EXPLANATORY MEMORANDUM TO

THE NUCLEAR REGULATED ASSET BASE MODEL (REVENUE COLLECTION) REGULATIONS 2023

2023 No. 254

1. Introduction

This explanatory memorandum has been prepared by the Department for Business, Energy and Industrial Strategy and is laid before Parliament by Command of His Majesty.

2. Purpose of the instrument

These Regulations establish a mechanism to allow a revenue collection counterparty, designated under section 16 of the Nuclear Energy (Financing) Act 2022 (the "Act"), to raise funds from all licensed electricity suppliers in Great Britain to pay for the liabilities that it has to relevant nuclear licensee companies (under revenue collection contracts), and to return money to suppliers where appropriate. The Regulations set out arrangements for the revenue collection counterparty to hold sums in reserve and to cover its losses in the situation of default by an electricity supplier. The Regulations also set out the arrangements for collection of a levy from all licensed electricity suppliers to pay for the revenue collection counterparty's operating costs.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

None.

4. Extent and Territorial Application

The extent of this instrument (that is, the jurisdictions which the instrument forms part of the law of) is England and Wales and Scotland.

The territorial application of this instrument (that is, where the instrument produces a practical effect) is England and Wales and Scotland.

5. European Convention on Human Rights

The Secretary of State for the Department for Business, Energy and Industrial Strategy, Grant Shapps, has made the following statement regarding Human Rights:

> "In my view the provisions of The Nuclear Regulated Asset Base Model (Revenue Collection) Regulations 2023 are compatible with the Convention rights".

6. Legislative Context

The Act makes provision for the introduction of a Regulated Asset Base ('RAB') model for nuclear project companies which are designated under the provisions of the Act. The Secretary of State would modify a designated nuclear company's electricity generation licence to insert new licence conditions, giving them a right to receive regulated revenues in relation to the provision of the infrastructure in question (i.e. 'RAB licence').

Part 2 of the Act makes provision in relation to the use of revenue collection contracts for RAB nuclear projects. Section 15 of the Act confers a power on the Secretary of State to make

regulations about revenue collection contracts. Section 15(2) provides that revenue collection contracts are contracts between revenue collection counterparties and designated nuclear companies entered into pursuant to a direction given under section 18 of the Act under which certain payments are to be funded by electricity suppliers (including payments made before the corresponding nuclear project starts generating). Where the Secretary of State is to make regulations under section 15 of the Act, section 19(1) of that Act requires that regulations make provision for electricity suppliers to pay the revenue collection counterparty for the purpose of enabling the counterparty to make payments under all revenue collection contracts to which it is a party. This obligation is fulfilled through the Regulations that are the subject of this Explanatory Memorandum.

7. Policy background

What is being done and why?

This instrument concerns the revenue stream under a Regulated Asset Base ('RAB') funding model for new nuclear projects, which will provide long-term revenue stabilisation to a low-carbon nuclear project (as designated under the Act, see paragraph 7.2), allowing investment to come forward at a comparably lower cost of capital to existing policy mechanisms.

Under the proposed model, a nuclear company designated under the Act and who has (1) entered into a revenue collection contract with the revenue collection counterparty and (2) whose generation licence has been modified in accordance with the Act (i.e. 'RAB licence'), known as a 'relevant licensee nuclear company', would be allowed to receive a regulated revenue stream during the design, construction, commissioning and operation of its nuclear project, such revenues determined by the Gas and Electricity Markets Authority (the 'Authority') and would be channelled from electricity suppliers. The duration of the revenue collection contract would depend on the nuclear RAB project in question.

The revenue stream mechanics in these Regulations have been, where possible, largely modelled on The Contracts for Difference (Electricity Supplier Obligations) Regulations 2014, which set out the revenue stream mechanics for the Contracts for Difference ('CFD') scheme. CFDs are contracts (mostly awarded through an allocation framework) between the CFD counterparty and persons concerned with the generation of low carbon electricity, which provide payments between the parties based on the difference between a 'strike price' determined under that contract and the market price of electricity at the time of generation.

By contrast, under the provisions in these Regulations, the revenue collection counterparty will enter into a revenue collection contract with the relevant licensee nuclear company (upon direction by the Secretary of State, see below paragraph 7.32) and any payments channelled to the relevant licensee nuclear company would be as confirmed to the counterparty by the Authority (in accordance with the terms of their revenue collection contract or pursuant to the same).

<u>Supplier obligation and revenue collection counterparty</u>

Part 2 of these Regulations deals with the supplier obligation, which is a compulsory levy on electricity suppliers that will fund the regulated revenues under the RAB project. As above, these Regulations have taken as precedent the existing CFD regime, with adaptations to allow for the functionality of the specific RAB revenue mechanics, for example see paragraph 7.9 below.

The supplier obligation will be managed by a revenue collection counterparty designated under section 16(1) of the Act. Its main role is to manage the collection of monies under the supplier obligation in order that it can make payments to (and from) a relevant licensee nuclear company under their revenue collection contract. On 6 June 2022 the Low Carbon Contracts Company Ltd ('LCCC'), a private company limited by shares and wholly owned by the Secretary of State, was designated as the revenue collection counterparty by notice pursuant to section 16 (1) of the Act.

It is possible under the Act for there to be more than one revenue collection counterparty to be designated (detail around the designation of more than one person designated is found in the Schedule to the Regulations). It is the Department's intention that there is not more than one revenue collection counterparty simultaneously (this is only ever likely to occur in extreme circumstances, for instance during a handover between two counterparties) so the Regulations are principally drafted on the basis that there is a single counterparty.

Supplier obligation and interim levies

Under these Regulations the counterparty will collect two levies: the supplier obligation and the operational costs levy. The operational costs levy is to fund the operational costs of the revenue collection counterparty.

Under arrangements set out in relevant nuclear companies' amended electricity licences and revenue collection contracts, the Authority would confirm to the revenue collection counterparty what revenues the relevant licensee nuclear company is entitled to receive or has to pay. Upon the Authority's confirmation of such payments, the revenue collection counterparty would then be able to estimate the amounts it would need to collect from suppliers during each quarterly period.

Under these Regulations, suppliers are liable for the supplier obligation for each quarter based on the payments that the revenue collection counterparty has to make under revenue collection contracts. Suppliers are liable in proportion to their market share in the period to which the payments relate – i.e. the proportion of total electricity that each supplier supplies in the relevant period. If the revenue collection counterparty receives payments from the relevant nuclear licensee company under the terms of the revenue collection contract then the revenue collection counterparty will pass this back to suppliers, again in proportion to electricity supply in that period.

In calculating each suppliers' market share, the counterparty will not include in its calculation any 'EII excluded electricity', within the meaning of regulation 6(1) of the Electricity Supplier Obligations (Amendment & Excluded Electricity) Regulations 2015.

The Regulations make provision which requires the revenue collection counterparty to adjust payments due from electricity suppliers to reflect certain financial assistance (and any specified repayments thereof) provided by the Secretary of State to the revenue collection counterparty.

In order to provide the relevant licensee nuclear company with a stable daily revenue stream, the revenue collection counterparty will forecast and set a fixed £/MWh interim rate which suppliers will be charged against the amount of electricity supplied each day.

Additionally, to ensure that the counterparty has sufficient funds to make payments to the nuclear company under the revenue collection contract, these Regulations make provision for the counterparty to hold a Reserve Fund. This will be funded by suppliers as a lump sum payment at the start of every levy period.

The levy period

Under these Regulations, both the interim rate and the reserve fund are set on a quarterly basis. This approach ensures that the counterparty should have sufficient funds to pay generators what is owed whilst minimising the cash call on suppliers through being reset regularly (quarterly).

The counterparty must set the interim rate and reserve fund at least 30 days in advance of each relevant quarter, and then each suppliers' individual share of that reserve fund 8 working days after setting this interim rate and reserve fund (in advance of each relevant quarter).

Sizing of the interim rate and reserve fund

Under these Regulations, the interim rate will be set according to the counterparty's forecast of expected payments under the revenue collection contract (in practice being largely the regulated revenues as confirmed by the Authority, though not set out in these Regulations), estimated electricity supply and estimated payments from relevant licensee nuclear companies over the levy period. The reserve fund will also be sized according to the counterparty's forecasts of payments to ensure the counterparty has a 95% certainty that they will have sufficient funds to make payments required under revenue collection contracts during the levy period.

Interim rate payments

Under these Regulations, suppliers must pay interim rate payments on a daily basis, with amounts owed calculated by multiplying the applicable interim £/MWh rate by the volume of electricity supplied by that supplier on each billing day. Suppliers will be invoiced in arrears of the day of supply (with the counterparty invoicing them once the first information about suppliers' electricity supply on that day is available) and will have 5 working days to make payments. To ensure that the revenue collection counterparty can still make payments to relevant nuclear licensee companies in the event that a supplier fails to make a payment that is due, all suppliers are required to post collateral calculated to cover 21 days of interim rate payments. If collateral is exhausted the revenue collection counterparty is able to mutualise (spread the cost of) any outstanding amounts across the non-defaulting suppliers.

Should a supplier fail to pay their invoice by the due date interest will be charged on the amount outstanding.

Reconciling against supplier obligation

Each quarter, the counterparty must reconcile suppliers' interim payments against the counterparty's underlying liability for payments. To do this, the counterparty will calculate:

- what each supplier has been invoiced to pay the counterparty in interim rate and reserve fund payments in the relevant quarter; minus
- each supplier's liability for payments in the quarter, according to their market share

This process will show the amount that each supplier is owed by or owes to the counterparty – i.e. whether it has paid the counterparty more or less in interim payments (including the reserve fund lump sum) than its underlying liability for payments. This amount is then likely to be offset against the amount of money required for the following quarter's reserve fund payment.

Data reconciliation

The amount that suppliers must pay the revenue collection counterparty depends on the volume of metered electricity generation and supply on each day of a levy period.

Within the CFD regime, EMR Settlement Ltd ('EMRS') currently performs the role of the CFD settlement provider. EMRS is a wholly owned subsidiary of Elexon Ltd ('Elexon'), who are in turn owned by the National Grid ESO Ltd.

EMRS are responsible for carrying out processes that enable supplier payments to be calculated and settled corresponding to each suppliers' market share. This includes collecting data on the volume of electricity supplied, (referred to as metered data) on each day of the levy period.

The data relating to each suppliers' share of payments are updated on a regular basis as more up to date meter readings are obtained. It typically takes 14 months from the day of generation or supply for metered data to be finalised. Until this data is finalised suppliers will be billed and invoiced on the basis of interim data provided through a standard industry process under the Balancing & Settlement Code ('BSC'), which is managed by Elexon (who is referred to as the 'BSCCo').

It is intended that EMRS will be the settlement provider under nuclear RAB and carry out these actions under the BSC given that they already perform these functions in relation to the CFD regime. The revenue collection counterparty will use the updated supplier metered data to adjust the amounts owed by suppliers to the revenue collection counterparty (or vice versa) on a regular basis.

Operational costs levy

Suppliers will be liable for the operational costs of the revenue collection counterparty. The proportion paid by suppliers will be split on the basis of how much electricity each supplier has supplied during the period specified.

The first operational cost period will be from the date of entry into the first revenue collection contract by the revenue collection counterparty and ending on the earliest 31 March to occur after that date (if the contract is entered into on 31 March then ending on that date). The operational cost period for any subsequent period would then begin on 1 April in a year and end on 31 March in the following year.

For each operational cost period the operational costs levy will be recovered from suppliers once relevant supplier data is available for each day that the relevant supplier supplies electricity. The operational cost periods are aligned to financial years for which an operational costs levy is applicable, and the operational costs levy payment will be collected daily along with the supplier obligation.

These Regulations contain the operational costs levies for three years of operational costs periods between 1 April 2022 to 31 March 2025 to mirror the operational costs levy cycle under The Contracts for Difference (Electricity Supplier Obligations) Regulations 2014. As it is expected that the revenue collection counterparty's costs will change over subsequent operational costs periods, the Department expects to conduct consultation on proposals to amend the operational costs levy rates (as set out in these Regulations) applicable over forthcoming years, with such amendments to the Regulations made through Parliament in accordance with the affirmative procedure. It is anticipated that the amendment to the operational costs levy will be made in early January of a three-year

period to allow for the operational costs levy to be in force by the beginning of the next three years of operational costs periods (1 April).

Should a supplier fail to make an operational levy payment by the due date interest will be charged on the amount outstanding.

If the revenue collection counterparty's expenditure during an annual operational cost period is less than income from the levy, any surplus at the year-end will be refunded to suppliers. The rebate will be based on suppliers' overall market share in the financial year and will be reimbursed after the end of that year (though this may in practice be offset against other payments due from suppliers under the Regulations).

Direction by Secretary of State

The Secretary of State may direct the revenue collection counterparty to offer to enter into a revenue collection contract with a designated nuclear company under Section 18 of the Act. These Regulations require that the direction must include the full contract terms on which the revenue collection counterparty is to offer to contract (including terms dealing with the circumstances in which the revenue collection counterparty must make payments to the relevant licensee nuclear company (or vice versa)). The revenue collection counterparty will not be able to amend the revenue collection contract without prior written consent of the Secretary of State. Additionally, these Regulations enable the Secretary of State to revoke a direction before it has been accepted by the designated nuclear company, in which instance the revenue collection counterparty is obliged to immediately withdraw its offer. Under the provisions of the Act, any modifications to the designated company's licence (RAB licence) will only come into effect once the revenue collection contract has been entered into.

Information sharing provisions

Under RAB revenue mechanics it is important that there is proper information sharing between relevant stakeholders, notably the confirmation of payments by the Authority to the revenue collection counterparty (under the terms of, or pursuant to, the revenue collection contract). To that end, these Regulations include provisions enabling information sharing between various persons including, among others, the Authority, revenue collection counterparty, suppliers, CFD Counterparty and the Secretary of State.

Use of RAB model and other financing/funding options

In line with recommendations from the National Audit Office and Public Accounts Committee, these Regulations establish the RAB model as an investible option for funding future projects by enabling investors to share some of a project's construction and operating risks with consumers and taxpayers. The RAB model has the potential to significantly reduce financing costs. Financing costs are the main driver for nuclear project costs, and hence the overall cost of a nuclear project for consumers could be reduced by using the model. The illustrative costs of building and financing a new nuclear power plant using the RAB model as compared to a CFD are outlined in paragraphs 72-75 and Tables 2-4 of the impact assessment accompanying the Act.[1] Section 4.1 of that impact assessment, and Annex 3 to the impact assessment for this statutory instrument sets out a summary of the modelling assumptions.

[1] https://publications.parliament.uk/pa/bills/cbill/58-02/0174/ImpactAssessment.pdf

The RAB model is also expected to help facilitate private investment into new nuclear projects, which are an important part of a low-carbon, low-cost and resilient electricity system that will help in meeting emission reduction targets and ensure energy security.

Decisions as to the most appropriate funding model for any new nuclear project will continue to be made on a case-by-case basis, taking into account factors such as what funding model is likely to be investible, the relative maturity of the project (e.g. is it operating or still to be constructed), and value for money considerations.

Costs associated with 'regulated revenues', e.g. decommissioning

Prior to the commencement of construction, it is a legal requirement (in accordance with the Energy Act 2008) for a nuclear site licensee to have a Secretary of State approved Funded Decommissioning Programme ('FDP') in place. The purpose of the FDP is to ensure that the nuclear site licensee meets their full costs of decommissioning and waste management and that the recourse to public funds is remote.

Under the RAB model the relevant licensee nuclear company would be allowed to receive revenues in respect of activities related to the design, construction, commissioning, and operation of the relevant nuclear project, including its activities in complying with any obligations it has under an approved FDP. These revenues would be determined by the Authority.

8. European Union Withdrawal and Future Relationship

This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

9. Consolidation

There are no plans to consolidate the relevant legislation.

10. Consultation outcome

The policy set out in this instrument was subject to an 8-week consultation by the Department. "Revenue stream for the Nuclear RAB model: Consultation in respect of revenue regulations relating to the implementation of the nuclear RAB model revenue stream"[2] was published on 14 June for stakeholders to provide feedback.

Overall, the Department received 40 responses to the consultation from organisations and members of the public. Most respondents were broadly content with the similarities to the CFD regime and the proposed RAB specific mechanics, suppliers however expressed their preference for a longer notice period for quarterly levy rates (see paragraph 13.4). Members of the public and community groups expressed concern that these RAB levies could place undue burden on vulnerable consumers and there was concern over replicating the existing Energy Intensive Industries (EII) exemption but not having measures to protect vulnerable consumers. The Government's response was that such protections should be afforded through holistic support rather than through provision in the Regulations, as set out in the Government response to the consultation. This would involve looking at all cost drivers for energy bills and considering how best to mitigate these as a whole, rather than targeting individual schemes and policy costs (such as nuclear RAB costs under this legislation). This approach ensures wider protection and

[2] https://www.gov.uk/government/consultations/revenue-stream-for-the-nuclear-regulated-asset-base-rab-model

support for a range of vulnerable consumer groups across different policy areas, for example, measures such as the Energy Price Cap, and schemes such as the Warm Home Discount, Winter Fuel Payments and Cold Weather Payments (which offer support with energy bills).

As required by section 25 of the Act the Scottish Ministers, Welsh Ministers, nuclear companies designated under section 2(1) of the Act, electricity suppliers, the Authority, the national system operator (i.e. National Grid ESO) have been consulted. Additionally, in accordance with section 25(1) (h) of the Act, the consultation was open to responses from the public (since this was the first time we had consulted on policy for these Regulations, which could support multiple nuclear projects benefitting from the RAB model in the future).

The Government response to the consultation[3] informing this instrument will be published to coincide with the laying of regulations in Parliament. The Government response sets out the views of stakeholders in response to the previously proposed policy positions, and an explanation of the final policy decisions taken.

11. Guidance

None.

12. Impact

The impact on business, charities or voluntary bodies is as a result of the levies charged under these Regulations. Costs to suppliers associated with the supplier obligation can be categorised as administrative and financing costs. Financing costs to suppliers expected to be passed on to customers include collateral financing costs, insolvency risk, a risk premium added to customer tariffs, and up-front reserve fund financing costs. Operational and financing costs are expected to be passed onto consumers in the form of higher bills. In terms of protections around insolvency or discontinuation, Part 3 of the Act introduced a Special Administration Regime (SAR) for relevant licensee nuclear companies. Given that under a RAB model, which facilitates private investments, consumers will be contributing from the beginning of the construction phase, the purpose of the SAR is to provide additional protections to consumers in the unlikely event of an insolvency. The Act will enable the Secretary of State to appoint a special administrator, who has the objective of commencing or continuing electricity generation, to ensure that consumers capture the intended benefit of the construction and operation of the nuclear power station.

The impact on the public sector is in respect of the Authority and the current designated revenue collection counterparty, LCCC, which is a private company limited by shares and wholly owned by the Secretary of State. These Regulations impose new duties on the current designated revenue collection counterparty in collecting payments from suppliers to meet their obligations under revenue collection contracts (in accordance with the various provisions to enable these duties such as setting interim levy rates, collecting reserves/collateral, invoicing and enforcing supplier payments etc, as set out in the paragraphs above 7.1 – 7.33).

A full Impact Assessment is submitted with this memorandum and published alongside this Explanatory Memorandum on the legislation.gov.uk website.

[3] https://www.gov.uk/government/consultations/revenue-stream-for-the-nuclear-regulated-asset-base-rab-model

13. Regulating small business

The legislation applies to activities that are undertaken by small businesses.

To minimise the impact of the requirements on small businesses (employing up to 50 people), the approach taken is that we engaged and consulted with suppliers on our policy proposals, see paragraph 10.2 above, and fed their responses into our policy proposals for these Regulations.

During the consultation process we ran an engagement exercise with electricity suppliers during the consultation period to seek their views on the proposals set out in the consultation. We sought evidence from suppliers of projected increases to financial and administrative costs as a result of these Regulations. Suppliers did not provide cost estimates in response to this question, however, they did provide comments on the nature of costs they would likely incur. This included costs related to internal forecasting of non-commodity costs (NCCs), commercial considerations on how to pass NCCs through to customer pricing, dealing with the daily receipt of invoices and ensuring collateral is available. Suppliers noted that by replicating much of the CFD revenue mechanics, most of the administrative costs arising from nuclear RAB would be minimal as it could be wrapped into existing processes (e.g. forecasting, billing etc.) related to CFDs.

Suppliers' preference was to have 3 months' notice of a forthcoming quarterly levy rate (as done for CFDs) instead of the 1 month notice under these Regulations. Their main areas of contention were regarding the amount of time it would give them to price tariffs and arrange for credit cover. For example, they expressed that they would use the interim levy rate to determine the price of their tariffs for fixed price contracts for customers. Suppliers stated that they would usually begin quoting prices months in advance of the start of the contract.

The basis for the final decision on what action to take to assist small businesses was to balance two things (1) the need to allow for the processes involved in the Authority confirming payments which the revenue collection counterparty would need to pay to/receive from the relevant licensee nuclear company (as set out in paragraph 13.6), alongside (2) giving suppliers adequate notice of forthcoming interim levy rates, reserves and collateral.

The reason for the 1 month (i.e. 30 days) notice period for interim levy rates (and shorter notice for the suppliers' reserve amounts) under these Regulations is to allow for the sequence of processes that need to take place before the counterparty can give suppliers notice. This includes the Authority calculating the payments in accordance with the revenue collection contract, communicating the same to the revenue collection counterparty, following which the counterparty would need to calculate an interim levy rate and total reserve amount to apply over the quarterly period to ensure it can meet all its payment obligations to relevant licensee nuclear companies.

The Department considers the 1-month notice period of a forthcoming interim levy rate and total reserve amount to be preferred in the context of smaller suppliers in that it would allow the Authority to confirm to the revenue collection counterparty more accurate payments (rather than relying on forecasts/projections which could be inaccurate), with the aim of potentially reducing fluctuations over the next quarterly interim levy rate and with less risk of amending the interim levy rate while it is in force (through provisions in these Regulations governing in-period adjustments).

14. Monitoring & review

The approach to monitoring of this legislation is in the context of information sharing provisions, as set out in paragraph 7.33 above.

Given their role in the designation and licence modification processes under the nuclear RAB model, and their powers to modify a relevant licensee nuclear company's licence in certain circumstances following entry into a revenue collection contract, these Regulations include provisions allowing the Secretary of State to request certain information from certain persons in connection with revenue collection contracts. It is intended that this would cover relevant information from the revenue collection counterparty, the Authority, the national system operator, relevant licensee nuclear companies, and/or a nuclear administrator appointed in the unlikely event that the relevant licensee nuclear company enters into special administration. There is also provision for the revenue collection counterparty, the Authority and the nuclear administrator to be able to provide information to the Secretary of State where not explicitly requested by the Secretary of State should they consider it necessary for the Secretary of State to carry out its functions. The Secretary of State may also request advice (as well as information) from the revenue collection counterparty, the Authority and national system operator.

These provisions will allow the Secretary of State to have some visibility in respect of the revenues being channelled to relevant licensee nuclear companies. Such information provided to the Secretary of State could inform wider policy making decisions on future designation applications for nuclear RAB project companies, or other matters, and is important given the scale, cost and length of nuclear RAB projects.

In terms of the monitoring of the operational costs levy, prior to financial year 25/26 the Department intends to conduct a consultation for the operational costs levies for the following three financial year period. Forthcoming operational levies will be implemented through an amendment to the Regulations and subject to the affirmative resolution procedure.

The instrument does not include a statutory review clause and, in line with the requirements of the Small Business, Enterprise and Employment Act 2015, Secretary of State, Grant Shapps, has made the following statement:

> "It is not considered appropriate to include a statutory review clause for policy reasons – in order to retain confidence in the stability of the revenue stream. There are existing review plans for the operational costs levy rates to be next reviewed in 2025, and internal plans to monitor and evaluate the effectiveness of the RAB policy as necessary or appropriate."

15. Contact

Saira Khan at the Department for Business, Energy and Industrial Strategy Telephone: 07557256738 or email: saira.khan@beis.gov.uk can be contacted with any queries regarding the instrument.

Declan Burke, Director for new nuclear projects at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.

Grant Shapps, Secretary of State for the Department for Business, Energy and Industrial Strategy, can confirm that this Explanatory Memorandum meets the required standard.