEW TECHNOLOGY



The vision of the Electricity Settlement Company's (ESC's) sister company (LCCC) is to accelerate the delivery of Net Zero. ESC has traditionally focused on the equally important task of securing the continuity of our electricity supplies, but the challenge now is to join these two imperatives in the drive to deliver a completely decarbonised power sector by 2035.

The key is securing low-carbon power that is also 'firm' – dispatchable, and able to fill the gaps that are left by variable sources such as wind and solar. Government is pointing to this with the consultation earlier this year on how the carbon factor can be brought into the Capacity Market (CM), which has been resolutely technology-neutral until now. Even before the structural changes that are being mooted can be brought in, however, there are ways of encouraging more low-carbon flexibility options into the CM.

So far, while some demand side response and an increasing amount of storage has participated in the CM, it is still the case that we need to do more to make the CM attractive to these types of resources. We are investing in automation to make participation easier, and helping developers of these technologies understand the benefits of participating in the CM. With clearing prices in this year's auctions at record highs, there are benefits to Capacity Providers in participating – and as more of them do so, there will be a welcome reduction in prices that will benefit consumers.

Government policy will drive fundamental change in the CM through the Review of Electricity Market Arrangements. We will play a two-fold role as that review is carried out. First, we will provide our knowledge of the CM on the ground, using data generated in running the system to help evolve the policy and the CM rulebook to deliver that change. Second, we will continue to refine and automate the existing system to make it more inclusive.

It's what we do – learn what works and what doesn't at the delivery sharp end, and bring that back to Government and the market to help make it better for everyone. I am proud of the attitude our staff bring to the continuous improvement of the CM, and of their dedication to serving the mission of net zero.

Regina Finn
Chair

Chief Executive's statement

SKILL IN DATA MANAGEMENT WILL MAKE THE CM MORE EFFICIENT



ESC has been driving forward a programme of continuous improvement to manage the operation of the Capacity Market (CM) in the face of increasing challenges to Great Britain's security of electricity supply. While again there have been no stress events to settle this year, margins are getting thinner and they are becoming more and more likely. The improvements we have made make the management of those events more efficient, and we are able to look to future delivery years with confidence. We don't rest on our laurels, however.

The number of Capacity Market Agreements we settle has been increasing, with 933 live agreements currently, made up of 5,499 components. To cope with this increase, we have been investing in automation and, crucially, making sure the data in the system is of suitable quality. As part of this, we are taking on more of the responsibility for metering to ensure we have confidence in the data we are processing. Our comprehensive continuous-improvement programme is resulting in greater visibility of assurance in the system from end-to-end.

All these improvements are key to getting more flexible and low-carbon technologies into the CM. These tend to be smaller and less tolerant of administrative overhead to participate, and we need them to participate – not only to bring down the carbon impact of firm power, but also to increase competition in the annual auctions. This year, the T-4 cleared at £63/kW and the T-1 at £60/kW, the former the highest and the latter the second-highest recorded for the respective auctions. So, it is important we do all we can to clear away barriers to participation for smaller and more innovative solutions.

Over the past few years, CM payments have been on a downward trend, totalling £680.5m this year, compared to £856.3m last year and £1,094.7m the year before. This will rise, however, as the recent higher clearing prices come into effect, underlining the need for greater participation.

Automation is therefore key to making the CM efficient and welcoming. However, it is also allowing us to have more data-based discussions about how capacity resources actually operate in the real world, rather than relying on theoretical assessments of what they should be doing. As more and more new technologies appear on the system, this evidence base will become more important to policy and rule-making debates, particularly as significant changes are considered under the Review of Electricity Market Arrangements. We look forward to contributing our hard-won knowledge to making our system run better and more efficiently.

All this is being done while continuing to keep operating costs under control. This year, the total net operating costs of the company were £5.2m (2021/22: £7.0m), and we will be returning £1.8m to suppliers (2021/22: £0.5m). This significant reduction can be attributed to the effect of LCCC starting to implement a number of new schemes through funding from the exchequer – overheads are being covered by more revenue streams and thus the call on each is less. The amounts LCCC has to recharge to ESC to carry out the CM functions are thus reduced, and this also benefits those paying the CM operating levy.

Neil McDermott
Chief Executive

Strategic report

Our role in accelerating the delivery of net zero

Our mission is to shape and implement schemes which enable low-carbon investment at least cost to the consumer.

- ESC is the **Capacity Market Settlement Body** responsible for **managing all financial transactions** and associated assurances under the CM scheme, such as: credit cover; meter assurance; penalties; and payments to Capacity Providers.
- ESC **maintains market participants' confidence** in the CM settlement process by providing guidance and communicating regularly through bulletins and our dedicated settlement portal.

Key outcomes in 2022/23

Capacity Market settlement outcomes ³	Total payments made by ESC to Capacity Providers	Total annual cost (including ESC settlement (i.e. operational) cost levy)	Operational costs as a percentage of total annual cost
Availability payments made to 48.4GW of capacity for delivery year 2021/22 and 52.7GW for delivery year 2022/23	£252.6m (for delivery year 2021/22) ⁴	£685.8m	0.8%
	£427.9m (for delivery year 2022/23 from October 2022 to March 2023) ⁴		



³ Figures may not reconcile due to rounding.
⁴ A Capacity Market delivery year runs from 1 October to 30 September the following year.

Performance against strategy

Overview of our role

The Electricity Settlements Company (ESC) is an operationally independent company wholly owned by the Secretary of State for Energy Security and Net Zero, which carries out the key role of Capacity Market Settlement Body. Our main function under the CM scheme is to perform the levy collection and settlement role set out in the CM Regulations. As part of this role, we also collect credit cover provided by applicants to CM Auctions, pay the

credit cover back to unsuccessful applicants, and process the credit cover of successful applicants in accordance with the CM Regulations. This credit cover is intended to provide a level of security for Capacity Providers' performance of their obligations under the CM Regulations.

In addition, as part of our role under the CM scheme, we undertake meter-assurance activities to check that

Capacity Providers are providing the capacity they are required to provide under their Capacity Agreements.

Our mission is to shape and implement schemes which enable low-carbon investment at least cost to the consumer. The illustration below depicts our three strategic objectives, against which we measure our performance.

Figure 1: ESC strategic objectives



Performance overview

We have continued to carry out our core CM business activities in what continued to be challenging times. During COVID-19 and the energy market crisis, our focus has been to inform and support generators and suppliers. Key initiatives we have worked on include:

- continuing to develop the data portal and the information available to our stakeholders

- better understanding our CM stakeholders, through qualitative interviews conducted as part of our annual stakeholder survey
- continuing to work on improvements to the settlement and wider end-to-end system.

We have achieved operational excellence in our settlements, with 99% of issued invoices (combined for Contracts for Difference – CfD – and CM), notifications and payments accurate and on time, and 100% of requested meter tests completed.

Auctions

In February 2023, the latest CM Auctions took place and some of the key takeaways are described below.

T1 Auction, delivery year 2023/24
The T1 Auction cleared at £60/kW/yr with a total of 5.783GW of capacity procured across 269 Capacity Market Units (CMUs). The total cost of this

auction is expected to be around £347m, or an additional cost of £4.80 to the average household electricity bill. The table below shows the mix of capacity procured, with battery storage increasing to 621MW compared to 385MW procured in the T1 Auction for the 2022/23 delivery year.

Type of capacity	Capacity procured
Gas	2.619GW
Demand side response	0.405GW
Coal	0.413GW
Nuclear	1.412GW
Battery storage	0.621GW
Waste	0.115GW
Pumped storage	0.000GW
Wind	0.065GW
Other sources	0.133GW

T4 Auction, delivery year 2026/27
This year's T-4 Auction is another where high clearing prices were recorded. The T-4 cleared at £63/kW/yr, with a total of 43GW procured compared to a previous

high of £30.59/kW/yr. This will result in a cost to the consumer of some £2.7bn for the 2026/27 winter, compared to £1.3bn for the 2025/26 winter. Again, battery storage is the big winner in the

T-4 Auction, with over 1GW of capacity procured – an increase of 192MW compared to the previous T-4. The battery storage capacity in this year's T-4 is split across 142 CMUs.

Type of capacity	Capacity procured
Gas	29.039GW
Interconnectors	6.854GW
Demand side response	0.925GW
Nuclear	0.964GW
Battery storage	1.284GW
Waste	0.576GW
Hydro	0.814GW
Pumped storage	1.790GW
Wind	0.068GW

Excellent scheme delivery

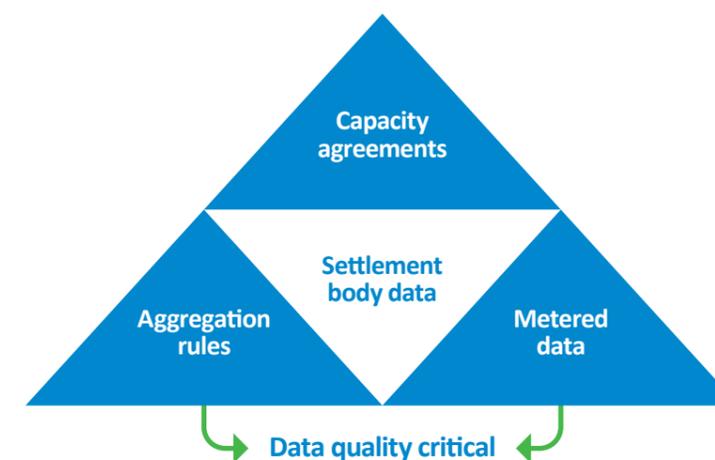
Automation and data focus

Our focus in 2022/23 has been to maximise the use of existing data to automate highly manual scheme processes and improve the overall level of data quality. We also did this to ensure the data used in potential stress events was validated and used appropriately.

Automation of Satisfactory Performance Day and Extended Performance process

Our development of a new Satisfactory Performance Day (SPD) and Extended Performance report, automating the process for Capacity Providers, went live in 2022. This uses existing data to satisfy requirements when there is already a known positive outcome, and we worked with the Delivery Body to enable this. We automated the SPD process fully in the 2022/23 delivery year following a proof of concept delivery in March 2022.

There have been several benefits to automating this highly manual process, a critical one being an increased focus on where issues with data exist. CM scheme data inputs are important to ensure any automation modelling is successful. If any inputs are erroneous, the automation will not work, and delivery partners and Capacity Providers have to use additional resources to resolve issues.



Improving data quality – initiatives

Metering aggregation

We have put in place initiatives to ensure accurate set-up. In the 2020/21 delivery year, metering aggregation was our largest missing data scenario, leading us to implement payment suspension for the 2021/22 delivery year. We continued this into the 2022/23 delivery year and successfully achieved 96% set-up by delivery start. We are now monitoring the next delivery year set-up in October 2023 and have reached over 90% set-up in April 2023 already (over 50% higher than last year). This is a huge leap in how we are managing workload and ensuring fixes are in place for future years, showing that data-quality initiatives have multi-year benefits.

Missing metered data

As we increased the level of metering aggregation submission, we had greater visibility of data-quality issues through SPD automation. For the 2021/22 delivery year, we identified that missing metered data was responsible for 16% of CMU issues during SPD testing and, in comparison, missing aggregation rules issues were less than 1%.

To help Capacity Providers, we have been monitoring CMU data flows for the current delivery year and implemented an email alert system and payment suspension mechanism when missing metered data flow issues exist.

Excellent scheme delivery

Stress-event preparation

Stress-event risks highlighting a focus on data issues and the importance of data quality:

It is a Capacity Provider's responsibility to submit all data for a stress event. Data issues would make the settlement of a stress event difficult in the timings allowed by the rules and regulations, but this data is not required for payments so has not affected the settlement-body processes. Through the data-quality initiatives and SPD process automation, we have seen a secondary benefit of mitigating unknown risks that are now visible, and improving the engagement and behaviour of Capacity Providers by actively flagging this to them.

Data utilisation: We have established a more efficient process, where we will now be using our own data rather than requesting data from Capacity Providers. This is a significant change and something that has been welcomed by the market. It will lead to more efficient penalty calculations if a stress event occurs. The only exception is relevant balancing services and interruptible data, which is an input required from Capacity Providers if a conflicting action exists and is validated by National Grid ESO.

Review of stress-event timings:

Following the stress-event testing programme we instigated in 2021, we found we had fewer days to provide results than it takes to get all the data from Capacity Providers and the Delivery Body (and appropriately validated in specific scenarios).

This was discussed with BEIS (now DESNZ), and led to a letter of comfort being sent to us, to ensure the prioritisation of accuracy in the calculation and issuing of penalties in the case of non-delivery in the CM.

Full details of this letter are available on the Government website – gov.uk – under the heading 'Issuing of penalties in the Capacity Market'. This change was also added to the January 2023 Capacity Market Consultation and will be laid for the next delivery year.

Through this stress-event preparation work, we have reduced administration for Capacity Providers and National Grid ESO, and improved overall checks and balances to use existing data in a better way.

We have also made the following system changes within EMR Settlement Ltd (EMRS) during the 2022/23 delivery year:

- removal of duplication risk of Suspended Capacity Obligation recovery
- additional fraud prevention activity on credit cover returns
- data-defaulting automation
- Line Loss Factor tool to reduce processing time
- metered data and payment-registration portal consolidation to create cost efficiencies.

Next steps

We will continue to identify processes within the CM that require streamlining and automation to reduce the administrative burden on the Capacity Provider. We will be investigating demand side response (DSR) and the involvement of flexibility technologies in the CM, engaging with industry and analysing DSR performance data as part of this process.

Stress-event preparation

We have developed a system stress event tool to replicate the event calculations for chosen Settlement Periods and Settlement Dates.

This replaces the mock stress-event activities that have been performed previously. In the coming months, we will send a breakdown of their data and metered data to Capacity Providers with active agreements for this delivery year. This is to allow each Capacity Provider to validate their Capacity Market Unit (CMU's) status and ensure their data accurately matches the information we hold.

As a result, we can provide greater data access to Capacity Providers and raise their awareness and understanding of their obligations and CMU status. Overall, the activities we have been undertaking will significantly reduce the risk of stress events being incorrectly settled, bringing much greater confidence to the system.

The future vision

Our work to improve data quality and visibility is providing a better experience for CM participants, but we want to go further to optimise the CM. Our data focus aligns with DESNZ's vision for the CM as part of a wider reform under the Review of Electricity Market Arrangements, making the electricity market fully aligned with the need to both decarbonise and be secure. An optimised CM with fewer manual processes and handover points will support this wider aim – the scheme will be better able to support the new flexible low-carbon technologies that are necessary to complement variable renewables. We look forward to integrating this operational improvement process with the bigger policy programme.

In keeping with this optimising thrust, we look forward to completing the handover of some key CM functions from the EMR delivery body to ESC, aligning data and processes with the organisations best placed to handle them. This should further improve the user experience and support our wider vision of an optimised CM as an enduring part of the low-carbon power sector.

Open data

Our stakeholders, particularly suppliers, continue to ask for more data to be provided, and with greater granularity.

As part of LCCC's responsibility for managing CfDs and CM schemes, we handle a huge amount of data. As an Arm's Length Body (ALB) of the Government and a strong supporter of the Presumed Open recommendations of the Energy Data Taskforce, we aim to share as much data as we can, and in as useful a format as possible.

Building on our data portal⁵, launched in January 2021, we continue to develop our dashboards, making as much data as possible available as downloadable spreadsheets, JavaScript Object Notation (JSON) and Application Programming Interface (API) formats.

In the coming year, in line with the open-data agenda, we are planning to expand the amount of data published, continuously assessing whether the public benefit of releasing further information outweighs commercial confidentiality concerns. LCCC will engage with stakeholders before publishing data and information to discuss any concerns with confidentiality.

The data portal remains a good platform on which to continue expanding our data provision, both to meet (and ideally exceed) stakeholder expectations and to drive forward the general open-data agenda by role-modelling best-in-class data management, including provision.

Change delivery

Industry changes

CM changes for the period include Balancing and Settlement Code (BSC) modification P399, which resulted in the need to update some data-input interfaces to continue to support the CfD and CM schemes.

Service improvements

The underlying hosting infrastructure has been modernised and improved with future resilience in mind. The main CM service-improvement processes for the Auction Acquired Capacity Obligation and associated meter data have been improved. Additional data validation has been put in place with National Grid to improve data quality. CPI annual adjustments for T-4 agreements have now been automated.

Additionally, a new registration portal has been developed from the ground up, catering for CfD generators, electricity suppliers and Capacity Providers, thus benefiting all users of the CfD and CM schemes – this is called My EMRS. Industry feedback on this new portal has been positive and further improvements are planned for the coming year.

Settlement-system enhancements

LCCC has been implementing enhancements to our systems, many linked to improvements in data transfer and processing. As this has been a year with a relatively low volume of regulatory-driven change, more time has been spent on optimising and improving other operational processes.

Engaging with our stakeholders

Over the last year, we have engaged with stakeholders by hosting webinars that provide updates to the CM scheme and explain how to use data to improve scheme requirements. We want to further engage with Capacity Providers to gather views and support for our simplification and automation agenda.

We are pleased that 67% of Capacity Providers are satisfied with the performance of the LCCC and ESC functions under their Capacity Agreements, when asked in our annual stakeholder survey.

This year, we conducted qualitative interviews with some of our Capacity Providers to help us understand how we support them. The interviews concluded that there is a desire to engage with us more, whether that involves understanding Capacity Providers' expectations for the future or working with them to prepare for future risks. We are working on an engagement plan as a result of the feedback.

5. <https://www.lowcarboncontracts.uk/data-portal/>

Advisory services

Having been closely involved with the development of the Capacity Market Advisory Group (CMAG) through its lengthy gestation, we are pleased to be a (non-voting) member of the panel. Our involvement is two-fold. Firstly, we provide advice based on our accumulated experience of settling the CM, which helps CMAG members in their work recommending CM rule changes to Ofgem. Secondly, we promote opportunities for wider change and ensure the group's members and wider industry are aware of the change activity that is not just focused on changing specific rules.

In recent months, we have presented a new mock stress-event process, going live early in the 2023/24 financial year; this was created as a result of our stress-event programme. Additionally, we have put forward a proposal for greater secondary-trading visibility. This coincided with several specific secondary-trading CMAG rule changes. Our position has been, and will continue to be, to ensure change is deliverable in a timely manner. But it must also be the right change, and we should look at wider reviews rather than piecemeal change, where appropriate and feasible.

We have also supported BEIS/DESNZ in its policy-development thinking through our attendance of the monthly CM Policy Board, which is chaired by DESNZ and attended by National Grid ESO and Ofgem. One of the outcomes of this engagement was the 2023 Winter CM Consultation, in which we were able to support the development of DESNZ policy proposals. We were recognised for enabling change by advancing our data capability, especially in delivery assurance, with the changes to the SPD process.

As part of the Review of Electricity Market Arrangements, we are advising DESNZ on options to resolve some of the complexities in the CM Policy, thus making the scheme more desirable and fit for a net-zero future.



Financial overview

Capacity payments

The total amount of capacity payments in the financial year was £680.5m (2021/22: £856.3m).

The delivery year for the CM runs from 1 October to 30 September. The capacity payments for each delivery year are

summarised in the table below, by reference to each financial year.

Capacity Market delivery	FY 2022/23 £m	FY 2021/22 £m
T-4 Capacity Auction DY 2018/19	16.6	16.2
T-4 Capacity Auction DY 2019/20	15.0	15.0
T-1 Capacity Auction DY 2020/21	nil	0.4
T-4 Capacity Auction DY 2020/21	27.1	538.7
T-1 Capacity Auction DY 2021/22	40.2	55.1
T-4 Capacity Auction DY 2021/22	208.1	230.8
T-1 Capacity Auction DY 2022/23	202.3	nil
T-3 Capacity Auction DY 2022/23	171.2	nil
Total	680.5	856.3

We obtain the funds to make payments to Capacity Providers by charging electricity suppliers as set out in the CM Regulations, with the suppliers being obliged to pay their charges within five working days of receiving an invoice from us. We do not, however, under the CM Regulations, make capacity payments until 33 working days after the end of the relevant delivery month. This protects us against cash-flow timing issues.

Suppliers must lodge credit cover as security against their failure to pay amounts they are liable for. Where the credit cover is called upon and proves insufficient to cover the amount due from a particular supplier, the shortfall is 'mutualised' between the remaining suppliers (that is, the remaining suppliers have to make up the shortfall between them). As at 31 March 2023, the company held £21.5m in supplier credit cover (2021/22: £18.3m). During the year, £13.3m of supplier charge was mutualised to other suppliers (2021/22: £23.2m); this increase is due to the high energy prices forcing suppliers into administration.

The CM also places financial obligations on Capacity Providers. If a Capacity Provider does not provide the capacity

required, it may, in accordance with the CM Regulations, be obliged to pay us a penalty. If we receive penalty payments from Capacity Providers, we pass the money on to suppliers. There may also be circumstances where a Capacity Agreement is terminated in accordance with the CM rules. Where we receive termination fees, we pass these amounts on to the Government's Consolidated Fund through DESNZ Treasury.

Operational costs

Our day-to-day operational costs are funded by suppliers under the annual fixed 'settlement' or operational costs charges set by the Supplier Payment Regulations. The amount set out in the Supplier Payment Regulations is amended by Parliament, after public consultation, to reflect our operational costs for the relevant financial year. The amount is then divided between suppliers and charged to them according to their market share.

The total settlement costs charges for 2022/23 were fixed at £6.954m. For 2023/24, they are set at £7.382m and for 2024/25, at £7.734m. We have fulfilled our operational role within the budget set by the operational costs levy for 2022/23.

We apply robust financial management to ensure we collect the settlement costs levy in good time to meet our commitments to Capacity Providers.

We share resources with LCCC, and LCCC pays for them, with the proportion of the costs relating to the CM being recharged to ESC, as further set out in note 2.6 to the financial statements.

Our total net operating costs for the year were £5.2m (2021/22: £7.0m). As a result of our strong financial performance over the financial year, we will return £1.8m to suppliers for 2022/23 (2021/22: £0.5m).

Post balance sheet events

There are no post balance sheet events to be recognised or disclosed.

Significant accounting matters and key judgements in the financial statements

There are no other significant accounting estimates or key judgements to be recognised or disclosed.

Viability statement

The directors have assessed the viability and prospects of our company over the next three years. In doing so, they have undertaken a thorough assessment of our current position, the emerging and principal risks we face, and the potential impact of those risks on our future prospects and development (including those that would threaten our business model, future performance, solvency or liquidity). The directors consider us to be viable for at least three years, up to March 2026, as we have approved budgets for 2023/24 and 2024/25 – which, if a new budget for the following period is not approved by Parliament, would remain at the level set for 2024/25 while the CM scheme is running.

The financial arrangements relating to our company minimise the risk of us being unable to meet our liabilities. As set out in the preceding Financial Overview, we are not obliged to make payments to Capacity Providers unless and until we have the funds to do so, and the annual budget for our operational costs will roll forward each year until the passing of regulations sets a new budget. We also apply prudent financial management and robust financial forecasting and cash-flow procedures to ensure our operating costs are covered by the settlement costs levy.

As part of the strategic planning process, and in assessing viability, our directors have considered the regulatory and legal environment within which we operate, and do not foresee any changes that will significantly affect our finances within the viability period of three years referred to above. Our directors have also carefully considered the way we manage our principal risks, and have assessed the potential financial impact of the principal risks identified, and do not feel that these risks will bring into question our company's viability.

A significant risk that has been under review by our directors, when making their assessment of our viability, is the impact of fluctuating prices in the energy market due to geopolitical events, which are currently affecting suppliers and have forced some into administration. The rate of collections, recovery of levy and the potential for mutualisation are continually being monitored to mitigate any potential risk. In the event of a supplier failure, we firstly draw upon credit cover, which in the majority of cases is sufficient to cover any shortfall. After that, there are processes laid down in the regulations to ensure any shortfalls can be met through mutualisation between the remaining suppliers.

Based on their assessment, our directors have a reasonable expectation that we will be able to continue in operation and meet our liabilities as they fall due over the relevant period.

Risk management – principal risks and uncertainties

Part of the internal audit programme in 2021/22 involved a review of joint assurance, which assessed the cross-cutting CM risks across ESC, EMRS, and National Grid ESO. This framework is continuing to develop a wider risk-management approach. We use it to assess the risk interdependencies, and we have developed actions to improve cross-scheme management into strategic and operational deliverables. These deliverables will be reported through the appropriate governance mechanisms (for example, the Audit and Risk Committees) to ensure they are tracked to completion and deliver improved outcomes.

As part of the wider risk framework for LCCC, the Board formally reviews the material risks facing ESC and ensures they are appropriately managed by the Senior Leadership Team (SLT), with a focus on ensuring that management is alert to, and takes account of, any new or emerging risks. The Board retains ultimate responsibility for our risk-management framework, with oversight of the overall effectiveness of the risk-management programme being delegated to the Audit, Risk and Assurance Committee. We have an Assurance and Risk function to provide assurance over controls, including those to mitigate key risks. Assurance and Risk co-ordinates risk-management activity, with regular sessions held by SLT to review, scrutinise, and update strategic risk. As well as the regular updates to the Audit, Risk and Assurance Committee, strategic risk is also presented twice-yearly to the Board for review and discussion.

Our risk-management framework has continued to develop in 2022/23. A more concise Strategic Risk Register has been developed, and now has a more direct alignment to our strategy and operational-risk registers. This work also involved resetting our risk appetite in relation to these areas and identifying thematic actions across different risks.

At operational level, risk management is continuing to be enhanced with updating of the operational registers and further development of an enterprise risk approach, including clear escalation points and operational interdependencies. We will also be developing key risk indicators to assist with the materialisation of the identified risks. A quarterly review of operational risk is conducted alongside performance reporting and as part of the Heads of Teams forum. Risk appetite is now a more active measure, as we seek to differentiate between the risks and opportunities in how we deliver our strategy.

Our approach to risk management is further detailed in the corporate governance report on pages 27 to 28. The assessment of the most significant principal risks considered by the Board, and the corresponding mitigating controls, are set out below.

Strategic risks

Our overall risk landscape continued to evolve in 2022/23, particularly given the changes in the wider energy market and our growth strategy. Our refreshed Strategic Risk Register reflects changes in how some of these risks are managed, as well as further emphasis on opportunities and efficiencies. We have also been reviewing how we can develop new areas of business and how we manage the associated risks and opportunities. A summary of key risk activity and movement since August 2022 is provided below; where appropriate, a risk trend is provided. Further mitigations are in progress to ensure risks are managed in line with risk appetite, with target scores and timescales captured in the assessment of the risk.

Risk management – principal risks and uncertainties (Continued)

RISK	SUMMARY	RISK TREND (SINCE AUGUST 2022)
<p>Stakeholder reputation Our stakeholders may lose confidence in our ability to deliver existing work or to take on new schemes. We may also miss opportunities to enhance our reputation with stakeholders.</p> <p>We may not be able to effectively maintain or demonstrate our operational independence due to taking on new areas of work.</p>	<ul style="list-style-type: none"> A new Director of Strategy and Development has been appointed. A new Communication and Stakeholder Engagement Team has been created to enhance the stakeholder journey. This area of risk reflects the opportunities that are inherent in how we manage our stakeholder reputation. For example, we will face increased reputational risk as we commit to new areas of work, although effective delivery will potentially enhance our overall reputation and improve confidence. 	
<p>Funding Our funding arrangements may restrict us in terms of how we operate. This could affect our ability to effectively deliver new schemes and reduce our flexibility as an organisation.</p> <p>There may be issues with the sustainability of our funding approach in the future longer term.</p>	<ul style="list-style-type: none"> This also brings in a longer-term focus on how schemes will be funded in the future, linking closely to the new institutional landscape risk. As with the previous risk, there are inherent opportunities within this risk area too, linked to how we are structured and how we manage our funding to pursue longer-term objectives. 	
<p>Institutional landscape There may be wider changes in LCCC's role, resulting from changes in political prioritisation (e.g. outcomes of the HMT net zero review), as well as positive or negative impacts from the wider macroeconomic situation.</p> <p>There is a risk that LCCC's operating model (e.g. CfDs) is not perceived to be viable in the longer term. This may present a risk to our core objectives, but may also present opportunities to how we support net zero.</p>	<ul style="list-style-type: none"> This risk reflects the wider institutional landscape, our strategy, and our ambitions. We will review our institutional landscape on an annual basis to continue to assess risks and opportunities. There is a degree of scalability associated with this area in terms of what new schemes are managed, balanced against the delivery of existing schemes. During the year, there has been an upturn in risk likelihood due to the medium to long-term impact of external geopolitical activity. 	

RISK	SUMMARY	RISK TREND (SINCE AUGUST 2022)
<p>External market We are unable to anticipate, and respond effectively to, the competition and the complexity and volume of change in the market.</p> <p>There is wider structural market change (e.g. market consolidation, merchant capacity in renewables) that provides us with opportunities.</p>	<ul style="list-style-type: none"> Significant challenges have continued within the energy sector. In particular, market price and the potential for rolling blackouts across the UK during late 2022 and early 2023. We have worked closely with stakeholders to manage the impacts, as well as understanding how this affects our existing internal activities (e.g. settlements). This has resulted in an increase in the overall risk environment. We have engaged strategically with our existing stakeholders to explore and manage change to the CfD and Capacity Market, as well as being responsive to wider market change. Internally, we have further developed our Insights programme, driven by our Policy and Advisory Team, aimed at influencing public debate and our positioning as key advisors on Carbon Capture Usage and Storage (CCUS). 	
<p>Organisational model We do not adopt the right organisational structure and culture to effectively deliver our new strategy, including the balance of existing work and new business development.</p>	<ul style="list-style-type: none"> During 2022/23, we continued to recruit for new roles and rearranged some existing structures to align business activities more closely. This also links closely to the people risk, recognising the dependency between how we manage change and our retention rates. 	
<p>Scheme management and delivery We are unable to effectively deliver our obligations on existing schemes due to growing complexity of the schemes and our stakeholder interactions.</p> <p>We do not have adequate systems or processes in place to effectively deliver new schemes.</p>	<ul style="list-style-type: none"> This reflects the changes in volume on our existing schemes as we prepare for further CfD Allocation Rounds, as well as the potential for additional complexities within the Capacity Market. AR4 has been completed with positive feedback. Additionally, operational risk-management registers are now in place for both the CM and CfD. This also encompasses the wider risks of scheme fraud and error. 	

Risk management – principal risks and uncertainties (Continued)

RISK	SUMMARY	RISK TREND (SINCE AUGUST 2022)
<p>Settlements Our business model, systems architecture, and controls may not be fit for the future, resulting in inefficiencies and late or missed delivery of change.</p> <p>We are not effectively aligned with our external stakeholders to deliver an efficient and cost-effective settlements process.</p>	<ul style="list-style-type: none"> This risk has reduced and is relatively stable, as it reflects business as usual. There are significant strategic and financial implications for our company if this risk were to materialise. Effective management of this risk also depends on the inputs from different external stakeholders. Tri-party meetings with a formal structure are now operating to provide a Joint Assurance Framework with the external bodies, providing a wider view of scheme risk. 	
<p>People We do not have sufficient capacity or capability to deliver our strategy. We also may miss opportunities due to delays in obtaining the right skills.</p> <p>We may also fail to sufficiently engage existing staff within the context of business change, resulting in a potential loss of skills and knowledge.</p>	<ul style="list-style-type: none"> This risk relates to ensuring we have the right capacity and capabilities in the organisation to continue to deliver on our existing commitments, as well as for new schemes. During 2022/23, two directors were recruited: Director of Strategy and Development, and Director of Scheme Delivery. The Director of People and Organisation Development left, but the position is being filled on an interim basis. We have focused on developing our wider recruitment approach and managing retention challenges, against a backdrop of difficult market conditions (e.g. higher market movement following COVID-19). Further work has been undertaken on our Business Agility initiative, focusing on culture and engagement, as well as applying these principles across operational delivery. 	
<p>Cyber and information security We are subject to a cyber-security incident, resulting in potential disruption to business operations, as well as data loss, financial loss and reputational damage.</p> <p>There is a cyber-security incident at a key stakeholder or within our supply chain, resulting in loss of our data, our wider reputation or confidence in the schemes.</p>	<ul style="list-style-type: none"> The audit review actions have been completed during 2022/23. A follow-up review is scheduled for completion in early 2023/24. The risk has remained static since last year – but, reflecting the wider geopolitical risks at present, there is an increased likelihood of external cyber-attacks. These are under continuous monitoring. 	

EFFECTIVENESS OF OUR RISK MANAGEMENT AND INTERNAL CONTROLS



The Head of Assurance and Risk provides an annual report and opinion on the systems of governance, risk management and control operating within LCCC, based on the work undertaken during the year, knowledge of the business environment, and the work of other assurance providers (e.g. the National Audit Office). The Head of Assurance and Risk leads on each internal audit review, with co-sourced support from Evelyn Partners, as well as the NCC Group for specialist assurance on cyber security. Of particular note is that the previous Head of Assurance and Risk left LCCC in early September 2022, and there was a lengthy gap before a new Head of Assurance and Risk was appointed and joined LCCC at the end of December 2022.

Additionally, following on from the Joint Assurance Framework review completed in 2022, the actions have been split into strategic or operational deliverables. These have formed a tri-party project plan with defined delivery dates that are monitored and reported accordingly.

Signed on behalf of the Board.

Neil McDermott
Chief Executive
12 July 2023

Key areas reviewed in 2022/23 include:

- Company Scorecard
- Purchase to Payment
- Recruitment, Retention and Workforce Planning.

ASSURANCE

Key areas reviewed include: Change Scorecard, Purchase to Payment, Recruitment, Retention and Workforce Planning.

Environment report

We do not have any employees, and our role is performed by LCCC on our behalf. So we do not have any direct Scope 1, Scope 2, or Scope 3 emissions. We are, however, committed to achieving our sustainability objectives, and we work closely with LCCC regarding environmental matters. For more details, please see the environment report in the LCCC annual report.



Board of directors

This was the Board as at 12 July 2023, with the changes during the year shown on page 30.



Regina Finn
Board Chair

Nomination Committee (Chair)
Remuneration Committee (member)



Neil McDermott
Chief Executive Officer



George Pitt
Chief Financial Officer



Amanda Aldridge
Non-Executive Director

Audit, Risk and Assurance Committee (Chair)



Helen Lamprell
Non-Executive Director

Remuneration Committee (member)



Steph Hurst
Non-Executive Director

Audit, Risk and Assurance Committee (member)



Chris Murray
Non-Executive Director

Remuneration Committee (Chair)
Nomination Committee (member)
Audit, Risk and Assurance Committee (member)



Maxine Mayhew
Senior Independent Director

Nomination Committee (member)



Gerard McIlroy
Non-Executive Director

Audit, Risk and Assurance Committee (member)

Committee memberships are stated under each profile.
The three committees are: Audit, Risk and Assurance Committee; Remuneration Committee; and Nomination Committee.

Declan Burke, Shareholder-nominated Non-Executive Board Director and member of the Remuneration Committee served for the full financial year 2022/23. Declan resigned from the Board on 10 July 2023.

Directors' report

THE BOARD IS RESPONSIBLE FOR THE STRATEGY AND DIRECTION OF THE COMPANY



The directors present their annual report on the affairs of the company, together with the financial statements and auditor's report for the year ended 31 March 2023. The company's registered number is 08961281.

Board

The Board is responsible for the overall strategy and direction of the company. Details of the Board's composition are set out on pages 25, 29 and 30.

Directors and corporate governance

Full details of the directors and corporate governance matters are set out on pages 24 to 33.

Position of the company

Information relating to our strategy, and to our development, performance and future prospects are set out in the corporate governance report and strategic report.

Employees

We do not have any employees, and our role is performed by LCCC on our behalf. LCCC recognises that the commitment of its highly skilled and experienced workforce is key to efficiently and effectively fulfilling our functions and achieving our strategic objectives.

Payment to suppliers

We pay our suppliers according to the provisions of our contracts with them, subject to their compliance with their contractual obligations.

Charitable and political contributions

During the year, the company made no charitable or political contributions.

Results and dividends

We have prepared our 2022/23 financial statements according to International Financial Reporting Standards (IFRS). The audited financial statements for the year ended 31 March 2023 are set out on pages 42 to 55.

We are a not-for-profit company, with the payments we make to CfD generators being matched or 'counterbalanced' by the Supplier Obligation Levy we collect from suppliers. Our other costs (operational costs) are funded by the operational costs levy referred to on page 13. Any operational costs levy we collect that exceeds our requirement is refunded to suppliers. This refund is recognised through the financial statements and matched with the income collected. On this basis, the financial results for the year reflect a neutral profit position, that is, nil profit-nil loss. Consequently, we do not pay a dividend.

For a more detailed review of the results for the year and a more detailed explanation of the accounting profit, see pages 40 to 53 of the financial statements, and the strategic report on pages 6 to 19.

Directors' third party indemnity provisions

The directors have been granted an indemnity against liability in respect of proceedings brought by third parties, subject to the conditions set out in the Companies Act 2006. Such qualifying third-party indemnity remains in force as at the date of approving this directors' report.

Going concern

The directors have a reasonable expectation that we have adequate resources to continue to operate for the foreseeable future. The financial statements therefore continue to be prepared on a going-concern basis. The basis of this view is outlined in more detail in note 2.2 to the financial statements.

Directors' responsibilities statement

The directors are responsible for preparing the annual report and financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law, the directors have elected to prepare the company financial statements according to international accounting standards (conforming to the requirements of the Companies Act 2006) and in line with applicable law. Under company law, the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs, and profit or loss, of the company for that period.

In preparing these financial statements, the directors are required to:

- select suitable accounting policies and apply them consistently
- make judgements and accounting estimates that are reasonable and prudent
- state whether the applicable IFRS has been followed, subject to any material departures disclosed and explained in the financial statements
- prepare the financial statements on a going-concern basis, unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy, at any time, our financial position and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company, and hence for taking reasonable steps to prevent and detect fraud and other irregularities.

Each of the directors, whose names and functions are detailed herein, confirms that to the best of his or her knowledge:

- the financial statements, which have been prepared according to international accounting standards (conforming to the requirements of the Companies Act 2006), give a true and fair view of the assets and liabilities, financial position and the profit or loss of the company; and
- the directors' report and the strategic report include a review of the development and performance of the business and the position of the company, together with a description of the principal risks and uncertainties we face.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on our website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The directors consider that the annual report and financial statements, taken as a whole, are fair, balanced and understandable, and provide the information necessary for the shareholder to assess the company's position, performance, business model and strategy.

Auditor

So far as each person who was a director at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing their report, of which the auditor is unaware. Having made enquiries of fellow directors and the company's auditor, each director has taken all the steps that they are obliged to take as a director in order to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

The company's auditor, the Comptroller and Auditor General (on whose behalf the National Audit Office acts) has expressed a willingness to continue in office. The Board and the Audit, Risk and Assurance Committee consider the performance of the auditor and assess their reappointment on an annual basis. A resolution to reappoint the auditor will be considered and proposed at the relevant time.

By order of the Board.

Allison Sandle
Company Secretary
12 July 2023

Corporate governance report

I AM PLEASED TO PRESENT OUR CORPORATE GOVERNANCE REPORT FOR THE YEAR



I am pleased to present our corporate governance report for the year, which describes our Board's general approach to corporate governance and how the UK Corporate Governance Code is applied within the company.

The Board believes that good corporate governance underpins the delivery of our strategy and objectives, and is committed to ensuring that high standards of corporate governance are maintained throughout our company.

I would like to thank all Board members for their support to me, and for their dedication and commitment over the year.

Regina Finn
Chair

Background to the company

Our company was established by the Secretary of State for Business, Energy and Industrial Strategy to be the Capacity Market Settlement Body. The Secretary of State is our sole shareholder.

While we were set up as an operationally independent private law company, we are also a governmental arm's length body, which is funded by and manages compulsory levies. Compulsory levies are normally classified as taxation, which effectively means we are managing public money.

Accordingly, as an independent private company and as an entity having responsibilities for administering of public money, we adopt the highest standards of governance and work to the highest standards of probity. We recognise the importance of operating with regularity and propriety, the need for effectiveness and prudence in administering public resources, and the need to secure value for public money. We also recognise the importance of embedding the seven principles of public life (selflessness, integrity, objectivity, accountability, openness, honesty and leadership) into our culture and operations.⁶

This corporate governance report outlines our governance structure and demonstrates how our arrangements align with the guidelines and principles set out in the UK Corporate Governance Code. Where any aspect of the Code has not been fully applied, an explanation is given below.

Our activities in the year are described in the corporate report and the strategic report.

Framework Document

Our main governing documents are our Articles of Association and our Framework Document⁷, which establishes the fundamental relationship between our shareholder and our company, is published on our website to provide transparency of the relationship.

The Framework Document reflects the basic tenet that functional independence is compatible with financial oversight of an arm's length body by its parent department. It makes it clear that we have day-to-day operational independence, subject to certain limited exceptions set out in legislation, our Articles of Association and the Framework Document itself.

The limitations on our independence are those which either:

- are common to Government-owned entities and necessary to satisfy Government and Parliamentary budgeting and accountability requirements; or
- provide our shareholder with specific controls in respect of policy implementation matters, which we are responsible for executing.

The Framework Document recognises that we are a separate corporate entity, and that our governance and decision-making processes flow through our Board, with our executives reporting to that Board.

The Framework Document states that, in carrying out our functions, activities and role, we will seek to maintain market participants' confidence in the Capacity Market process and minimise costs to consumers. This is known as the Guiding Principle. We recognise the importance of this Guiding Principle.

UK Corporate Governance Code

We are required by the Framework Document to comply with the UK Corporate Governance Code as it applies to small, quoted companies (other than Section E relating to relations with shareholders) or to specify and explain any non-compliance in our annual report. We also believe the adoption of the UK Corporate Governance Code is important as a means of recognising and embedding best practice in corporate governance.

The Board considers that we have complied in full with the Code, other than as explained in this corporate governance report. Any non-compliance is due to either the requirements of our shareholder, as reflected in our Articles of Association and the Framework Document, or to a timing matter relating to the Senior Independent Director or other Board appointments.

Role of the Board

The Board is committed to ensuring high standards of corporate governance. It accepts that good governance is based on the underlying principles of accountability, transparency and probity, and a focus on the sustainable success of our company over the longer term.

The Board is collectively responsible for our long-term success, and is ultimately responsible for our strategy, management, direction and performance. The Board sets our strategic aims, ensures the necessary financial and human resources are in place for us to meet our objectives, reviews progress towards the achievement of objectives, and reviews the performance of our management.

The Board establishes the values, culture, ethics and standards of our company, and sets the framework for prudent and effective controls, which enable risk to be assessed and managed. The Board has delegated authority to its committees to carry out the tasks defined in the committees' terms of reference. The committees are the Audit, Risk and Assurance Committee and the Nomination Committee. The written terms of reference of the committees are available on our website.

The Board has delegated the day-to-day management of the company to the Chief Executive.

Composition of the Board

The Framework Document and the Articles of Association state that our shareholder's approval is required for all Board appointments. They also state that our shareholder has the right to appoint the Chair, the Senior Independent Director and up to two shareholder-nominated directors.

Regina Finn is the current Chair of the Board and Maxine Mayhew is the current Senior Independent Director, since 13 August 2020.

At year end, the Board comprised ten directors, being two shareholder-nominated directors, six independent non-executive directors (including the Chair and the Senior Independent Director), the Chief Executive and the Chief Financial Officer. The shareholder-nominated directors at year end (and currently) were Declan Burke and Steph Hurst, both civil servants employed by DESNZ. They were appointed for the period required by our shareholder.

The six non-executive directors as at year end (and currently) are Regina Finn, Amanda Aldridge, Helen Lamprell, Maxine Mayhew, Gerard McIlroy and Chris Murray. Each of them was appointed with the consent of our shareholder, in accordance with the Framework Document and the Articles of Association. The term of office of each independent non-executive director is three years from the date of appointment or reappointment (as applicable, and may be extended).

Neil McDermott, the Chief Executive, was appointed as a director on 22 July 2014. George Pitt was appointed Chief Financial Officer on 13 August 2020.

An external recruitment consultancy was used in the appointments or original appointments of the Chair, Senior Independent Director, independent non-executive directors, Chief Executive and Chief Financial Officer. The search process was formal, rigorous and transparent, and the searches were conducted, and appointments made, on merit, against objective criteria and with due regard for the benefits of diversity on the Board. The shareholder-nominated directors are civil servants selected by our shareholder.

No recruitment consultancy we use has any other connection with the company.

The details of all Board members, any changes in the year and attendance at Board meetings, are listed on pages 30 to 31. All directors, with the exception of the shareholder-nominated directors, have written terms of appointment. These are available for inspection at our registered office during normal business hours.

The Chair was independent on appointment. The Board considers the Senior Independent Director and all non-executive directors, other than the shareholder-nominated directors, to be independent of the company.

The Board and its committees have an appropriate, effective and broad balance of skills, experience, independence and knowledge, which enables them to discharge their respective duties and responsibilities effectively. An annual review of the skills of the Board has been undertaken to ensure they are the skills needed to support our company as we evolve.

New directors receive an induction programme and additional training, tailored to their individual needs.

Board changes

Please see the table on page 30.

6. The 7 Principles of Public Life, available at <https://www.gov.uk/government/publications/the-7-principles-of-public-life/the-7-principles-of-public-life-->

7. Framework Document available at <https://www.lowcarboncontracts.uk/sites/default/files/publications/Electricity%20Settlements%20Company%20Framework%20Document%20-%20August%202014%20-%20Signe....pdf>.

Corporate governance report

(Continued)

Board governance

The Board meets sufficiently regularly to discharge its duties effectively, generally several times a year (with additional ad hoc meetings as required).

The Board met six times in 2022/23 and also held a separate strategy meeting in February 2023.

The following summarises the Board's main activities over the course of the year:

- Business performance and oversight – including receiving regular updates during the year on how the business is performing against its business plan, budget, strategic priorities and KPIs.
- Strategy and progress – participated in the annual strategic workshop, also attended by senior management, to set a new long-term strategy. The Board also reviewed the results of the annual industry stakeholder survey and the lessons to be learned from it, and received strategy updates during the course of the year.
- Risk and opportunity – reviewed the principal risks faced by the company and the actions being undertaken to mitigate against these risks, including in relation to cyber and information security.
- Audit and annual report – reviewed the annual report and considered matters such as the reappointment of the external auditor.
- Governance and compliance – reviewed the results of an independent annual Board evaluation and internal committees evaluation. Further information about the evaluation process can be found on page 38.
- Capacity Market – oversight and consideration of issues relating to the Capacity Market.
- Settlement – reviewed matters relating to the outsourced settlement services and proposed improvements in the future period.

The Chair has held a meeting with the non-executive directors without the executives being present. The non-executive directors, led by the current and former Senior Independent Director, have met without the Chair and executive directors being present, to discuss matters such as the appointment of the Chair or executive directors.

We record details of the directors' interests in a register, and review them at each Board meeting. We have procedures in place to ensure any actual or potential conflicts of interest are appropriately declared and managed. Directors are required to declare any actual or potential conflict of interest to the Board and to the Company Secretary as soon as they arise. No such conflicts of interest were identified in the financial year 2022/23.

The Board is supplied in a timely manner with the appropriate information, of the required quality, to enable it to discharge its duties effectively and properly. The Chair, Chief Executive and Company Secretary have review processes in place to ensure the quality of the information provided to the Board and its committees. The Board and committees have concluded, after assessing the question as part of their annual evaluation processes, that they were being provided in a timely manner with appropriate information of the required quality. Board members have access to the Company Secretary, and to independent legal advice, if they need it.

There is a formal schedule of matters specifically reserved for the Board. In high-level terms, the day-to-day management of the company is delegated to the Chief Executive and senior management with the matters reserved for the Board including:

- setting and approving the company's strategy
- responsibility for our leadership
- approving our financial statements
- approving (subject to shareholder consent) our annual business plan and budget
- monitoring and overseeing risk management, financial reporting and the system of internal control
- overseeing our operations
- approving financial commitments over specified monetary thresholds
- setting the terms of reference for the Board committees.

The main roles and responsibilities of the Chair, Chief Executive, Senior Independent Director and non-executive directors are summarised in high-level terms below. There is a formal document, approved by the Board, setting out the division of responsibilities between the Chair and the Chief Executive, which is reviewed annually.

The Chair:

- provides clear and effective leadership to the Board
- is responsible for maintaining high standards of operation and governance
- is responsible for promoting a culture of openness and constructive debate by facilitating the effective contribution of the non-executive directors
- facilitates the effective contribution, and encourages the active engagement, of all members of the Board
- ensures the annual evaluation of the performance of the Board, its members and its committees
- ensures constructive relations between the executive and non-executive directors
- speaks on behalf of the Board and represents the Board to our shareholder
- manages the business of the Board, including its agenda, and ensures adequate time is available for the discussion of all agenda items, in particular, strategic issues
- is responsible for ensuring the directors receive accurate, timely and clear information.

The Chief Executive:

- fulfils his responsibilities as Accounting Officer⁸
- leads the Executive Team in the day-to-day running of our company
- makes and executes operational decisions
- implements the strategy agreed by the Board
- ensures delivery within the annual budget
- ensures appropriate internal controls and risk-management processes are in place

- maintains the appropriate dialogue with the Chair and the Board
- facilitates effective communication to our shareholder and external stakeholders, including service providers, industry parties, regulatory bodies and governmental authorities
- ensures our values are embedded in our operations and staff culture.

The Senior Independent Director:

- works alongside the Chair and provides a sounding board for the Chair
- is available as an intermediary to other directors when necessary
- leads the meeting(s) with the other non-executive directors without the Chair being present, including to appraise the performance of the Chair.

Non-executive directors:

- ensure the Board fulfils its responsibilities, including in relation to strategy
- monitor the performance of management
- satisfy themselves as to the integrity of financial information and the strength of internal controls and our risk-management system
- include these responsibilities in their activities in relevant committees.

Board evaluation

The Board undertakes an annual formal and rigorous evaluation of its own performance and that of its committees and individual directors. The UK Corporate Governance Code recommends that Boards should be evaluated externally once every three years; our last independent Board evaluation was concluded in March 2022 and we have acted on recommendations arising from it. Also, recommendations from the annual internal Board evaluation have been analysed and are being acted on.

Each committee also separately undertakes an internal annual evaluation. In 2022/23, this was done through a questionnaire, with the results being discussed by the Board and the

committees. We concluded that the committees are working cohesively and effectively, and performing their role in a proper and appropriate manner with strong corporate governance in place.

The Chair also regularly reviews and discusses with each director their training and development needs. The Company Secretary also seeks to identify useful refresher training or industry familiarisation sessions for directors, including briefings on internal expertise areas (such as forecasting and settlement systems), industry developments, data protection, cyber security and compliance matters.

Audit, Risk and Assurance Committee

At year end, membership of the Audit, Risk and Assurance Committee (ARAC) comprised four non-executive directors, namely Amanda Aldridge (Chair), Steph Hurst, Gerard McIlroy and Chris Murray.

The Chair of the committee is a chartered accountant with current and relevant financial experience. The committee is composed of three independent non-executive directors and one shareholder-nominated non-executive director. The Framework Document, as permitted by the Articles of Association, requires the committee to include a director nominated by the shareholder.

The committee met three times in the financial year 2022/23, with meetings in June 2022, September 2022 and January 2023.

The Chief Executive (as Accounting Officer), Chief Financial Officer (or, as relevant, interim CFO), Head of Assurance and Risk, Company Secretary and the external auditor attended each meeting, and they have access to the Chair of the committee outside formal committee meetings. The Head of Assurance and Risk and the external auditor each meet with the committee, separately and informally, in advance of every scheduled committee meeting.

The committee's main responsibilities include:

- monitoring the assurance needs of the company in relation to risk, governance and the control framework
- reviewing the company's internal controls (including financial controls) and risk-management systems
- monitoring the integrity of the company's financial statements, and reviewing and reporting to the Board on significant financial reporting issues and judgements
- monitoring the effectiveness of the company's internal audit function
- making recommendations to the Board in relation to the appointment, reappointment and removal of the external auditor, and approving their remuneration and terms of engagement
- reviewing the independence and objectivity of the external auditor, and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements
- reporting to the Board, identifying any matters it considers need action or improvement, and making recommendations as to the steps to be taken
- reporting to the Board on how it has discharged its responsibilities
- undertaking an evaluation of its own performance.

The committee has reviewed arrangements by which anyone can, in confidence, raise concerns about possible improprieties in financial reporting or other matters.

The committee applies a policy on external-auditor independence to safeguard auditor objectivity and independence where the company's auditor have provided non-audit services. The external auditor has not provided any non-audit services in the financial year.

⁸ The responsibilities of an Accounting Officer are described in HM Treasury guidance "Managing Public Money". They include accountability for the activities of the company, the stewardship of public funds and the extent to which key performance targets and objectives are met.

Corporate governance report

(Continued)

In the financial year, the committee discussed the following matters:

- status of any significant accounting estimates, judgements and special issues
- external auditor report
- committee annual report on activities to the Board
- annual report – governance statement, accounts recommendation and report process
- Internal Audit Charter – annual review
- appointment of the external auditor and letters of engagement
- external audit plan
- risk deep dive – settlements
- internal audit activity, strategy and plan
- information security update
- committee annual evaluation
- review of the Delegated Authority Framework
- review of the ARAC terms of reference
- risk-management reviews and risk-register updates
- letters of representation.

The minutes of meetings are circulated to the Board.

There were no significant issues considered by the committee in relation to accounting treatments in the financial statements.

The company's main risks and related mitigating actions are set out on pages 15 to 18 of the strategic report. There have been no failures in, or breaches of, information security (other than minor or non-significant ones). There was one whistleblowing concern raised in the last year. This has been investigated according to the company's whistleblowing process and reported directly to the Chair of the Audit, Risk and Assurance Committee. The concern was not upheld.

The reappointment of the external auditor was approved by the Board in December 2022 on the recommendation of the committee. Due to timing differences with the ARAC meetings and receiving the National Audit Office (NAO) 2022/23 audit fee quote, it was not possible to receive approval from the ARAC before the Board meeting on 1 December 2022. The Board approved the reappointment, taking into account the fact that the Framework Document stated the strong presumption that the company would appoint the NAO as its auditor and also that shareholder consent was required for the appointment of any external auditor. It also noted the significant benefits of appointing the NAO based on value for money, the potential synergies with DESNZ's audit requirements and the NAO's understanding of both the complex environment within which the company operates and the wider government and public-sector context.

The committee assessed the effectiveness of the external audit process and provided its comments on the effectiveness to the external auditor. In addition, the Chair of the committee attended a BEIS audit committee, which provided an opportunity to learn from its experience and activities, and to discuss any common issues.

Nomination Committee

At year end, the committee comprised Regina Finn (Chair), Maxine Mayhew and Chris Murray.

All members of the nomination committee are independent non-executive directors.

The committee met three times during the year, in July 2022, November 2022 and March 2023. No member of the committee attended an agenda item in respect of which they had a personal interest or were discussed or appraised.

The committee's responsibilities include:

- regularly reviewing the structure, size and composition of the Board, including skills, knowledge, diversity and experience
- reviewing plans for the orderly succession for appointments to the Board and senior management, so as to maintain an appropriate balance of skills and experience within the company and on the Board and to ensure progressive refreshing of the Board
- undertaking an evaluation of its own performance.

These matters were discussed by the committee during the course of the year, with particular reference to the:

- composition, size and diversity of the Board, including a review of skills
- committee membership and tenure
- succession planning and training for the Board, executive directors and senior leadership
- succession planning below senior leadership level
- review independence and time commitment of non-executive directors
- review of the Nomination Committee terms of reference
- committee annual evaluation and review of previous evaluation actions arising.

The minutes of committee meetings are circulated to the Board.

Board and committee membership

The table below sets out the appointment dates of Board and committee members, along with details of those Board members who resigned in the year.

Director	Role	Board	Audit, Risk and Assurance Committee	Nomination Committee
Amanda Aldridge	Non-executive director	App. 02/04/2020	App. 02/04/2020	
Declan Burke	Non-executive director	App. 29/01/2020		
Regina Finn	Chair	App. 02/09/2019		App. 04/10/2019
Steph Hurst	Non-executive director	App. 29/01/2020	App. 29/01/2020	
Helen Lamprell	Non-executive director	App. 19/01/2021		App. 29/07/2021
Maxine Mayhew	Senior Independent Director	App. 13/08/2020		App. 01/10/2020
Neil McDermott	Chief Executive	App. 22/07/2014		
Gerard McLroy	Non-executive director	App. 27/10/2020	App. 03/12/2020	
Chris Murray	Non-executive director	App. 26/06/2018 (extended on 19 January 2021 for a further three years effective from 25 June 2021)	App. 18/07/2018	App. 03/12/2020
George Pitt	Chief Financial Officer	App. 13/08/2020		

Corporate governance report

(Continued)

Board and committee meetings

The table below shows the number of Board and committee meetings held during the year ended 31 March 2023 and the attendance of the individual directors. Please note that the table does not fully reflect the contribution made to our business by many of the

directors who have also attended other meetings (including with senior managers), attended briefings on various matters, addressed matters raised ex-committee, attended training and conferences, given talks to staff and attended events relating to our

business and activities during the year. In addition, generally members who could not attend a meeting provided comments on the papers for the meeting.

Member attendance record during 2022/23

	Board	Audit, Risk and Assurance Committee	Nomination Committee	Remuneration Committee
Number of meetings	7	3	3	5
Amanda Aldridge	7	3		
Declan Burke	7			5
Gerard McIlroy	7	3		
Regina Finn	7		3	5
Steph Hurst	6	2		
George Pitt	7			
Maxine Mayhew	5		3	
Helen Lamprell	6			4
Neil McDermott	7			
Chris Murray	7	3	3	5

Relations with shareholder and stakeholders

In accordance with our Framework Document, we maintain an appropriately regular dialogue with our shareholder. We have two shareholder-nominated directors, and have engaged in regular communication with industry and other stakeholders, including by stakeholder-engagement events, annual stakeholder surveys, regular newsletters and through our website. As a non-traded entity, we do not propose to have an annual general meeting.

Maintenance of a sound system of internal control

The Board has overall responsibility for our risk management and system of internal controls, and for reviewing their effectiveness. While retaining overall responsibility, the Board has established a clear organisational structure and well-defined delegated accountabilities for more regular and granular review of the effectiveness of the company's risk-management framework to the Audit, Risk and Assurance Committee and executive.

The key elements and procedures established to provide effective risk management and internal controls have been established. The systems in place are monitored and embedded and are as set out below:

Control and assurance environment

- The Board is responsible for the company's system of internal control and for reviewing its effectiveness. The system is designed to manage and, where possible, mitigate the risks facing the company, safeguard the assets and provide reasonable (although not absolute) assurance against material financial misstatement or loss. The Audit, Risk and Assurance Committee helps the Board discharge its responsibilities (as further described below and in the section headed Audit, Risk and Assurance Committee on pages 27 to 28).
- The Board, with the help of the Audit, Risk and Assurance Committee, has reviewed and is satisfied with the effectiveness of the company's systems of risk management and internal control.
- There have been no significant lapses in protective security.

Risk-management framework

The identification, mitigation and continual monitoring of significant business risks is the responsibility of senior management. The company's Strategic Risk Register is kept under regular review by the Senior Management Team and reported to the Board and Audit, Risk and Assurance Committee, with the top strategic risks and emerging risks receiving particular attention. Strategic risk is also discussed and monitored by the relevant Heads of Teams to ensure there is alignment and escalation of operational risk where appropriate. Operational risk registers are also maintained to identify local and emerging risks, allocating responsibility for appropriate monitoring and the implementation of mitigating controls. Risk-management processes are incorporated into our management and governance systems at all levels and form a part of our day-to-day operations.

- The Audit, Risk and Assurance Committee formally reviews the risk position at each scheduled meeting (in 2022/23, in May 2022, September 2022 and January 2023) and is updated on any significant risk matters that fall outside its formal review cycle. The committee considers the risk appetite of the company in relation to the principal risks and receives a completion report relating to the actions being undertaken to minimise and mitigate risk items.
- The Board reviewed the Strategic Risk Register in June 2022. The reports to the Audit, Risk and Assurance Committee and the Board include a report from management on the status of risk management and internal control, significant failings or weaknesses identified during the period (if any) and any actions taken to remedy any significant weaknesses (if relevant). The Board has reviewed the risk framework, with the assistance of the Audit, Risk and Assurance Committee, and is satisfied that a comprehensive and robust process for identifying, assessing and managing the company's principal risks is in place, including in respect of those risks that would threaten our business model, future performance, solvency or liquidity. Please see the more detailed risk report on pages 15 to 19.

Internal audit

We have an Internal Audit function that provides the Audit, Risk and Assurance Committee with independent, objective assurance regarding governance, risk management and internal controls, as part of our risk management and assurance regime. The Audit, Risk and Assurance Committee agrees a programme of internal audit work annually and reviews progress at each of its meetings. The annual audit plan takes into account current business risks. The Head of Assurance and Risk is supported by an external co-sourced partner to deliver the Internal Audit plan. The previous Head of Assurance and Risk left LCCC in early September 2022; there was a delay in appointing a replacement, but the post was filled and commenced in late December 2022.

Financial management and reporting

- We have a comprehensive strategic planning, budgeting and forecasting process, with the business plan (including the annual budget) being approved by the Board.
- Our operational costs are set out in the annual budget. The process for establishing the annual budget involves a number of stages, which provide challenge and accountability to ensure a robust and prudent budget is prepared, providing cost control and value for money for consumers. The draft budget, which can be for a single year or multiple, is reviewed by the Board and then submitted to our shareholder for further review. Our shareholder then undertakes a public consultation on the proposed budget. Subsequently, the settlement costs levy, which funds our budget, is laid before Parliament in the form of regulations.
- We operate robust financial-management processes to ensure we manage within our operational budget and do not exceed the settlement costs levy.
- An update on our progress, financial performance, budget forecasts and results is reported in the management information report submitted to each Board meeting.

Corporate governance report

(Continued)

- Senior management meet regularly with the Chief Executive and Chief Financial Officer to discuss business progress. Management accounts are reviewed regularly.
- There is shareholder oversight of financial management as set out in the Framework Document and the Finance and Reporting Letter from the shareholder to the company dated 1 August 2014, including monthly reporting.
- We are required to comply with the requirements set out in the Framework Document and the Finance and Reporting Letter, including compliance with the relevant requirements in HM Treasury guidance entitled 'Managing Public Money'.⁹

Operational

- The Senior Management Team meets on a fortnightly basis to review our operations, delivery, progress, issues and challenges. The Chief Executive has regular meetings with each member of the senior Executive Team.
- The Chief Executive and the Executive Team meet with appropriate regularity with our shareholder and other stakeholders.
- The Settlement Team and other functional teams work closely together to ensure the appropriate interfaces and communication in relation to Capacity Agreement settlement and metering assurance, with the governance, internal decision making and critical processes being documented.
- We report on significant matters relating to our operational activities at each Board meeting.
- The Board decides on matters falling within the schedule of reserved matters (for example, financial commitments over the specified threshold) or otherwise raised for decision.

Procurement

- We have a Procurement Policy that requires us to procure all goods and services in compliance with the relevant requirements in Managing Public Money, Cabinet Office controls and the public procurement regulations.
- We are required to carry out procurement and project appraisal objectively and fairly, using cost-benefit analysis and generally seeking good value for money.

Legal and compliance

- There is a system for monitoring and embedding compliance, including by company policies and procedures as well as training and guidance to support compliance (for example, relating to anti-bribery, whistleblowing, data protection, anti-money laundering, health and safety, and other legislative and good-practice requirements). External obligations are driven primarily by key legal, statutory and regulatory requirements.
- We expect the highest standards from all our personnel and our supply chain.
- We consider and implement the requirements of the Alexander Tax Review in relation to the retention of consultants.¹⁰

Treasury management

Our finance department:

- operates within policies agreed by the Audit, Risk and Assurance Committee
- uses its resources efficiently, economically and effectively, avoiding waste and extravagance
- uses management information systems to gain assurance about value for money and the quality of delivery and so make timely adjustments
- uses internal and external audit to improve its internal controls and performance.

Insurance

- Appropriate insurance is in place, with insurance cover being reviewed annually by the Board.



Neil McDermott
Chief Executive and
Accounting Officer
12 July 2023



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

10. HM Treasury, Review of tax arrangements of public sector appointees, May 2012: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/220745/tax_pay_appointees_review_230512.pdf

Remuneration report

The company's registered number is 08961281.

Employees

We do not have any employees. We perform our functions through LCCC.

Executive directors

Our executive directors are employed and paid by LCCC, and do not, therefore, receive any remuneration from us. LCCC charges us for its services, with an amount relating to the full cost of the executive directors forming a fair and properly allocated component of that charge. This arrangement is detailed in the 'recharge' arrangements described in note 2.6 to the financial statements.

Non-executive director fees

We do not pay the shareholder-nominated (or 'governmental') directors.

We obtained advice on remuneration for the executive directors and Senior Management Team in early 2022 from consulting firm, Korn Ferry. Korn Ferry is currently retained (as one of our panel of recruitment consultants) to help us recruit non-executive directors and senior executive staff. Korn Ferry has no other connection with the company.

No director is involved in deciding their own individual remuneration.

For reasons of synergy, operational efficiency and cost effectiveness, our Board of directors and that of LCCC are identical. As the fees paid to the remunerated non-executive directors relate to work for both companies, they are paid by LCCC, with a fair and properly allocated amount (generally 20%) being recharged to us by LCCC under the arrangements described in note 2.6 to the financial statements. This allocation is illustrated in the table on below. These fees (paid by LCCC with the relevant recharge to us) are the only form of remuneration received by the remunerated non-executive directors.

Non-executive directors' remuneration (audited)

Name	2022/23 fees ¹¹	Principal positions held elsewhere during 2022/23
Amanda Aldridge	12% of £30,000 2021/22: 20% of £30,000	<ul style="list-style-type: none"> • LCCC – non-executive director • Impact Healthcare REIT plc – non-executive director • The Brunner Investment Trust plc – non-executive director • The Letchworth Garden City Educational Trust (Formerly St Francis College Trust) – director and trustee
Declan Burke	£Nil (shareholder-nominated director – civil servant)	<ul style="list-style-type: none"> • DESNZ – director, Nuclear projects and Development • LCCC – non-executive director • British Nuclear Fuels Ltd – director • British Nuclear Group Ltd – director • BNFL (Investments US) Ltd – director
Regina Finn	£12,000 2021/22: £25,000	<ul style="list-style-type: none"> • LCCC – chair • Places for People Group Ltd – non-executive director • Places for People Homes Ltd – non-executive director • Places for People Living + Ltd – non-executive director • Places for People Ventures Ltd – non-executive director • Places for People Ventures Operations Ltd – non-executive director • Lucerna Partners Ltd – director • Chorus Homes Group Ltd – non-executive director • Chorus Homes Ltd – non-executive director • Cotman Housing Association Ltd – non-executive director • Derwent Housing Association – non-executive director • Motor Fuel Group Ltd – non-executive director
George Pitt	N/A	<ul style="list-style-type: none"> • LCCC – Chief Financial Officer and director • Pitt Consulting Ltd – director
Steph Hurst	£Nil (shareholder-nominated director – civil servant)	<ul style="list-style-type: none"> • DESNZ – Director, Energy Efficiency and Local Directorate • LCCC – non-executive director
Neil McDermott	N/A	<ul style="list-style-type: none"> • LCCC – Chief Executive and director

11. This column shows the only form of remuneration each non-executive director receives from ESC. ESC pays 12% to reimburse LCCC under the recharge arrangements with LCCC (other than in respect of Regina Finn) – see note 2.6 to the financial statements.

Remuneration report

(Continued)

Non-executive directors' remuneration (audited) continued

Name	2022/23 fees ¹¹	Principal positions held elsewhere during 2022/23
Chris Murray	12% of £30,000 2021/22: 20% of £30,000	<ul style="list-style-type: none"> LCCC – non-executive director APX3 Limited – director LOROS Commercial Innovations Limited – director LOROS (Leicestershire Hospice) – trustee Water Resources South East – chair MS Society – non-executive director
Maxine Mayhew	12% of £35,000 2021/22: 20% of £35,000	<ul style="list-style-type: none"> LCCC – non-executive director Hopkinsons of Lymm Limited – director Biffa Waste Services Limited – director Biffa Municipal Limited – director Biffa Environmental Municipal Service Limited – director Company Shop Limited – director
Gerard McIlroy	12% of £25,000 2021/22: 20% of £25,000	<ul style="list-style-type: none"> LCCC – non-executive director WTL Holdings Ltd – director West Transmission Limited – director Moyle Energy Investments Ltd – director West Transmission Financing plc – director Moyle Interconnector Limited – director Moyle Interconnector (Financing) plc – director Moyle Holdings Limited – director Mutual Energy Limited – director Premier Transmission Limited – director Premier Transmission Holdings Limited – director Premier Transmission Financing plc – director Interconnector Services (NI) Limited – director Belfast Gas Transmission Limited – director Belfast Gas Transmission Holdings Limited – Director Belfast Gas Transmission Financing plc – director Northern Ireland Gas Transmission Holdings Limited PRISMA European Capacity Platform GmbH – non-executive director
Helen Lamprell	12% of £25,000 2021/22: 20% of £25,000	<ul style="list-style-type: none"> LCCC – non-executive director Employers Initiative on Domestic Abuse – trustee Aveva Solutions Ltd – General Counsel and Company Secretary Aveva Group Plc – General Counsel and Company Secretary

Independent auditor's report

to the sole shareholder of Electricity Settlements Company Ltd

Opinion on financial statements

I have audited the financial statements of the Electricity Settlements Company Ltd ("the company") for the year ended 31 March 2023 which comprise the company's:

- Statement of Financial Position as at 31 March 2023;
- Statement of Comprehensive Income, Statement of Cash Flows and Statement of Changes in Equity for the year then ended; and
- the related notes including the significant accounting policies.

The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and the UK adopted International Accounting Standards.

In my opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2023 and of the result for the year then ended;
- have been properly prepared in accordance with the UK adopted International Accounting Standards; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on regularity

In my opinion, in all material respects the income and expenditure recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them.

Basis for opinions

I conducted my audit in accordance with International Standards on Auditing (UK) (ISAs (UK)), applicable law and Practice Note 10 'Audit of Financial Statements and Regularity of Public Sector Bodies in the United Kingdom (2022)'. My responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of my report.

Those standards require me and my staff to comply with the Financial Reporting Council's Revised Ethical Standard 2019. I considered the threat to my independence arising from the Engagement Director's long association with the entity. This is the sixth year that the Engagement Director has directed the audit of the company as Senior Statutory Auditor. The company's financial statements do not involve the making of any significant accounting estimates or judgements. On this basis I was satisfied, in consultation with others within the firm, that no safeguards were

required to mitigate the independence threat. In all other respects I am independent of the company in accordance with the ethical requirements that are relevant to my audit of the financial statements in the UK. My staff and I have fulfilled our other ethical responsibilities in accordance with these requirements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

The framework of authorities described in the table below has been considered in the context of my opinion on regularity.

Framework of Authorities

Authorising legislation

- Energy Act 2013
- Companies Act 2006

Parliamentary authorities

- Capacity Market Rules
- Electricity Capacity Regulations 2014

Shareholder, HM Treasury and related authorities

- Articles of Association
- Framework Document between the Secretary of State for the Department for Energy Security and Net Zero and the company
- Managing Public Money and Cabinet Office spending controls (to the extent they are applicable to the company)

Independent auditor's report

to the sole shareholder of Electricity Settlements Company Ltd

(Continued)

Conclusions relating to going concern

In auditing the financial statements, I have concluded that the company's use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

My evaluation of the directors' assessment of the entity's ability to continue to adopt the going concern basis of accounting included:

- reviewing the provisions of the legislation under which the company collects settlement costs levy it uses to fund operational costs;
- considering the internal business planning process relevant to operating costs; and
- considering additional funding options available to the company (relevant to operating costs).

I consider the key aspects of management's assessment to be their view that:

- there is minimal cash flow risk arising from the company's role as settlement body for the Capacity Market as a result of the statutory 'pay when paid' mechanism; and
- there are options available to the company to mitigate forecast cashflow and funding shortfalls.

The assertions made by management are consistent with the findings of my review of the Contracts for Difference (Electricity Supplier Obligations) Regulations 2014 and the company's framework agreement with the Department for Energy Security and Net Zero.

Based on the work I have performed, I have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the company's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

In relation to the entities reporting on how they have applied the UK Corporate Governance Code, I have nothing material to add or draw attention to in relation to the directors' statement in the financial statements about whether the directors' considered it appropriate to adopt the going concern basis of accounting.

My responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

Overview of my audit approach

Key audit matters

Key audit matters are those matters that, in my professional judgment, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditor, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team.

These matters were addressed in the context of the audit of the financial statements as a whole, and in forming my opinion thereon. I do not provide a separate opinion on these matters.

I have not identified any key audit matters throughout the course of my audit. In the prior year, I identified a risk in relation to the company's change of accounting system. The change of accounting system was completed in the prior year and I did not identify any associated risks for my current year audit.

The Audit, Risk and Assurance Committee report on matters that they considered to be significant to the financial statements is set out on pages 27 to 28.

Application of materiality

Materiality
I applied the concept of materiality in both planning and performing my audit, and in evaluating the effect of misstatements on my audit and on the financial statements. This approach recognises that financial statements are rarely absolutely correct, and that an audit is designed to provide reasonable, rather than absolute, assurance that the financial statements are free from material misstatement or irregularity. A matter is material if its omission or misstatement would, in the judgement of the auditor, reasonably influence the decisions of users of the financial statements.

Based on my professional judgement, I determined overall materiality for the company's financial statements as a whole as follows:

Materiality	£13.6 million
Basis for determining materiality	Approximately 2% of gross expenditure of £69 million (2021-22, 2% of gross expenditure).
Rationale for the benchmark applied	In my professional judgement, the users of the financial statements are most interested in gross expenditure, comprising operating costs and Capacity Market payments, on the basis that these are the costs which fall to energy suppliers and ultimately bill payers.

Performance materiality

I set performance materiality at a level lower than materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed the materiality for the financial statements as a whole. Performance materiality was set at 75% of materiality for the 2022-23 audit (2021-22: 75%). In determining performance materiality, I have considered the low level of uncorrected misstatements identified in the previous period.

Other materiality considerations

Apart from matters that are material by value (quantitative materiality), there are certain matters that are material by their very nature and would influence the decisions of users if not corrected. Such an example is any errors reported in the Related Parties note in the financial statements. Assessment of such matters needs to have regard to the nature of the misstatement and the applicable legal and reporting framework, as well as the size of the misstatement.

I applied the same concept of materiality to my audit of regularity. In planning and performing audit work to support my opinion on regularity and in evaluating the impact of any irregular transactions, I considered both quantitative and qualitative aspects that would reasonably influence the decisions of users of the financial statements.

Error reporting threshold

I agreed with the Audit, Risk and Assurance Committee that I would report to it all uncorrected misstatements identified through my audit in excess of £180,000 as well as differences below this threshold that in my view warranted reporting on qualitative grounds. I also report to the Audit Committee on disclosure matters that I identified when assessing the overall presentation of the financial statements

There were no unadjusted misstatements or disclosure matters to report.

Audit scope

The scope of my audit was determined by obtaining an understanding of the company and its environment, including the entity-wide controls, and assessing the risks of material misstatement.

Other information

The other information comprises the information included in the Annual Report, but does not include the financial statements and my auditor's report thereon. The directors are responsible for the other information.

My opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in my report, I do not express any form of assurance conclusion thereon.

My responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

If I identify such material inconsistencies or apparent material misstatements, I am required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work I have performed, I conclude that there is a material misstatement of this other information, I am required to report that fact.

I have nothing to report in this regard.

Opinion on other matters prescribed by the Companies Act 2006

In my opinion the part of the Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

In my opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements;
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements; and
- the information about internal control and risk management systems in relation to financial reporting processes, and about share capital

structures, in compliance with rules 7.2.5 and 7.2.6 in the Disclosure Rules and Transparency Rules sourcebook made by Financial Conduct Authority (the FCA Rules), is consistent with the financial statements and has been prepared in accordance with applicable legal requirements; and

- information about the company's corporate governance code and practices and about its administrative, management and supervisory bodies and their committees complies with rules 7.2.2, 7.2.3 and 7.2.7 of the FCA Rules.

Matters on which I report by exception

In light of the knowledge and understanding of the company and its environment obtained in the course of the audit, I have not identified material misstatements in:

- the Strategic Report or the Directors' Report; and
- the information about internal control and risk management systems in relation to financial reporting processes and about share capital structures, given in compliance with rules 7.2.5 and 7.2.6 of the FCA rules.

I have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires me to report to you if, in my opinion:

- adequate accounting records have not been kept or returns adequate for my audit have not been received from branches not visited by my staff; or
- I have not received all of the information and explanations I require for my audit; or
- the financial statements and the parts of the Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors remuneration specified by law are not made; or
- a corporate governance statement has not been prepared by the parent company.

Independent auditor's report

to the sole shareholder of Electricity Settlements Company Ltd

(Continued)

Corporate Governance Statement

The Listing Rules require me to review the Directors' statement in relation to going concern, longer-term viability and that part of the Corporate Governance Statement relating to the company's compliance with the provisions of the UK Corporate Governance Statement specified for my review.

Based on the work undertaken as part of my audit, I have concluded that each of the following elements of the Corporate Governance Statement is materially consistent with the financial statements or my knowledge obtained during the audit:

- Directors' statement with regards the appropriateness of adopting the going concern basis of accounting and any material uncertainties identified [set out on page 22];
- Directors' explanation as to their assessment of the entity's prospects, the period this assessment covers and why the period is appropriate [set out on page 14];
- Directors' statement on fair, balanced and understandable [set out on page 23];
- Board's confirmation that it has carried out a robust assessment of the emerging and principal risks [set out on page 31];
- The section of the Annual Report that describes the review of effectiveness of risk management and internal control systems [set out on page 31]; and
- The section describing the work of the Audit, Risk and Assurance Committee [set out on pages 27 to 28].

Responsibilities of the directors for the financial statements

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for:

- maintaining proper accounting records;
- providing the C&AG with access to all information of which management is aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
- providing the C&AG with additional information and explanations needed for his audit;
- providing the C&AG with unrestricted access to persons within the company from whom the auditor determines it necessary to obtain audit evidence;
- preparing financial statements, which give a true and fair view, in accordance with the Companies Act 2006;
- ensuring such internal controls are in place as directors determine are necessary to enable the preparation of the financial statements to be free from material misstatement, whether due to fraud or error;
- preparing the Annual Report, which includes the Remuneration Report, in accordance with the Companies Act 2006; and
- assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the entity or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

My responsibility is to audit and report on the financial statements in accordance with the applicable law and International Standards on Auditing (UK) (ISAs (UK)).

My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue a report that includes my opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Extent to which the audit was considered capable of detecting non-compliance with laws and regulations including fraud

I design procedures in line with my responsibilities, outlined above, to detect material misstatements in respect of non-compliance with laws and regulations, including fraud. The extent to which my procedures are capable of detecting non-compliance with laws and regulations, including fraud is detailed below.

Identifying and assessing potential risks related to non-compliance with laws and regulations, including fraud

In identifying and assessing risks of material misstatement in respect of non-compliance with laws and regulations, including fraud, I:

- considered the nature of the sector, control environment and operational performance including the design of the company's accounting policies
- inquired of management, the company's head of internal audit and those charged with governance, including obtaining and reviewing supporting documentation relating to the company's policies and procedures on:
 - identifying, evaluating and complying with laws and regulations;
 - detecting and responding to the risks of fraud; and
 - the internal controls established to mitigate risks related to fraud or non-compliance with laws and regulations including the company's controls relating to the company's compliance with the Companies Act 2006, Managing Public Money, Capacity Market Rules and the Electricity Capacity Market Regulations 2014
- inquired of management, the company's head of internal audit and those charged with governance whether:
 - they were aware of any instances of non-compliance with laws and regulations; and
 - they had knowledge of any actual, suspected, or alleged fraud;
- discussed with the engagement team regarding how and where fraud might occur in the financial statements and any potential indicators of fraud.

As a result of these procedures, I considered the opportunities and incentives that may exist within the company for fraud and identified the greatest potential for fraud in the following areas: revenue recognition, posting of unusual journals, complex transactions, and bias in management estimates. In common with all audits under ISAs (UK), I am also required to perform specific procedures to respond to the risk of management override.

I obtained an understanding of the company's framework of authority and other legal and regulatory frameworks in which the company operates. I focused on those laws and regulations that had a direct effect on material amounts and disclosures in the financial statements or that had a fundamental effect on the operations of the company. The key laws and regulations I considered in this context included Companies Act 2006, Managing Public Money, the Energy Act 2013, Capacity Market rules and the Electricity Capacity Market Regulations 2014.

Audit response to identified risk

To respond to the identified risks resulting from the above procedures:

- I reviewed the financial statement disclosures and testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described above as having direct effect on the financial statements;
- I enquired of management, the Audit, Risk and Assurance Committee and in-house legal counsel concerning actual and potential litigation and claims;
- I reviewed minutes of meetings of those charged with governance and the Board and internal audit reports;
- in addressing the risk of fraud through management override of controls, I tested the appropriateness of journal entries and other adjustments; assessed whether the judgements made on estimates are indicative of a potential bias; and evaluated the business rationale of any significant transactions that are unusual or outside the normal course of business.

I communicated relevant identified laws and regulations and potential risks of fraud to all engagement team members and remained alert to any indications of fraud or non-compliance with laws and regulations throughout the audit.

A further description of my responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of my report.

Other auditor's responsibilities

I am required to obtain evidence sufficient to give reasonable assurance that the expenditure and income recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them.

I communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control I identify during my audit.



Susan Clark
Senior Statutory Auditor
12 July 2023

For and on behalf of the
Comptroller and Auditor General
(Statutory Auditor)
National Audit Office
157-197 Buckingham Palace Road
Victoria
London
SW1W 9SP

Financial statements and notes to the accounts

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Statement of comprehensive income for the year ended 31 March

	Note	2023 £'000	2022 £'000
Other income	6	685,759	863,238
Other operating costs	7	(685,759)	(863,238)
Profit for the year		–	–
Other comprehensive income for the year		–	–
Total comprehensive income for the year		–	–

All operations are continuing operations.

The notes on pages 45 to 53 form part of these accounts.

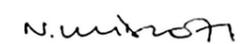
Statement of financial position

as at 31 March

	Note	2023 £'000	2022 £'000
Non-current assets			
Current assets			
Levy and capacity payments receivable	9	9,578	7,880
Prepayments and other debtors		2,873	74
Cash and cash equivalents	11	243,629	181,648
Total current assets		256,080	189,602
Total assets		256,080	189,602
Current liabilities			
Levy and capacity payments payables	12	(163,794)	(142,307)
Trade and other payables	13	(92,286)	(47,295)
Lease liabilities	14	(0)	(0)
Total current liabilities		(256,080)	(189,602)
Non-current liabilities			
Total non-current liabilities			
Total liabilities		(256,080)	(189,602)
Net assets			
Shareholders' equity and other reserves			
Share capital	15	–	–
Retained earnings		–	–
Total equity		–	–

The notes on pages 45 to 53 form part of these accounts.

The financial statements were approved by the Board of directors on 12 July 2023 and signed on its behalf by:



Neil McDermott
Chief Executive Officer



George Pitt
Chief Financial Officer

Statement of changes in equity

for the year ended 31 March

	Share capital £'000	Retained earnings £'000	Total equity £'000
As at 31 March 2021	1	–	1
Share capital issued	–	–	–
Total comprehensive income for the year	–	–	–
As at 31 March 2022	1	–	1
Share capital issued	–	–	–
Total comprehensive income for the year	–	–	–
As at 31 March 2023	1	–	1

As at 31 March 2023 the company has one authorised Ordinary share issued and fully paid.

Statement of cash flows

for the year ended 31 March

	Note	2023 £'000	2022 £'000
Cash flows from operating activities			
Profit for the year		–	–
Adjustments to reconcile profit before tax to net cash flows:			
Amortisation of intangible assets	8	–	248
Working capital adjustments:			
Decrease/(increase) in levy and capacity payments receivables	9	(1,698)	4,038
Increase in prepayments	9	(2,799)	82
Increase in levy and capacity payments payables	12	21,487	(131,114)
Increase in trade and other payables	13	44,991	(25,685)
Net cash inflow from operating activities		61,981	(152,431)
Cash flows from financing activities			
Repayment of lease liabilities	14	–	(293)
Net cash outflow from financing activities		–	(293)
Net increase in cash and cash equivalents in the year		61,981	(152,724)
Cash and cash equivalents at the beginning of the year		181,648	334,372
Cash and cash equivalents at the end of the year	11	243,629	181,648

The notes on pages 45 to 53 form part of these accounts.

Notes to the financial statements

for the year ended 31 March 2023

1. Authorisation of financial statements

The financial statements of Electricity Settlements Company Ltd (the “company”) for the year ended 31 March 2023 were approved and authorised for issue in accordance with a resolution of the directors on 12 July 2023.

The company is a company limited by shares, incorporated and domiciled in the UK. The company’s registered office is at 10 South Colonnade, London, E14 4PU. The company is unlisted and wholly owned by the Secretary of State for Business, Energy and Industrial Strategy (the “shareholder”) making it the company’s ultimate controlling party. During the year there was a reorganisation of Government departments, with the Department of Energy Security and Net Zero (DESNZ) formed, among others. For this financial year accounting is being undertaken under the old structure, and thus BEIS is referred to below. Going forward the shareholder will be the Secretary of State for Energy Security and Net Zero.

1.1 Principal activities

The company has been established to act as the settlement body for the Capacity Market. The company will also undertake such other activities that the Board considers to be consistent with the company’s functions, duties, obligations and constitution.

2. Accounting policies

2.1 Basis of preparation

These financial statements are presented in pounds sterling and all values are rounded to the nearest thousand pounds (£’000).

The financial statements of the company have been prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006.

These accounts have been prepared under the historical cost convention as modified for the treatment of financial instruments.

The Capacity Regulations as identified below are defined hereafter as the “Regulations”:

- The Electricity Capacity Regulations 2014 as amended;
- The Electricity Capacity (Supplier Payment etc.) Regulations 2014 as amended.

2.2 Going concern

The directors have a reasonable expectation that the company has adequate resources to continue to operate for the foreseeable future. The financial statements are, therefore, prepared on a going concern basis.

In forming this view, the directors note that the company:

- applies prudent financial management in order to ensure that its commitments are accommodated within the timing of its collection of its settlement costs levy;
- undertakes a robust and detailed annual business planning and budgeting process to establish its operational costs requirements for each financial year;
- has considered the potential impact of credit risk and liquidity risk detailed in note 3; and
- is exposed to minimal cash flow risk through Capacity Market transactions as a result of the statutory ‘pay when paid’ mechanism explained below.

The day-to-day operational costs of the company are funded by electricity suppliers under the Capacity Market “settlement costs levy” which is set by the Regulations.

The settlement costs levy is reset by new amending Regulations and has currently been set for the year (to March 2023).

The directors note the risk that the total settlement costs levy set for a year will be insufficient or that a timing mismatch might arise between the time when monies are raised by the levy and the time when monies are required to meet a spend commitment made by the company.

During the course of a year, the company may, where it identifies that there is likely to be a shortfall in the collection of the settlement costs levy against its

requirements, request DESNZ to support an in-year adjustment to the applicable levy rate. Such an adjustment would be subject to public consultation and the making of new regulations in accordance with the same process that has applied to the setting of the annual settlement costs levy. The company can also request a working capital loan from DESNZ if there is a shortfall in its operating cash flow.

The requirement to pay capacity payments to Capacity Providers is set out in the Regulations. The payments to be made to Capacity Providers are funded by suppliers under the Regulations. It should be noted that the Regulations state that the company’s obligation is to pay when paid (i.e. the company has no obligation to pay the Capacity Providers until it receives adequate funds from suppliers to perform its obligation).

The budget for ESC has been publicly consulted on and set in regulations up to 31 March 2025. In the absence of new regulation, the levy would continue at the same amount as the most recent regulation.

2.3 Settlement costs levy income

Under the Regulations, the company is entitled to recover its operational costs through the settlement costs levy on suppliers referred to above. The total amount of the levy has been set for the next year. Any surplus at the year-end is reimbursed to suppliers by issuing credit notes against the following year’s levy and is classified as part of levy and capacity payments payables within current liabilities.

Settlement costs levy income is recognised as ‘other income’ in the financial year to which it relates and is presented net of any settlement costs levy repayable to suppliers.

ESC continues to apply its accounting policy of recognising the income to match operational costs which follows the IFRS Conceptual Framework for Financial Reporting.

The settlement costs levy is collected through monthly invoices. The settlement services provider, EMRS, administers the collection process.

Notes to the financial statements

for the year ended 31 March 2023 (Continued)

2.4 Capacity Market supplier charge income

Capacity Market supplier charge income relates to the charges which electricity suppliers are required to pay under the Regulations to meet the cost of funding capacity payments. Under the Regulations, the company is entitled to collect the Capacity Market supplier charge before making capacity payments. The total amount of the Capacity Market supplier charge is set before the start of the delivery year based on suppliers' forecasts. The Capacity Market supplier charge is re-determined in monthly and yearly reconciliations. Re-determination of the Capacity Market supplier charge takes the following into account:

- i. Transition from forecast to actual meter data; and
- ii. Adjustments to capacity payments payable.

Any surplus Capacity Market supplier charge at the year-end is classified as part of levy and capacity payments payables within current liabilities.

2.5 Capacity payments

Capacity payments are payments to the Capacity Providers under the Regulations for their commitment to meet a capacity obligation during a delivery year. Total capacity payments are based on the capacity cleared price achieved in the auction in respect of which the Capacity Agreement was awarded. Capacity payments are split into 12 monthly payments which are weighted to reflect the seasonal variation of electricity demand in Great Britain during a year.

Following a transmission system stress event, Capacity Providers may be eligible for additional payments or subject to financial penalties, depending on whether they exceed their capacity obligations (over-deliver) or fail to meet them (under-deliver).

2.6 Recharges

The company is recharged a proportion of costs which it shares with Low Carbon Contracts Company Ltd (LCCC). LCCC is a sister arm's length body owned by the Secretary of State for Energy Security and Net Zero and is responsible for acting as the counterparty to Contracts for Difference (CfDs). In order to maximise operational cost efficiency, LCCC provides certain services to the company and makes certain payments on its behalf. Typically, this includes common costs such as staff costs, shared IT infrastructure and the use of shared resources and facilities. The

recharge also includes costs incurred on those activities that allow the company to perform its functions in relation to the Capacity Market.

This recharge is based on an estimate of the time LCCC's employees will spend on the company's activities during the relevant financial year, together with an appropriate allocation of overhead costs (including rent, service charge, IT infrastructure and telephony support) and a 'use of asset' charge. It also includes a proportion of the salaries of the Board members who divide their time between the two companies. LCCC undertakes these activities on behalf of the company and the company's Board retains responsibility and accountability for the quality and cost of services provided by LCCC.

The company and LCCC are part of the same VAT group, therefore no VAT is charged on costs recharged by LCCC. The company's income is outside the scope of VAT so it will be unable to recover its input VAT on any of its expenditure.

2.7 Government grants

Grants from the government are recognised at their fair value where there is a reasonable assurance that the grant will be received and the company will comply with all the attached conditions.

2.8 Financial assets

The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition. Management determines the categorisation of financial assets at initial recognition and re-evaluates this designation at each reporting date.

2.8.1 Classification

Financial assets are classified and measured at amortised cost.

2.8.2 Recognition and measurement

Financial assets at amortised cost are initially recognised at fair value, subsequently measured at amortised cost using the effective interest rate (EIR) method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

ESC holds financial assets comprising of cash and cash equivalents and receivables at the reporting date.

For the purposes of presentation in the statement of cash flows, cash and cash equivalents includes cash held at bank

and is subject to an insignificant risk of change in value.

2.9 Financial liabilities

2.9.1 Recognition and measurement
Financial liabilities are classified, at initial recognition, as other liabilities (i.e. lease liabilities, borrowings and payables as appropriate).

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings and payables, net of directly attributable transaction costs.

2.9.1.2 Other financial liabilities

After initial recognition, other liabilities are subsequently measured at amortised cost using the EIR method (if material). Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR amortisation process.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as finance costs in the statement of comprehensive income.

2.9.2 Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognised in the statement of comprehensive income.

2.10 Intangible assets

Intangible assets are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and accumulated impairment losses (if any). Intangible assets have finite lives and are amortised over their useful economic life or assessed for impairment whenever there is an indication that the asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life is reviewed at least at the end of each reporting period.

Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are considered to modify the amortisation period or method, as appropriate, and are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the statement of comprehensive income in the expense category that is consistent with the function of the intangible assets.

Intangible assets are amortised over the following periods:

	Years
Settlement system	5
Other IT software	5

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the statement of comprehensive income when the asset is derecognised.

2.11 Leases

2.11.1 Company as a lessee

At inception of a contract, the company assesses whether a contract is, or contains, a lease based on whether the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The company recognises a right-of-use asset and a corresponding lease liability with respect to all lease agreements in which it is the lessee, except for short-term leases (defined as leases with a lease term of 12 months or less) and leases of low value assets.

2.11.2 Measurement of leases liabilities

Lease liabilities are initially measured at the present value of the contractual lease payments that are not paid at the commencement date, discounted (if material) by using the rate implicit in the lease. If this rate cannot be readily determined, the company uses its incremental borrowing rate. Variable lease payments are only included in the measurement of the lease liability if they depend on an index or rate. In such cases, the initial measurement of the lease liability assumes the variable element will remain unchanged throughout the lease term.

2.11.3 Measurement of right-of-use assets

Right-of-use assets are initially measured at the amount of the lease liability, reduced for any lease incentives received, adjusted for any lease payments made at or before the commencement date, and increased for any initial direct costs. Whenever the company incurs an obligation for costs to dismantle and remove a leased asset, restore the site on which it is located, or restore the underlying asset to the condition required by the terms and conditions of the lease, a provision is recognised and measured under IAS 37. The costs are included in the related right-of-use asset.

Right-of-use assets are amortised to the earlier of the end of the useful life of the right-of-use asset or the lease term using the straight-line method as this most closely reflects the expected pattern of consumption of the future economic benefits. The amortisation starts at the commencement date of the lease.

The company applies IAS 36 to determine whether a right-of-use asset is impaired and accounts for any identified impairment loss as described in note 2.12.

2.12 Impairment of non-financial assets

Intangible assets are only subject to amortisation to the extent that they are available for use. Assets, which are not available for use, are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. At each reporting date, the company reviews the carrying amounts of its intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of any impairment loss.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are largely independent cash inflows (cash-generating units). Impairment losses are charged to the statement

of comprehensive income and prior impairments of non-financial assets are reviewed for possible reversal at each reporting date.

2.13 Provisions

Provisions are recognised when the company has a present obligation (legal or constructive) as a result of a past event, that can be reliably measured, and it is probable that an outflow of economic benefits will be required to settle that obligation.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation. The accounting policy allows for an increase in the provision due to the passage of time (time value of money) which would be recognised as an interest expense.

2.14 Segmental reporting

The company operates solely within the UK and within one business segment; hence no segmental reporting is required. This is consistent with the internal reporting provided to the directors of the company, who are considered the company's chief operating decision makers.

2.15 Bid bond collateral

In order to enter Capacity Market Auctions, applicants must lodge bid bond collateral with the company where, on Prequalification Results Day, those applicants receive a notice from National Grid, as Transmission System Operator, that states Prequalification of their Capacity Market Unit(s) is conditional on providing bid bond collateral.

Bid bond collateral will be held by the company until one of the following triggers set out in the Regulations occurs:

- the relevant Capacity Market auction is delayed;
- the potential Capacity Provider notifies that it no longer intends to bid in the relevant Capacity Market auction;
- the Capacity Market auction takes place, and the potential Capacity Provider does not win a Capacity Agreement; or
- the Capacity Provider demonstrates capacity in the manner required by the Regulations.

Bid bond collateral may not be returned to the Capacity Providers if the Capacity Agreement is terminated.

Notes to the financial statements

for the year ended 31 March 2023 (Continued)

When a Capacity Agreement is terminated, either a termination fee becomes payable or bid bond collateral is drawn down. These amounts are passed onto the Government's Consolidated Fund via DESNZ and are not included in the statement of comprehensive income.

3. Financial risk management

3.1 Financial risk management and financial risk factors

Due to the nature of its operational and financial arrangements the company is not exposed to any significant financial risk. The financial risk is minimal by virtue of the company's levy funding arrangements with licensed suppliers, which are set out below.

3.2 Credit and liquidity risk

Under the legislation there is an obligation placed on licensed suppliers to fund in advance, via payment through a levy, the capacity payment obligations as they crystallise. The company has no obligation to pay the Capacity Providers until it receives adequate funds from suppliers to perform its obligations.

As the Capacity Market settlement timetable is structured such that monies to be received by the company are invoiced and collected prior to the issue of credit notes and payments out from the company, the liquidity risk is minimal.

4. Accounting judgements, estimates and assumptions

The preparation of the company's financial statements requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and other factors, including expectations or future events that are believed to be reasonable under the circumstances. The results form the basis of making judgements about carrying values of assets and liabilities that are not readily apparent from other sources.

Revisions to accounting estimates are recognised in the period in which the estimate is revised, if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

4.1 Estimates

The assumptions and estimation uncertainties at the reporting date are not deemed to have a significant risk of resulting in a material adjustment to the carrying amounts of the assets and liabilities in the next financial year. The company based its assumptions and estimates on parameters available when the financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances arising that are beyond the control of the company. Such changes are reflected in the assumptions when they occur.

4.1.1 Estimating useful lives and residual values of intangible assets

At each reporting date, the useful lives and residual values of intangible assets are reviewed. Assessing the appropriateness of useful life and residual value estimates requires the company to consider a number of factors such as the technological advancement, expected period of use of the asset by the company, and expected disposal proceeds (if any) from the future sale of the asset. An incorrect estimate of the useful life or residual value will affect the amortisation expense recognised in the statement of comprehensive income and the asset's carrying amount.

4.2 Significant judgement

Management has made the following judgement in applying the company's Accounting Policy:

4.2.1 Capacity Agreements

Capacity Agreements are arrangements between National Grid (as System Operator) and Capacity Providers. They require the Capacity Provider to be ready to provide a certain amount of capacity in their applicable delivery years when called upon to do so by National Grid.

The company is not party to Capacity Agreements but is only responsible for acting as an administrator for the settlement process. A Capacity Market obligation for the company only arises when settlement levy payments are received from electricity suppliers (i.e. only pay when paid) and the Capacity Provider delivers the required capacity in line with the capacity arrangements. As a result no provision is raised in the statement of financial position and Capacity Agreements are not classified as financial instruments because the company's role is driven by statute rather than contract.

5. New standards, amendments and interpretations applicable to the company but not yet adopted

There are a number of standards, amendments to standards, and interpretations which have been issued by the IASB that are effective in future accounting periods that the company has decided not to adopt early.

The following amendments are effective for the period beginning 1 January 2023:

- Amendments to IAS 1 Presentation of financial statements, classification of liabilities as current or non-current and disclosure of accounting policies; and
- Amendments IAS 8 Accounting policies, changes in accounting estimates and errors, definition of accounting estimates.

The following amendments are effective for the period beginning 1 January 2024:

- Amendments to IFRS 17 Insurance contracts Requirements for a company reporting information about insurance contracts it issues and reinsurance contracts it holds.

The adoption of the above is not expected to have any impact on the company's accounting policies or have any other material impact on the financial position or performance of the company.

6. Other income

	2023 £'000	2022 £'000
Settlement costs levy income	6,963	7,487
Less: amount repayable to suppliers	(1,762)	(536)
Net settlement costs levy income	5,201	6,951
Capacity Market supplier charge income	680,507	856,264
Late payment interest	51	23
Other income	685,759	863,238

7. Other operating costs

	2023 £'000	2022 £'000
Capacity payments	680,507	856,264
Operational settlement costs	3,303	3,748
Costs recharged by LCCC	1,748	2,793
Amortisation	–	249
Auditor's remuneration	40	37
Miscellaneous costs	161	147
Other operating costs	685,759	863,238

Auditor's remuneration represents audit fees of £34K (2022: £31K) excluding VAT. The fees shown in the table above are VAT inclusive.

The delivery year for the Capacity Market runs from 1 October to 30 September of each year.

The capacity payments for each delivery year (DY) are summarised in the table below:

Capacity Market Payments	FY 2022/23 £m	FY 2021/22 £m
T-4 Capacity Auction DY 2018/19	16.6	16.2
T-4 Capacity Auction DY 2019/20	15.0	15.0
T-1 Capacity Auction DY 2020/21	nil	0.4
T-4 Capacity Auction DY 2020/21	27.1	538.7
T-1 Capacity Auction DY 2021/22	40.2	55.1
T-4 Capacity Auction DY 2021/22	208.1	230.8
T-1 Capacity Auction DY 2022/23	202.3	nil
T-3 Capacity Auction DY 2022/23	171.2	nil
Total	680.5	856.3

Notes to the financial statements

for the year ended 31 March 2023 (Continued)

8. Intangible assets

	Settlement system £'000	Other IT software £'000	Total £'000
Cost			
As at 31 March 2020	2,538	15	2,553
Additions during the year	–	–	–
As at 31 March 2021	2,538	15	2,553
Additions during the year	–	–	–
As at 31 March 2022	2,538	15	2,553
Additions during the year	–	–	–
As at 31 March 2023	2,538	15	2,553
Amortisation			
As at 31 March 2020	1,782	14	1,796
Charge for the year	508	1	509
As at 31 March 2021	2,290	15	2,305
Charge for the year	248	–	248
As at 31 March 2022	2,538	15	2,553
Charge for the year	–	–	–
As at 31 March 2023	2,538	15	2,553
Net book value as at 31 March 2022	–	–	–
Net book value as at 31 March 2023	–	–	–

The settlement systems are fully amortised, however they are still in use. ESC has invested in the system to update for regulation changes and followed a continuous improvement mindset which has prolonged the life of the asset. Given the work undertaken and the scale of task to replace the settlement system, it is expected the settlement system will be used until at least 2026.

9. Levy and capacity payments receivable

	2023 £'000	2022 £'000
Capacity Market supplier charge	3,325	615
Capacity Providers receivable	2,195	5,047
Termination charges receivable	4,034	2,079
Settlement costs levy	24	139
Total levy receivable	9,578	7,880

Capacity Market supplier charge receivable relates to unpaid Capacity Market supplier charge invoices (i.e. suppliers ceased trading). Balance recoverable through the mutualisation process.

10. Prepayments and other debtors

	2023 £'000	2022 £'000
Prepayments	118	74
Due from LCCC	983	–
Other debtors	1,772	–
Prepayments and other debtors	2,873	74

The amount due from LCCC relates to the true up of the recharge.

Other debtors relates to an amount due back from HMT in relation to termination payments

11. Cash and cash equivalents

	2023 £'000	2022 £'000
Cash at bank	150,733	132,745
Bid bond collateral	70,816	30,652
Suppliers' credit cover	22,080	18,251
Total cash and cash equivalents	243,629	181,648

For the purpose of the statement of cash flows, cash and cash equivalents comprise cash at bank, suppliers' credit cover and bid bond collateral as stated above. Suppliers' credit cover and bid bond collateral are restricted cash balances and relate to credit cover provided by the Capacity Providers and electricity suppliers. No interest is earned on suppliers' credit cover and interest earned on bid bond collateral is returned to the Capacity Providers.

12. Levy and capacity payments payables

	2023 £'000	2022 £'000
Capacity payments	136,724	109,673
Capacity Market supplier charge	20,746	28,280
Settlement costs levy	2,291	2,092
Termination charges payable	4,034	2,261
Total levy and capacity payments	163,794	142,307

Capacity payments payables are the amounts due to the Capacity Providers under the Regulations for their commitment to meet a capacity obligation during a delivery year. Total capacity payments are based on the capacity cleared price achieved in the auction that the Capacity Agreement was awarded.

The settlement costs levy payable relates to the difference between the operational costs which have been collected from electricity suppliers during 2022/23, based on estimated spend for the year, and the operational costs actually incurred during the year. The difference is refunded to suppliers in the following financial year.

The Capacity Market supplier charge payable relates to the difference between Capacity Market supplier charges which have been collected from electricity suppliers during the 2022/23 financial year, based on estimated payments to the Capacity Providers, and the actual payments made during the year. The difference is refunded to suppliers in the following financial year.

Termination charges payable relate to the relevant charges receivable, when a Capacity Agreement is terminated, that are payable to the Government's Consolidated Fund.

Notes to the financial statements

for the year ended 31 March 2023 (Continued)

13. Trade and other payables

	2023 £'000	2022 £'000
Bid bond collateral	70,743	28,983
Suppliers' credit cover	21,503	18,252
Accruals and other payables	40	60
Total trade and other payables	92,286	47,295

Bid bond collateral relates to credit cover provided by the Capacity Providers.

14. Lease liabilities

	£'000
As at 31 March 2021	293
Repayment of lease liability	(293)
As at 31 March 2022	–
As at 31 March 2023	–

Maturity analysis:

	2023 £'000	2022 £'000
Less than 1 year	–	–
Between 1 and 5 years	–	–
As at 31 March	–	–

The lease liability was held in respect of the settlement system right-of-use asset which has been funded by BEIS through EMRS, a wholly owned subsidiary of ELEXON limited.

15. Share capital

Authorised shares	
Ordinary share capital £1 each	1 £
Ordinary share capital issued and fully paid:	
As at 31 March 2021 and 31 March 2022	1
Share capital issued during the year	–
As at 31 March 2023	1

16. Related party transactions

The following table provides the total amount of transactions that have been entered into with related parties for the relevant financial year:

	Services from related parties £'000	Amounts owed by related parties £'000	Amounts owed to related parties £'000
Entities with significant influence:			
2022			
LCCC	2,793	–	–
BEIS	–	–	–
2023			
LCCC	1,748	983	–
DESNZ	–	–	–

Services from LCCC comprise shared costs of premises, staff and directors' payroll costs, IT infrastructure and use of assets which are incurred in the first instance by LCCC but are then recharged to the company based on the estimated usage of those services. Amounts owed to BEIS/DESNZ in the previous year related to the lease liability in respect of the settlement system asset.

17. Financial assets and liabilities

Financial assets	Note	2023 £'000	2022 £'000
Cash and cash equivalents	11	243,629	181,648
Total financial assets		243,629	181,648
Financial liabilities	Note	2023 £'000	2022 £'000
Trade and other payables	13	92,286	47,295
Lease liabilities	14	–	–
Total financial liabilities		92,286	47,295
Total current		92,286	47,295
Total non-current		–	–
Total financial liabilities		92,286	47,295

18. Events after the reporting period

There are no post balance sheet events which have a material impact on the company's financial results.

Glossary

Acronym	Description
BEIS	Department for Business, Energy and Industrial Strategy.
BSC	Balancing and Settlement Code (BSC) is a legal document which defines the rules and governance for the balancing mechanism and imbalance settlement processes in respect of the wholesale electricity market in Great Britain. Find it at: https://www.elexon.co.uk/bsc-and-codes/
Capacity Agreement	A Capacity Agreement is a regulatory and rule based arrangement between National Grid, as System Operator, and a successful applicant in a Capacity Market Auction. The Capacity Agreement provides a regular retainer payment to the successful applicant or "Capacity Provider".
Capacity Auction	At a Capacity Auction, applicants who offer the lowest bid can win a Capacity Agreement. A Capacity Auction relates to delivery of capacity approximately four years ahead (T-4). For instance, the Capacity Agreements resulting from the 2014 T-4 Capacity Auction will require capacity to be delivered in the delivery year commencing 2018/19.
Capacity Market	The Capacity Market has been designed by BEIS (formerly DECC) to offer Capacity Providers who have been awarded Capacity Agreements via an auction with a revenue stream, with the aim of ensuring they are available to contribute to security of supply at least cost to consumers. Capacity Providers can be new or existing generators, electricity storage providers and significant users of electricity who provide voluntary demand reductions.
Capacity Market Regulations	Capacity Market Regulations means the Electricity Capacity Regulations 2014 (as amended) and the Electricity Capacity (Supplier Payment etc.) Regulations 2014 (as amended).
Capacity Market Settlement Body	Means the entity appointed under the Capacity Market Regulations 2014 to obtain supplier charges and make capacity payments and to have overall accountability and control of the Capacity Market settlement process.
Capacity Market Stress Event	A system stress event that has occurred at least four hours after a Capacity Market Notice has been issued and post-event analysis by National Grid ESO has confirmed that a system stress event has occurred.
Capacity Provider	A Capacity Provider is the holder of a Capacity Agreement with National Grid (as System Operator). Capacity Providers can be new or existing generators, electricity storage providers and significant users of electricity who provide voluntary demand side reductions (demand side response). Capacity Providers provide capacity under either a Capacity Agreement resulting from a Capacity Market Auction or from a Transitional Arrangement Auction.
CCUS	Carbon Capture Usage and Storage
CMU	Capacity Market Unit
Delivery Partners	Organisations involved in delivering the Capacity Market, namely ESC, and Electricity Market Reform (EMR) Delivery Body, Electricity System Operator, National Grid, and Ofgem.
Delivery year	This is a defined term within the Capacity Market Rules referring to the obligation period of a Capacity Agreement being 1 October to 31 March of the following year.
Demand side response	Demand side response helps to manage the demand for electricity. It involves changing the usage patterns of electricity users (the "demand side") in response to incentives. It is used to match supply with demand when unpredictable fluctuations occur and provides a mechanism through which demand can be reduced in peak times when system capacity is tight, thereby minimising the amount of additional generation capacity being brought onto the grid. Demand side response is seen as having the potential to help to lower consumer bills, electricity system costs and carbon emissions produced by traditional peaking plant, such as oil, coal and gas-fired generation.
DESNZ	Department for Energy Security and Net Zero.
ECJ	Means the General Court of the Court of Justice of the European Union. The General Court annulled the relevant scheme Approval on 15 November 2018 (Case T-793 14).
EMRS	EMR Settlement Ltd (EMRS) is a wholly owned subsidiary company of ELEXON Ltd.* It is the settlement services provider under a contract with LCCC to manage the operation of the settlement system. (*ELEXON website: www.elexon.co.uk/)

Acronym	Description
Energy Data Taskforce	The Energy Data Taskforce was established by Government and Ofgem to develop a set of recommendations for how industry and the public sector can work together to facilitate greater competition, innovation and markets in the energy sector through improving data availability and transparency.
ESC	Electricity Settlements Company Ltd.
ESO	The Electricity System Operator (ESO), a ring-fenced part of National Grid, includes the 'EMR Delivery Body', which manages CfD and Capacity Market Auctions.
LCCC	Low Carbon Contracts Company Ltd.
Meter assurance	Under the Capacity Market, Capacity Providers with complex or non-BSC metering arrangements need to undergo metering checks in accordance with ESC meter standards guidance. Find it at https://www.electricitysettlementscompany.uk
Ofgem	Office of Gas and Electricity Markets, a non-ministerial government department and an independent national regulator.
Review of Electricity Market Arrangements (REMA)	DESNZ is undertaking REMA with NGENSO and Ofgem to assess the needs for longer term reform to GB electricity market design to achieve net zero, security of supply and efficient energy system operation goals by 2035. This will have potential implications for EMR schemes and new schemes to be managed by LCCC.
Scheme Approval	State aid approval (SA.35980) granted by the European Commission in July 2014 for the main Capacity Market scheme.
Secretary of State	Means the Secretary of State for Business, Energy and Industrial Strategy, our shareholder.
Settlement system	The settlement system used to settle all monies collected from suppliers to make payments to Capacity Market providers, and to settle all monies collected from Capacity Market providers which are payable to suppliers (or, in the case of the termination payments, to DESNZ).
Standstill	Means the situation affecting the Capacity Market as a result of the annulment of the relevant scheme Approval on 24 October 2019. The full operation of the Capacity Market therefore could not take place during the Standstill Period, and the Capacity Market was termed in "standstill" for this period.
Standstill Period	Standstill Period means the period beginning on 24 October 2019 and ending on (as further described in the Supplier Payment Regulations).
Standstill Regulations	Refers to the Electricity Capacity (No. 1) Regulations 2019, http://www.legislation.gov.uk/uksi/2019/862/contents/made
State aid	State aid is any advantage granted by public authorities through state resources on a selective basis to any organisations that could potentially distort competition in the European Union.
Supplier Payment Regulations	Supplier Payment Regulations means the Electricity Capacity (Supplier Payment etc.) Regulations 2014 (as amended), including as amended by the Electricity Capacity (No. 1) Regulations 2019). http://www.legislation.gov.uk/uksi/2014/3354/contents/made Also amended by the Electricity Supplier Payments (Amendments) Regulations 2021 https://www.legislation.gov.uk/ukdsi/2021/9780348219296
System Operator	Organisation licenced by Ofgem to operate the GB electricity system, a role currently held by National Grid Plc. The Electricity System Operator's current responsibilities include balancing the electricity system, running electricity Capacity Auctions, coordinating and administering aspects of industry rules and codes and supporting efficient transmission network development.
Voluntary Supplier Arrangement	Voluntary Supplier Arrangement means the arrangement provided by ESC under which it will accept and hold payments made, on a voluntary basis, by suppliers during the Standstill Period. All such payments are made by suppliers and received and held by ESC on the basis of the terms and conditions published by ESC and in accordance with the new Capacity Market Regulations.

Senior Leadership Team

This was the Senior Leadership Team as at 12 July 2023.



Neil McDermott
Chief Executive Officer



George Pitt
Chief Financial Officer



Sarah Taylor
Interim Director of People & Organisational Development



Andrew Deeley
Director of Strategy & Development



Allison Sandle
General Counsel & Company Secretary



James King
Director of Scheme Delivery



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