Electricity Settlements Company

Annual Report 2016/17

Capacity Market transactions and assurance

Our vision…

is to be at the heart of the delivery of the UK's goals for secure, affordable and sustainable energy

ESC's Guiding Principle is **to maintain market participants' confidence** in the Capacity Market settlement process and **minimise costs to consumers.**[1]

Electricity Settlements Company (ESC) is an independent, non-profit private company owned by the Secretary of State for Business, Energy and Industrial Strategy (BEIS) and established to manage the financial processes under the Capacity Market scheme. Our role contributes to the government's objective of "ensuring that the country has secure energy supplies that are reliable, affordable and clean".[2]

"The Capacity Market contributes to security of supply by ensuring that there is sufficient reliable capacity to meet customer demand."[3]

[1] https://lowcarboncontracts.uk/corporate-governance
[2] DECC Consultation of further reforms to the Capacity Market, 1 March 2016, available at https://www.gov.uk/government/uploads/system/uploads/attachement_data/file/504217/March_2016_Consultation_Document.pdf
[3] DECC Single departmental plan: 2015 to 2020 available at https://www.gov.uk/government/publications/decc-single-departmental-plan-2015-to-2020

Contents

Highlights for 2016/17

Capacity Market scheme[4]

Managing payments

109 meters tested

for capacity providers successful in the 2015 Transitional Arrangement Auction

first Capacity Market payments

commenced in October 2016

£211m

total credit cover managed across three separate auctions

Delivering excellence

advised BEIS

on changes to Capacity Market regulations

improved Capacity Market settlement system

following industry wide consultations by BEIS and Ofgem

IT system migration

onto an independent platform in October 2016

2016/17 has been about starting operations, managing, maintaining and monitoring – going into a phase of business as usual but still having a lot of firsts… it's been a dynamic year!

Neil McDermott
Chief Executive

[4] 133 participating companies holding between them a total of 1,585 valid capacity agreements, of which 46 were receiving capacity payments in 2016/17

Chairman's foreword

A new phase

The operations of ESC continue to be delivered by our sister company LCCC, which allows efficiencies through operational synergies. It has been pleasing to see the growing maturity of the two organisations as we have moved into a new phase of activity.

The Capacity Market scheme is now fully operational, with payments commencing to capacity providers in late 2016. We have been involved in three Capacity Auctions this year, all on different timescales, as well as managing the first payments to the capacity providers successful in last year's Transitional Arrangements. This is against a backdrop of ongoing changes to the payment mechanism as a result of Ofgem's annual consultation process.

Delivering key services

We have worked extremely hard behind the scenes to enable the Capacity Market to operate effectively, through coordination across multiple delivery bodies.

There have been complexities and challenges on the way, unsurprising since we are doing many things for the first time. We have had many interactions with Demand Side Response providers coming through the Capacity Market auctions and worked hard to ensure that scheme requirements on meter assurance are proportionate to the risks posed by the various types of participants. We have also implemented a number of further changes to the settlement system as a result of Ofgem's annual consultation process. This year, we started making payments to capacity providers for the first time and by the end of the financial year we had paid 46 capacity agreement holders a total of £9.2m, for more than 600MW of reliable capacity to be made available as required. Despite the scale and complexity of the activities we are managing, we have consistently met all our operational targets, delivering new capabilities successfully and within agreed timescales.

Our people

We have an experienced board which is adding tangible value to the work of both LCCC and ESC as the companies have worked through a variety of demanding issues. I am grateful to my colleagues for their insights and commitment. I should also like to thank all our staff for their hard work and dedication during a time of considerable challenge and their success in meeting all our deadlines.

Looking ahead

Our vision is to be at the heart of the delivery of the UK's goals for secure, affordable and sustainable electricity. We are constantly looking for opportunities to add value in achieving these goals.

We are particularly focused on looking for simplifications and further efficiencies in delivering the Capacity Market scheme. For example, we are making proposals to streamline settlement processes.

As the market evolves, we are increasingly working with the regulator, Ofgem, alongside our core delivery partners BEIS, National Grid and EMRS. We stand ready to collaborate further to respond to technological change across the energy sector. We are particularly mindful of the growing importance of electricity storage and the increasing appetite for decentralised and smarter energy solutions that give communities a personal stake and greater control. We also see cross sector innovation and the electrification of heat and transport as important drivers of change in the future. All this will undoubtedly impact on electricity suppliers and affect the way the market operates.

In the year ahead, we will continue to deliver the Capacity Market scheme effectively and efficiently and to assist BEIS by advising on how to futureproof it. We look forward to achieving further success and supporting the government's objectives of ensuring security of supply, reduced costs to consumers and decarbonisation.

Dr Martin Read CBE
Chairman

Glassenbury battery park (artist's impression)
has a 15-year agreement to provide electricity during stress events

Chief Executive's foreword

Making it happen

It has been a busy year, in which we have made great strides in delivering our milestones and making improvements as we move into effective operational delivery of the Capacity Market scheme.

Running the Capacity Market

During 2016, we targeted the rollout of the settlement system Capacity Market functionality for mid-2016. Consequently, we were ready to start making capacity payments on time and in line with all requirements, and successfully paid our first capacity providers from the Transitional Arrangements Auction held earlier in 2016. This year we have paid out a total of £9.2m across 46 capacity agreements, for more than 600MW of available capacity. Additionally, as a result of Ofgem's annual industry consultation process, we implemented a number of settlement system improvements.

Alongside delivering settlement operations, we met the challenge of managing up to £211m credit cover for three capacity auctions; the Transitional Arrangements Auction, the T-1 (one year ahead) Capacity Auction and the T-4 (four year ahead) Capacity Auction. It has been interesting to see a significant growth in the number of Demand Side Response providers holding capacity agreements, which required us to assure 109 metering systems to check that they were compliant with the rules and regulations governing the Capacity Market. Despite the complexity of the activities, I'm pleased to say that we met all our operational targets and delivered new capabilities successfully and within agreed timescales and budget.

Delivering efficiencies

During the year, ESC collected just under £4.3m from suppliers under its operational cost levy, but spent around £2.9m, which means that we can return almost £1.4m to suppliers. We are pleased that we have been able to deliver our operational role not only within budget, but in such a way that we can return monies to suppliers, with a significant amount of these monies resulting from savings and the recovery of a sum from the sub-contractor retained to provide the original settlement system.

To drive efficiencies through the use of shared systems, ESC outsources the performance of its day to day operations to LCCC. This has enabled ESC to deliver synergies with the CFD operations and minimise costs to consumers. LCCC's expertise on the settlement side is growing. It has proposed changes to the settlement regulations to better align CFD and Capacity Market settlement, which have now been implemented and are helping to ensure that we minimise the burden of the schemes on electricity suppliers, and ultimately consumers.

Looking ahead

Our strategy has been to focus on delivery first and this is serving us well, but we are also committed to proactively influencing and supporting change, as the scheme will undoubtedly need to adapt to the evolving market.

ESC will continue to work with BEIS, National Grid and Ofgem to continue to improve the effectiveness and efficiency of Capacity Market processes.

Our vision remains to be at the heart of the delivery of the UK's goals for secure, affordable and sustainable energy. We continue to pursue our mission to build confidence in the Capacity Market scheme through effective commercial delivery and continuous improvement. That means we must become more resilient and ensure that our current delivery standards are sustainable going forward. It's an exciting time ahead!

Neil McDermott
Chief Executive

©UKPowerNetworks
Leighton Buzzard – inside a battery storage facility that received capacity payments in 2016/17

Corporate report

Our role

ESC plays a key role in supporting the government's objective to ensure the UK has a secure and resilient energy system, by managing the financial transactions and associated assurances required pre- and post-auction under the Capacity Market scheme.

The Capacity Market is designed to provide payment for reliable sources of capacity, to ensure that electricity is available when needed and to provide sufficient backup for more intermittent or inflexible low carbon generation sources. The Capacity Market has also been designed to support the development of more active demand management in the electricity market.

We are responsible for Capacity Market payments and related activities. This includes holding credit cover for auction participants and conducting meter tests for successful applicants (which are required before they can start receiving payments).

Our sister company LCCC delivers all Capacity Market activities on behalf of ESC under a cost-sharing arrangement, enabling efficient governance of settlement across the Capacity Market and CFD schemes through management of a shared settlement service. ESC's key responsibilities are:

Managing transactions

- providing accountability, governance and delivery of settlement operations under the electricity Capacity Market payment regulations
- holding and monitoring credit cover from applicants in Capacity Auctions and Transitional Arrangements Auctions.

Providing assurance

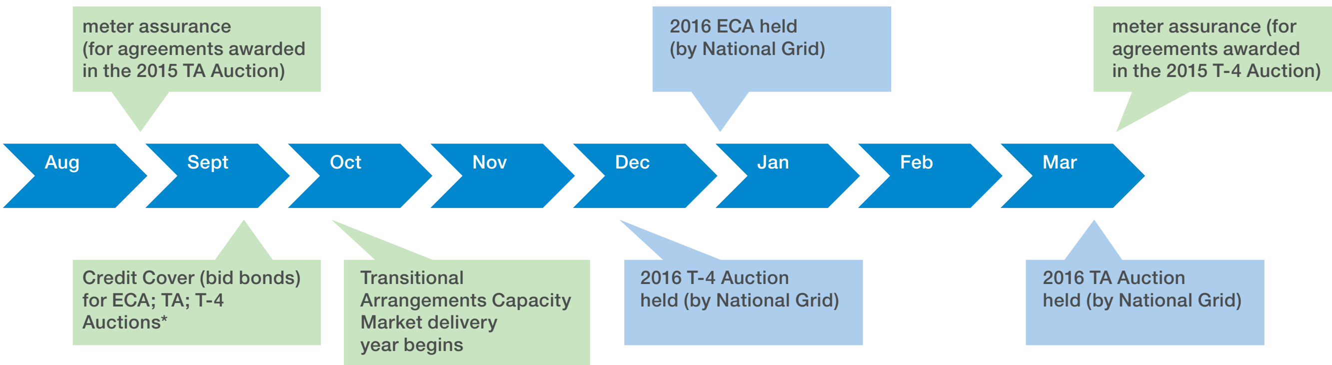
- ensuring meter checks on capacity providers
- resolving Capacity Market settlement disputes
- monitoring and reviewing the rules and regulations relating to the settlement functions of the Capacity Market.

2016/17 activities

The Capacity Market settlement process has been gathering momentum throughout the year, with LCCC making payments to capacity providers on ESC's behalf. This means that the Capacity Market scheme is now fully operational and contributes to security of supply by ensuring that there is sufficient reliable capacity to meet the demand for electricity by consumers.

In addition to making payments to capacity providers, we have been holding and monitoring credit cover from applicants in Capacity Auctions and Transitional Arrangements Auctions, ensuring that meter checks are undertaken, and advising the government during consultation periods relating to the regulations for Capacity Market settlement.

Key Capacity Market events for 2016/17



*see bottom of page 9 for more information

First year of operations...

Chart: total cost of capacity agreements by auction and year[5]

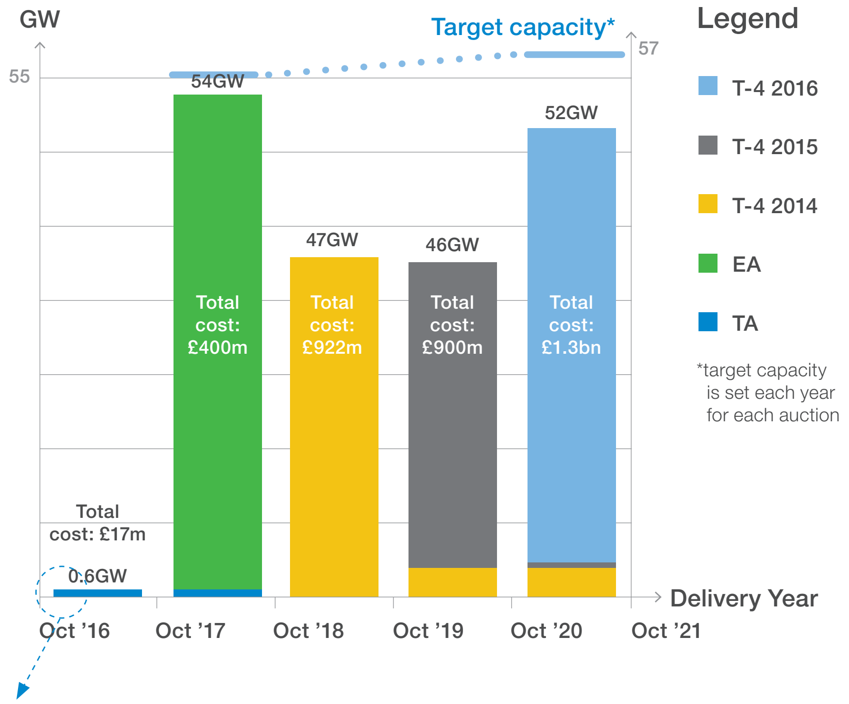


Table: 2016/17 Capacity Market outcome

Scheme	Outcome	Total payments made by ESC to capacity providers	Total ESC operational cost
Capacity Market	620MW of reliable capacity provided	£9.2m	£2.9m

Making a success of the Transitional Arrangements

From 1 October 2016, small scale generation (2MW to 50MW)[6] and Demand Side Response received payments, having secured agreements a year earlier under the 2015 Transitional Arrangements Auction. To ensure this ran smoothly and provided confidence to a new section of the market, LCCC on behalf of ESC ensured that:

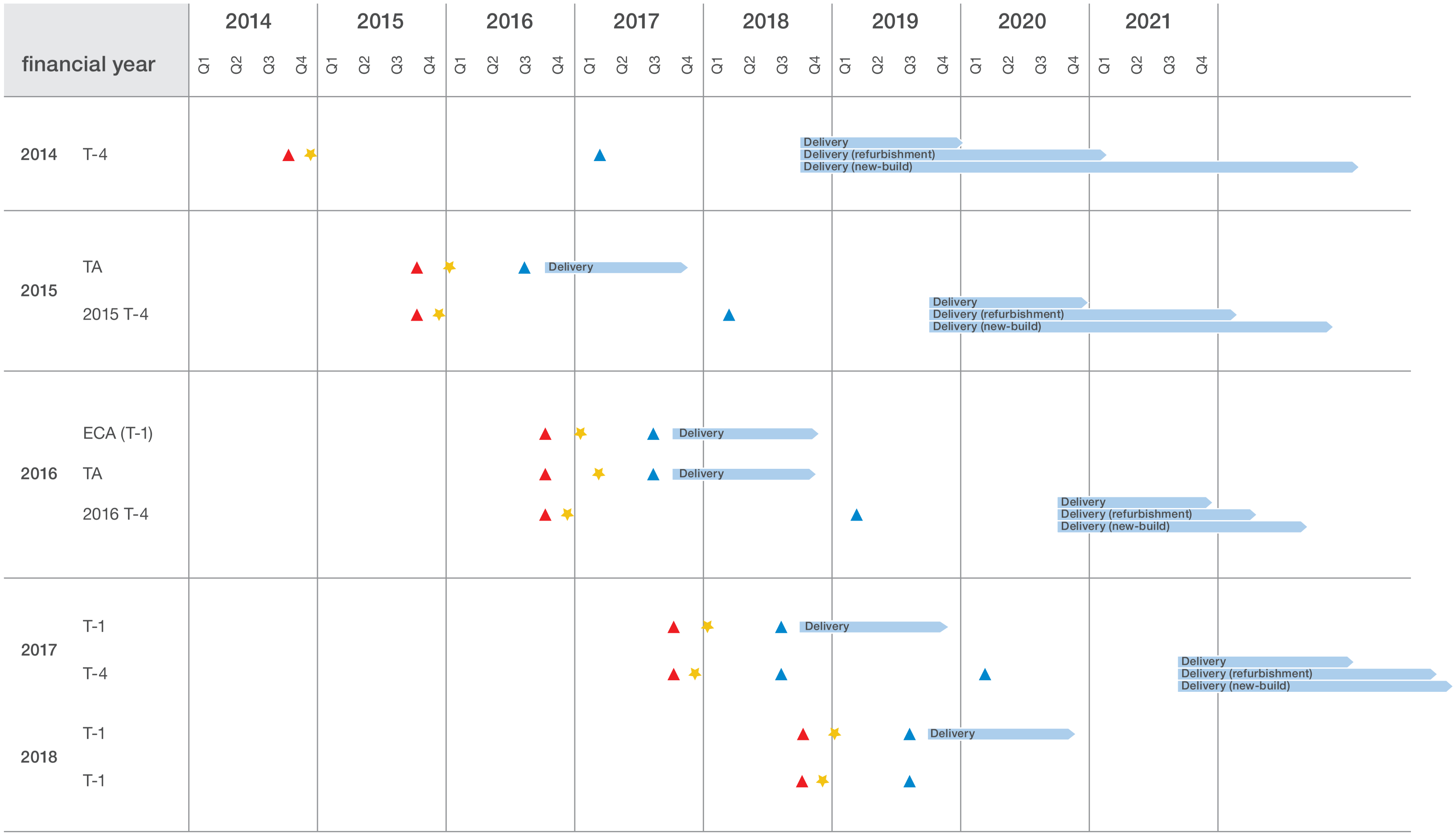
- 109 meters were tested
- £1.5m of payments (on average) per month were made for 620MW of capacity.

Capacity Auctions

Capacity agreements are entered into with successful applicants (both generators and Demand Side Response providers) after a Capacity Auction. A Capacity Auction relates to delivery of capacity four years in advance (known as T-4 Auction) or for delivery in the following year (known as a T-1 Auction). The capacity agreements awarded in the first T-4 Capacity Auction will be delivered in 2019/20.

[5] LCCC estimate based on input data sources taken from www.emrdeliverybody.com and assuming that electricity suppliers pass on the full costs of the Capacity Market charge and operational costs levy equally to all consumers. Note this does not include operational costs of other delivery partners such as BEIS or National Grid.
[6] National Grid, Final Auction Results: Transitional Capacity Market Auction for 2016/17, Appendix A – results by CMU, January 2016, pp9-10 https://www.emrdeliverybody.com/Capacity%20Markets%20Document%20Library/Transitional%20Auction%20 2016%20-%20Final%20Results.pdf

Expected Capacity Market activity to 2021/22



Legend

- Pre-auction credit cover submission deadline
- Auction
- Metering tests deadline for non-balancing and settlement code
- Delivery — Delivery periods (payments)

Notes

- **ECA:** Early Capacity Market Auction (a type of T-1 Auction) to cover any gaps in capacity in 2016/17. BEIS, Capacity Market: Consultation on Reforms to the Capacity Market Government Response, 2016, p9 available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/504050/Govt_response_to_the_consultation.pdf
- **T-1** and **T-4 Auctions** are described in the Capacity Auctions box on page 8. T-4 (2014) Auction was for delivery year 2018/19.
- **Delivery:** refers to when capacity generation becomes operational, capacity providers can have 1-year; 3-year (for refurbishment of exisiting facilities) and 15-year contracts (for new-build capacity generation)

Working with BEIS to drive change

"Under EMR, the Capacity Market provides security of supply. It does this by giving financial payments to encourage existing capacity to remain operational for longer and new peaking plant to back up the low carbon generation built under the CFD scheme."

ESC prepares for consultations on regulation and rule changes brought in by BEIS and Ofgem on the Capacity Market scheme, for example secondary trading. We also engage with National Grid who administers the auctions.

Secondary trading will allow holders of Capacity Market agreements to trade their obligation with participants who may or may not hold such agreements, but are fully registered to participate in the Capacity Market scheme. In effect it allows Capacity Market agreement holders to manage the risk of not being available to provide the required capacity when called upon, by having a Capacity Market applicant who can pick up the shortfall. This should help to deliver security of supply and keep costs down.

From late 2017, secondary trading will give the Capacity Market scheme further market based flexibility aimed at ensuring security of supply and preventing the lights going out.

Omer Ahmad
Capacity Market Policy Delivery Manager

- The first T-4 Auction in 2014 awarded capacity agreements worth approximately £1bn. ESC will commence payments under those agreements from October 2018.
- Secondary trading will be implemented from October 2017.

With the Capacity Market, there has been ongoing yearly consultations and regulations on some complex issues. We must continually deliver while ensuring that the operational environment reflects the regulatory environment.

Nick Skates
former policy manager

Metering: custodians of securing energy

Ensuring the metering assurance regime is fit for purpose.

"The deadline for awarding metering certificates was set one month ahead of the start of the first delivery year. Because of the way the test groups are provided in list form by National Grid, there was a potential that we would get thousands of metering requests to be completed in the space of a couple of weeks!

To avoid a late spike in requests for meter tests, we conducted engagement work with capacity providers to ensure they understood their obligations and made their requests at an early stage. We also ensured there was sufficient resource in place with our delivery partners (Ofgem/EMRS/National Grid) to respond effectively. Additionally, we worked towards a more sustainable solution by developing a risk-based sampling approach in consultation with Ofgem as a contingency plan in case there was an overwhelming quantity of meters requiring tests.

As a result, Ofgem agreed to a change in the rules which gave greater flexibility to our operations. This means the rules are now fit for purpose should we need to deploy risk-based sampling in the future."

Matt Johnson
ESC Settlement Lead

Our last metering assurance deadline was 31st March 2017 for agreements awarded in the 2015 T-4 Auction. 25 meters were tested; a total of 954MW of capacity.

Environment report

The company does not have any employees.

Its role is performed by its agent, LCCC. The company accordingly does not itself have any Scope 1, Scope 2, or Scope 3 emissions. The company is, however, committed to ensuring its sustainability objectives and works closely with LCCC in relation to environmental matters.

Strategic report

The company

ESC plays a key role in the implementation of the Capacity Market scheme by delivering the credit cover, meter assurance, levy collection and settlement functions required for the operation of the Capacity Market. The Capacity Market was introduced by the government in August 2014 and aims to ensure security of supply in future years while minimising the cost to consumers.

The company's strategy is to focus on delivery first, given ESC's crucial operational role in key elements of a major government scheme, while also being committed to proactively influencing and supporting change as the Capacity Market scheme adapts to the needs of the evolving market. The company's mission is to build confidence in the Capacity Market scheme through effective delivery and continuous improvement.

This mission reflects the company's Guiding Principle to, in carrying out its functions, activities and role, seek to maintain market participants' confidence in the Capacity Market scheme and minimise costs to consumers.

This Guiding Principle and ESC's role as an operationally independent company are fundamental to its work and align with its strategy to focus on delivery first, given ESC's critical operational role and the importance of its offering to the electricity sector.

The principal activities of the company are further described on pages 3 to 11 and pages 13 to 16. The company's functions are performed through LCCC, which gives cost savings and efficiencies due to the synergies between the operations of the two companies. The company has no plans to change this business model.

The company's performance

The company monitors its progress against its strategic objectives through key performance indicators ("**KPIs**"). The company's KPIs for 2016/17 have been defined by reference to the key milestones or targets required for it to perform its role and achieve its strategic objectives. The KPIs for 2016/17 are set out below.

Key performance indicator	Description of performance
Financial and budget performance	The financial and budget performance of the company was well managed with: • the company successfully delivering within its operational and capital budgets, as a result ESC will be returning £1.4m to suppliers • no 'material issues' were identified in the period 9 and year end financial audits of the company • effective controls in place to identify, monitor and manage strategic risks, with the mitigating actions for strategic risks being completed in a timely manner and with >90% of mitigating actions being completed by their target date.

Capacity Market settlement systems	The company has successfully and efficiently managed its Capacity Market settlement operations, including: • by the delivery on time of a well functioning Capacity Market settlement system that achieves collections and capacity provider payments in accordance with the Capacity Market rules and regulatory requirements • collecting 100% of credit cover from eligible Capacity Market applicants in accordance with the requirements relating to Capacity Auctions and Transitional Arrangements Auctions • ensuring that the cost per capacity agreement shows a year on year improvement (adjusted for external factors such as the termination of capacity agreements or limited Capacity Market agreement volume) • establishing a baseline measure and ensuring that, subject to externalities, >/=95% of issued invoices, notifications and payments are accurate and that </=2% of invoices and notifications were issued late by more than 2 business days.
Capacity Market metering assurance	The company has delivered on its metering assurance responsibilities effectively, efficiently and on time, including: • by awarding a meter assurance contract to a reputable supplier • implementing a meter assurance framework that enables the company to meet its metering assurance regulatory requirements • agreeing with BEIS, National Grid and Ofgem processes for the more efficient and effective management of Capacity Market metering assurance.
Corporate governance and strategy – including leadership of company, organisational vision and structure	The company has implemented good and effective corporate governance processes, including: • effective external communications with stakeholders – ensuring that stakeholders confidence is increased through the delivery of communications and engagement with sector (as measured by rolling improvement in feedback from stakeholder events and other engagement activity such as webinars and conducting a perception survey) • by the refreshing of the strategy and business plan on an annual basis, with the business plan being aligned to and supporting the implementation of the strategy. The successful delivery of the first limb of the strategy of "delivery first" is demonstrated by the effective, efficient, timely and within budget delivery of Capacity Market administration, Capacity Market settlement operations and the other matters referred to on pages 3 to 11 and 13 to 16 of this report. The second limb of the strategy of "influencing and supporting change" is demonstrated by matters including the company's input into aligning the Capacity Market and CFD settlement processes, providing input into BEIS consultations and the other matters referred to in pages 3 to 11 and 13 to 16 of this report.

Overview of company's role

ESC is a BEIS departmental arm's length body set up to administer critical elements of the Capacity Market.

The Capacity Market was introduced to ensure that there is sufficient investment in the overall level of reliable capacity to provide secure electricity supplies to meet peak demand – e.g. during cold, windless periods. The Capacity Market was designed by BEIS to provide capacity providers holding capacity agreements with a steady, predictable revenue stream upon which they are able to base their future investments. This revenue is paid as "capacity payments".

Capacity agreements are arrangements between National Grid (as system operator) and capacity providers. In return for the predictable revenue stream generated by the capacity agreements, capacity providers must deliver energy at times of system stress or face penalties.

Capacity providers can be new or existing generators, electricity storage providers and/or significant users of electricity who provide voluntary "demand side" reduction. Potential capacity providers compete in Capacity Auctions and/or Transitional Arrangement Auctions to secure capacity agreements. The auction sets the level of the capacity payment.

The company's primary role is to "settle" the Capacity Market by making capacity payments to capacity providers who hold capacity agreements. It may also receive payments from capacity providers in the form of penalties should they not make this capacity available.

The company's main function is therefore to perform the levy collection and settlement role set out in the Electricity Capacity Regulations 2014 (as amended) and the Electricity Capacity (Supplier Payment etc.) Regulations 2014 (as amended) (the "Regulations").

The company also collects credit cover provided by applicants to Capacity Auctions and Transitional Arrangements Auctions, paying the credit cover back to unsuccessful applicants and processing the credit cover of successful applicants in accordance with the requirements of the Regulations. This credit cover provides some security for the performance by capacity providers of their obligations under the Regulations.

The company also undertakes meter assurance activities to check that capacity providers are providing the capacity they are required to provide under their capacity agreements. These activities are mainly undertaken via outsourced subcontracting arrangements overseen by LCCC.

Financial overview

Capacity payments

The first payments to capacity providers, who were awarded agreements for the 2016/17 capacity year, were made in December 2016. The total costs relating to capacity payments made in the financial year was £9.2m.

The company obtains the funds to make payments to capacity providers from a levy upon electricity suppliers as set out in the Regulations. Suppliers are obliged to pay their levy within three working days of receipt of the invoice, but the company does not have to make capacity payments until 29 working days after the end of the relevant month. This insulates the company against cashflow timing issues.

The company calculates the difference between the amount of payments to capacity providers with the amounts collected from suppliers on a monthly basis. As at 31 March 2017, £2.8m Capacity Market supplier charge was due to be returned to suppliers.

In addition, suppliers must lodge credit cover as security against their failure to pay amounts for which they are liable. If, in due course, this 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 (i.e. the remaining suppliers have to make up the shortfall between them). As at 31 March 2017, the company held £1.05m in supplier credit cover. During the year £0.02m of supplier payments were mutualised to other suppliers.

Where the company receives penalty monies from capacity providers, it pays these monies to suppliers. If a capacity provider fails to pay an amount due from it and, as a result, the company does not make an expected payment to suppliers, the shortfall is borne by suppliers (i.e. it is shared between them). The company has no obligation to make up any shortfall.

Operational costs

The day to day operational costs of the company are funded by suppliers under the Capacity Market "settlement costs levy" that is set by the Electricity Capacity (Supplier Payment etc.) Regulations 2014 as amended.[7] The amount is updated annually by amending regulations made subsequent to a public consultation process. The settlement costs levy for 2016/17 was fixed at £4.3m and for 2017/18 is fixed at £6.2m.

The total net operating costs of the company for the year were £2.9m (2015/16: £2.7m). As a result of the financial performance in the financial year, the company will return £1.4m to suppliers for 2016/17 (2015/16: £1.2m).

The company has delivered its operational requirements within the budgeted levels of spend set in the relevant regulations. The company applies strong financial management in order to ensure that its commitments are managed within the timing of its collection of the settlement costs levy which funds its operational costs.

There have been a number of contributory factors to the company's performance, including lower than expected metering charges which has resulted in total savings of £0.3m. The company shares resources with LCCC, which are paid for by LCCC with the proportion of the costs related to the Capacity Market being recharged to ESC as further set out in note 2.6 to the financial statements.

A further reason for the lower cost base in the last year is a reduction of £0.3m in the depreciation charge associated with the settlement system, which reflects a delay in the commissioning date for the delivery of the fully automated system.

In addition, as a result of the delay in the build and testing of the original planned system, the contract between EMR Settlement Ltd (EMRS), as settlement services provider, and its then principal subcontractor was terminated on 9 November 2015. Following an agreement between the parties involved, £0.8m was received by ESC as its share of the termination settlement.

ELEXON Limited and its subsidiary, EMRS, through grant funding from BEIS, have invested a further £1m (2015/16: £1m) in improving the functionality of the settlement system. This investment was required to deliver a better CFD settlement operation.

[7] Regulations 9 and 10 of the "Electricity Capacity (Supplier Payment etc) Regulations 2014" and subsequent amendments: http://www.legislation.gov.uk/uksi/2014/3354/contents/made

Key judgements and estimates exercised in the preparation of the financial statements

As mentioned above, in November 2015 a decision was taken by EMRS to terminate the development contract for the settlement system with its principal contractor. As a result of this decision, the carrying value of the intangible asset was reviewed and subsequently adjusted to its recoverable amount. No further impairment of the settlement system was identified for the current financial year.

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

Viability statement

The directors have assessed the company's prospects, taking into account the company's current position and the principal risks faced by it over the projected business plan period of three years. The period of three years has been chosen as this is the time period over which the company has reasonable visibility of its strategy implementation and business planning and is the period for which BEIS has requested a three year business plan and budget.

The financial arrangements relating to the company minimise the risk of the company being unable to meet its liabilities. As set out in the preceding Financial Overview, the company is not obliged to make payments to capacity providers unless and until it has the funds to do so. The company also applies prudent financial management to ensure that its operating costs are covered by the settlement costs levy.

As part of the strategic planning process, the directors have analysed the regulatory and legal environment in which the company operates and do not foresee any changes that will significantly affect the finances of the company within the period of the three year plan. The directors have also carefully considered the way in which the company manages its principal risks which are set out on pages 17 to 19. They do not believe these risks will bring into question the company's viability.

Based on their analysis, the directors have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due.

Risk management – principal opportunities and risks

The board formally reviews the material risks facing the company and ensures that they are appropriately managed by the executive team. The board retains ultimate responsibility for the company's risk management framework, with oversight of the overall effectiveness of the risk management programme being delegated to the audit, risk and assurance committee. The company's internal audit function provides further assurance on the effectiveness of the internal controls relating to risk.

Risk management is embedded within the company's operational activities. The company's approach to risk management is further detailed in the Corporate Governance Report on pages 31 to 32.

The board considers the matters outlined below are, as at the date of this report, the principal risks and uncertainties that could adversely impact the company's reputation and operations and thus its ability to deliver against its strategic objectives.

Risk or uncertainty	Risk brief description	Main mitigating actions
Settlement services	There is a risk that the newly-built system and processes will not effectively deliver settlement services and that the increasing level of settlements will place an unanticipated strain on the system. There is also a risk that delays occur in the delivery of ongoing changes to the settlement system or that key processes are not fully designed, documented and fit for purpose or are delayed.	• Good project governance is in place • Discussions with BEIS to agree an implementation plan for policy changes to avoid delivery risk to the implementation of system change • All changes relating to the agreed change programme are impact assessed and implemented on agreed timelines • There is an interim agreement in place on roles and responsibilities in relation to Capacity Market settlement interfaces with BEIS and National Grid • A proposal for a longer term framework to support the Capacity Market (including the definition of roles and responsibilities across delivery partners) has been produced • Working level and executive level meetings are in place to coordinate deliverables involving delivery partners • A controls workshop is held with the settlement system delivery partner to obtain system and controls assurance • Controls assurance performance reporting is in place.
Policy and market change	There is a risk of policy and market change which impacts the strategy or operations of the company or requires additional operational activity for which the company has not been given the time to fully prepare.	• Regular shareholder meetings and liaison with government is in place • Staff members attend various government forums • There is ongoing industry engagement • The impact of potential policy and market change is assessed, including in relation to matters such as Brexit • Monitoring of potential policy and industry issues and consultations is ongoing • A company business design authority is in place to approve, monitor and assess change • Resource is in place to monitor, review and respond to consultations • Regular change board meetings take place with relevant bodies and delivery partners.
LCCC's delivery	There is a risk that LCCC is inadequately resourced and/or does not meet ESC's business needs.	The company has close oversight of and receives regular reporting on the delivery of ESC services, financial and risk management and internal controls.

Scheme fraud risk	There is a risk of fraudulent activity from individuals or third parties.	• Key finance controls and fraud controls are in place and monitored, including embedded segregation of duties in finance processes and systems access controls • Control environment assurance report on the settlement system controls has been obtained from an external adviser • A company fraud prevention officer is in place • Annual credit-worthiness checks for capacity providers are in place as part of a risk-based sampling approach • Fraud awareness and anti-money laundering training has been provided to the settlement services delivery partner • Internal audit function is in place and internal audit checks are being undertaken • Compliance and checking processes have been developed against a fraud control matrix • Metering assurance and inspection regime is in place • IT security is in place • A risk framework is being developed with the settlement services delivery partner • A data analytics tool to flag potential frauds or discrepancies is in place. Meetings and liaison with key individuals within partner organisations and managers of other schemes are taking place.
Change management	There is a risk that proposals for change initiated by other bodies (e.g. BEIS, Ofgem or National Grid) may not be identified or responded to at a sufficiently early stage to enable the company to address the proposals appropriately.	• Company business design authority is in place to approve, monitor and assess change • Resource is in place to monitor, review and respond to consultations • Regular change board meetings take place with the relevant bodies and delivery partners • IT change assessment board is in place • Governance is in place for project delivery and management.
Strategic delivery	There is a risk of insufficient focus on the development and implementation of the company's strategy and how it fits within the broader developments within the energy sector.	• Board strategy sessions are in place • Strategy sessions with senior management are in place • Company-wide strategy communication is in place • Strategy is aligned with the business plan • Strategy delivery is a company key performance indicator • Engagement with BEIS and government is in place, including regular scheduled meetings • Engagement with the wider sector is being expanded.

Signed on behalf of the Board

N McDermott.

Neil McDermott
Chief Executive

21 June 2017

Board of Directors

Martin Read
Chairman

Jim Keohane
Senior Independent Director

Neil McDermott
Chief Executive

Catherine Gan
Chief Finance Officer

Anne Baldock
non-executive director

Tony Bickerstaff
non-executive director

Simon Elliston
shareholder
nominated director

Simon Orebi Gann
non-executive director

Marion King
non-executive director

David Long
shareholder
nominated director

Tony White
non-executive director

Directors' report

The directors present their annual report on the affairs of the company, together with the financial statements and auditors' report for the year from 1 April 2016 to 31 March 2017. The company's registered number is 8961281.

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 pages 24 and 30.

Directors and corporate governance

Full details of the directors and corporate governance matters are set out on pages 23 to 35.

Position of the company

Information relating to the strategy and to the development, performance and the future prospects of the company are set out in the Strategic Report and on pages 3 to 11.

Employees

The company does not have any employees.

Environment

Details are set out on page 12 in the Environment Report.

Payment to suppliers

The company pays its suppliers in accordance with the provisions of its contracts with suppliers, subject to compliance by the suppliers with their obligations.

Charitable and political contributions

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

Results and dividends

The company has prepared its 2016/17 financial statements in accordance with International Financial Reporting Standards ("IFRS"). The audited financial statements for the year ended 31 March 2017 are set out on pages 40 to 54.

The company is a not-for-profit company. The settlement role it performs ensures that the capacity payments it is required to make to capacity providers holding capacity agreements are matched with the levies it collects from suppliers. The company's costs are funded by the settlement costs levy referred to on page 16. The amount of any excess settlement costs levy collected above 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 i.e. nil profit-nil loss. Consequently, the company does 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 the financial statements on pages 45 to 54 and the Strategic Report on page 16.

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 the company has 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 in accordance with IFRS as adopted by the European Union and in accordance 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 then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs have been followed, subject to any material departures disclosed and explained in the financial statements; and
- 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 the financial position of the company 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 for the prevention and detection of fraud and other irregularities.

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

- the financial statements, which have been prepared in accordance with IFRS as adopted by the EU, 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 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 that it faces.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's 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.

Auditors

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 its 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 he/she is obliged to take as a director in order to make himself/herself aware of any relevant audit information and to establish that the auditor is aware of that information.

The company's auditors have expressed a willingness to continue in office. A resolution to reappoint them will be proposed at the relevant time.

By order of the board

Claire Williams
Company Secretary

21 June 2017

Corporate Governance report

The 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 the sole shareholder of the company.

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

The company accordingly, both as a private company and as an entity having responsibilities for the administration of public monies, adopts the highest standards of governance and works to the highest standards of probity. The company recognises the importance of operating with regularity and propriety, the need for effectiveness and prudence in the administration of public resources and the need to secure value for public money. The company also recognises the importance of embedding the seven principles of public life (selflessness, integrity, objectivity, accountability, openness, honesty and leadership) into its culture and operations.[8]

This Corporate Governance Report outlines the company's governance structure and demonstrates how its arrangements align with the guidelines and principles set out in the UK Corporate Governance Code. An explanation is given below where any aspect of the Code has not been fully applied.

The company's activities in the year are described in pages 3 to 11 and in the Strategic Report at pages 13 to 19.

Framework Document

The company's main governing documents are its Articles of Association and its Framework Document. The Framework Document, which establishes the fundamental relationship between the shareholder and the company, is published on the company's 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. The Framework Document makes it clear that the company has day to day operational independence, subject to certain limited exceptions set out in legislation, the company's Articles of Association and in the Framework Document itself. The limitations on the company's independence are those which are either:

- common to government owned entities and necessary to satisfy government and Parliamentary budgeting and accountability requirements; or
- provide the shareholder with specific controls in respect of policy implementation matters which it is the company's responsibility to execute.

The Framework Document recognises that the company is a separate corporate entity and that its governance, and decision making processes, flow through its board, with its executives reporting to that board.

The Framework Document establishes that in carrying out its functions, activities and role the company shall seek to maintain market participants' confidence in the Capacity Market process and minimise costs to consumers. This is known as the "Guiding Principle". The company recognises the importance of this Guiding Principle.

UK Corporate Governance Code

The company is 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 specify and explain any non-compliance in its annual report. The board considers that the company has complied in full with the Code, otherwise than as explained in this Corporate Governance Report. Any non-compliance is due to the requirements of the company's shareholder as reflected in company's Articles of Association and the Framework Document.

[8] 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--

The company additionally believes that the adoption of the UK Corporate Governance Code is important as a means of recognising and embedding best practice in corporate governance.

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, probity and focus on the sustainable success of the company over the longer term.

The board is collectively responsible for the long term success of the company and is ultimately responsible for its strategy, management, direction and performance. The board sets the company's strategic aims, ensures that the necessary financial and human resources are in place for the company to meet its objectives, reviews progress towards the achievement of objectives and reviews the performance of management.

The board establishes the values, culture, ethics and standards of the company and sets the framework for prudent and effective controls, which enables 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 (i) the audit, risk and assurance committee and (ii) the nomination committee. The written terms of reference of both committees are available on the company's 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 provide that the shareholder's approval is required for all board appointments. The Framework Document and the Articles of Association also state that the shareholder has the right to appoint the Chairman, the Senior Independent Director and two shareholder nominated directors.

Martin Read was appointed as Chairman designate in early 2014 and as Chairman on 22 July 2014. Jim Keohane was appointed in early 2014 as Senior Independent Director designate and, on 22 July 2014, as Senior Independent Director. Both Martin Read and Jim Keohane were re-appointed to these roles in March 2017. The two shareholder nominated directors are currently David Long (appointed on 27 October 2015) and Simon Elliston (appointed on 16 December 2015).

After obtaining the consent of the shareholder in accordance with the Framework Document and the Articles of Association, the board, on 11 November 2014, appointed an additional five independent non-executive directors (Anne Baldock, Tony Bickerstaff, Marion King, Simon Orebi Gann and Tony White).

Neil McDermott, the Chief Executive, was appointed as a director on 22 July 2014 and Catherine Gan, the Chief Finance Officer, was appointed as director effective on 24 April 2017 (replacing Helen Turner, the previous Chief Finance Officer, who resigned her roles as both CFO and director on 7 December 2016).

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 two shareholder nominated directors, have written terms of appointment. These terms of appointment are available for inspection at the company's registered office during normal business hours. The shareholder nominated directors are, respectively, a civil servant employed by central government and a public servant employed by a government wholly owned company.

The Chairman was independent on appointment. The board considers all non-executive directors to be independent of the company, with the exception of David Long and Simon Elliston who were appointed by the shareholder as its nominated directors.

The independent non-executive directors are appointed for a term of three years as set out in the Framework Document, subject to statutory and appropriate other provisions relating to the cessation of their appointment. The shareholder nominated directors are appointed for the period required by the shareholder.

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.

New directors receive an induction programme that is tailored to their individual needs.

The company maintains a register of directors' interests.

Board changes

Helen Turner, the Chief Finance Officer, stepped down from the board and her role as Chief Finance Officer on 7 December 2016. She was replaced in both roles in April 2017 by Catherine Gan.

Board governance

The board meets sufficiently regularly to discharge its duties effectively, generally meeting eight times per year (with additional ad hoc meetings as required). The board met nine times in 2016/17 and also held a separate strategy meeting.

The Chairman has held a meeting with the non-executive directors without the executives being present. The non-executive directors, led by the Senior Independent Director, have met without the Chairman and executive directors being present.

Details of the directors' interests are recorded in the register maintained by the company and reviewed at least annually by the board. The company has 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.

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 Chairman, executive directors 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 also to independent legal advice if appropriately required.

There is a formal schedule of matters specifically reserved to 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 to the board including:

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

The main roles and responsibilities of the Chairman, Chief Executive, Senior Independent Director and non-executive directors are summarised in high level terms below. There is a document which sets out the division of responsibilities between the Chairman and the Chief Executive, which has been approved by the board.

The Chairman:

- 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 the shareholder
- manages the business of the board, including the board's agenda and ensuring that adequate time is available for the discussion of all agenda items, in particular, strategic issues
- is responsible for ensuring that the directors receive accurate, timely and clear information.

The Chief Executive:

- fulfils his responsibilities as Accounting Officer[9]
- leads the executive team in the day to day running of the 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 Chairman and the board
- facilitates effective communication to the shareholder and external stakeholders, including service providers, industry parties, regulatory bodies and governmental authorities
- ensures the values of the company are embedded within its operations and staff culture.

The Senior Independent Director:

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

Non-executive directors:

- Non-executive directors (including via their activities in relevant committees) ensure that the board fulfils its responsibilities, including in relation to strategy, monitoring the performance of management and satisfying themselves as to the integrity of financial information and that there is in place robust internal controls and a sound system of risk management.

Board evaluation

The board has undertaken a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors. The committees also each separately undertake an annual evaluation process. The Chairman has, with the input and assistance from the other directors and the executive management, undertaken an objective and thorough evaluation of the performance of the Senior Independent Director. The non-executive directors, led by the Senior Independent Director, have undertaken an objective and thorough performance evaluation of the Chairman, taking into account the views of executive directors.

These evaluations have concluded that the board and the committees are working effectively, they are performing their role in a proper, good and appropriate manner and there is strong corporate governance in place.

The Chairman also regularly reviews and agrees with each director their training and development needs, including as part of the evaluation process.

[9] 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.

Tony Bickerstaff

chair of audit, risk and assurance committee

Audit, Risk & Assurance Committee

This committee was established by the board on 16 December 2014.

During the year and at the year end the membership of this committee comprised five non-executive directors, namely Tony Bickerstaff (chairman), Jim Keohane, Marion King, Simon Elliston and Simon Orebi Gann.

The chairman of the committee is a qualified accountant with recent and relevant financial experience. The committee is composed of four 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 2016/17, with meetings in May 2016, September 2016 and in January 2017. The company's external auditor attends committee meetings.

The Chief Executive (as Accounting Officer), Chief Finance Officer (or Acting Chief Finance Officer), Head of Internal Audit, Company Secretary and external auditors are invited to attend each meeting. The Accounting Officer, Chief Finance Officer (or Acting Chief Finance Officer), Head of Internal Audit and the external auditors have access to the chairman of the committee outside formal committee meetings. The Head of Internal Audit and the external auditors each separately meet informally with the committee after every scheduled committee meeting.

The main responsibilities of the committee 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, re-appointment and removal of the external auditor and approving the remuneration and terms of engagement of the external auditor
- reviewing external auditor independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements
- reporting to the board, identifying any matters in respect of which it considers that action or improvement is needed 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 employees are able, in confidence, to raise concerns about possible improprieties in matters of financial reporting or other matters.

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

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

- Review of Financial Performance
- Risk Register Review
- Deep Dive on Contract Lifecycle Management Risk
- Internal Audit Activity Update
- Status of Significant Accounting Estimates, Judgements and Special Issues
- Annual Report Update: Going Concern & Viability Statement
- External Auditors Report for 2015/16
- Letters of Representation for 2015/16

- Recommendation of Annual Report and Accounts for 2015/16
- Committee Annual Report to the Board
- Review of Procedures for Handling Reporting Errors or Irregularities
- Lessons Learnt on 2015/16 External Audit
- Re-Appointment of External Auditors for 2016/17
- Approval of External Audit Fee for 2016/17
- Annual Evaluation of Committee
- Risk Deep Dive on Organisation Coordination
- Risk Management and Internal Control Framework
- Annual Report Process for 2016/17
- External Audit Plan and Update on Period 9 Work 2016/17
- External Audit Letter of Engagement
- Assessment of Committee Training Requirements
- Internal Audit Plan, Objectives and Updates on Internal Audit Activity
- Business Continuity Planning for IT Infrastructure Support Provider Failure
- Deep Dive on Fraud Risk.

The minutes of the meeting are circulated to the board.

The significant issues considered by the committee in relation to the financial statements relates to the accounting treatment for the settlement monies paid by EMRS's former subcontractor in relation to the original settlement system. This matter is further referred to on page 17 of the Strategic Report and note 6 of the financial statements.

The company's main risks and related mitigating actions are set out on pages 17 to 19 of the Strategic Report. There have been no lapses in data security (other than possibly trivial lapses).

The re-appointment of the external auditor was approved by the board in November 2016 upon the recommendation of the committee. The committee in recommending the re-appointment, and the board in approving the re-appointment, took into account the fact that the Framework Document stated the strong presumption that the company would appoint the National Audit Office (NAO) as its auditor and also that shareholder consent was required for the appointment of any external auditor. They also noted the significant benefits of appointing the NAO based on value for money, the potential synergies with BEIS's audit requirements and the NAO's understanding of both the complex environment within which the company would operate 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.

Martin Read

chair of nomination committee

Nomination Committee

During the year and at the year end the committee comprised Martin Read (chairman), Anne Baldock, Marion King, Simon Orebi Gann and Tony White. A majority of members of the nomination committee are independent non-executive directors.

The committee met twice during the year, in May 2016 and September 2016, in order to discuss the re-appointment of the Chairman and Senior Independent Director. The committee was chaired by Mr Orebi Gann in place of the committee chair (Dr Martin Read) who was not present as the question of his re-appointment as board chair was being discussed. During the course of the meetings the committee also discussed the composition of the board and matters relating to the timing for directors to be appointed or re-appointed. The committee recommended the re-appointment of the Chairman and the Senior Independent Director to the shareholder.

Under the Articles of Association and the Framework Agreement, the shareholder has reserved the right to appoint the board chair, the Senior Independent Director and up to two shareholder nominated directors. The shareholder has also reserved the right to approve the appointment of the other directors of the company.

The committee did not lead the process for board appointments as it was not established until December 2014, shortly after the appointment of the majority of board members (which took place in November 2014).

The shareholder in early 2014 appointed the Chairman and Senior Independent Director for a three year term (effective, in each case, from 1 March 2014), and has re-appointed the Chairman for a further three year term (effective from 1 March 2017) and the Senior Independent Director for a further two year term (effective from 1 March 2017). The nomination committee recommended the re-appointment of both the Chairman and Senior Independent Director to the shareholder.

The Chairman and the Senior Independent Director led the process in 2014 for the Chief Executive and the independent non-executive directors and recommended the proposed appointments to the shareholder. The shareholder consented to these appointments. The shareholder appointed the two original shareholder nominated directors in early 2014 and appointed replacement shareholder nominated directors in late 2015.

An external recruitment consultancy, Odgers Berndtson, was used in the appointment of the Chairman, the Senior Independent Director, Chief Executive and the independent non-executive directors. The shareholder nominated directors are civil servants selected by the shareholder. Odgers Berndston was also used in the recruitment of some members of the senior management team. Odgers Berndtson does not have any other connection with the company.

An external recruitment consultancy, Sartori Executive Search, was used in the search for the replacement Chief Finance Officer. Catherine Gan was appointed as Chief Finance Officer effective on 24 April 2017 and as a director on the same date. Sartori Executive Search does not have any other connections with the company.

The search process for the appointment of the Chairman, Senior Independent Director, Chief Executive, Chief Finance Officer and other directors 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 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 to 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.

The minutes of meetings are circulated to the board.

Remuneration Committee

The membership and responsibilities of this committee are described in the Remuneration Report on pages 34 to 35.

Board and committee membership

The table below sets out the dates of appointment of the members to the board and the committees and details of those board members who resigned in year.

Director	Role	Board	Audit, Risk & Assurance Committee	Nomination Committee
Anne Baldock	non-executive director	App. 11/11/2014		App. 16/12/2014
Tony Bickerstaff	non-executive director	App. 11/11/2014	App. 16/12/2014	
Simon Elliston	non-executive director	App. 16/12/2015	App. 16/12/2015	
Catherine Gan	Chief Finance Officer	App.24/04/2017		
Jim Keohane	non-executive director	App. 22/07/2014	App. 16/12/2014	
Marion King	non-executive director	App. 11/11/2014	App. 16/12/2014	App. 16/12/2014
David Long	non-executive director	App. 27/10/2015		
Neil McDermott	Chief Executive	App. 22/07/2014		
Simon Orebi Gann	non-executive director	App. 11/11/2014	App. 16/12/2014	App. 16/12/2014
Martin Read	Chairman	App. 22/07/2014		App. 16/12/2014
Helen Turner	Chief Finance Officer	App. 22/07/2014 Res. 07/12/2016		
Tony White	non-executive director	App. 11/11/2014		App. 16/12/2014

Board and committee meetings

The table below shows the number of board and committee meetings of the company held during the year ended 31 March 2017, and the attendance of the individual directors. All directors are expected to attend all board meetings and all members of committees are expected to attend all committee meetings.

It should be emphasised that the table does not fully reflect the contribution made to the company's business by many of the directors who have also attended other meetings (including with senior managers and/or for briefings on various matters), addressing matters raised ex-committee and attending events relating to the company's business and activities during the year.

Member attendance record

	Board	Audit, Risk & Assurance Committee	Nomination Committee
Number of meetings	**9**	**3**	**3**
Anne Baldock	9		3
Tony Bickerstaff	8	3	
Simon Elliston	9	3	
Catherine Gan*	N/A		
Jim Keohane	8	2	
Marion King	8	3	2
David Long	7		
Neil McDermott	9	X (attends but not a member)	
Simon Orebi Gann	8	2	2
Martin Read	9		2†
Helen Turner**	5	X (attends but not a member)	
Tony White	9		3

*Appointed after year end
**Resigned part way through the year
†interested in subject matter of the meeting (which related to his re-appointment) and therefore did not attend that meeting

Relations with shareholder and other stakeholders

The company in accordance with its Framework Document maintains an appropriately regular dialogue with its shareholder. The shareholder has appointed two shareholder nominated directors.

The company has also engaged in regular communication with industry and other stakeholders, including by stakeholder engagement events and via its website.

As a non-traded entity the company does not propose to have an annual general meeting.

Maintenance of a sound system of internal control

The board has overall responsibility for the company's risk management and system of internal controls and for reviewing their effectiveness. While retaining overall responsibility, the board has delegated responsibility for more regular and granular review the effectiveness of the company's risk management framework to the audit, assurance and risk committee.

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 over the page:

Control and assurance environment

- The board is responsible for the company's system of internal control and for reviewing its effectiveness. The company's system of internal control is designed to manage and where possible to 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 assists the board in discharging 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 assistance 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.
- There is an appropriate quality assurance framework in place and applied to all business critical models.

Risk management framework

- The identification, mitigation and continual monitoring of significant business risks is the responsibility of senior management. Each functional department of the company maintains a risk register identifying the business risks and allocating responsibility for appropriate monitoring and the implementation of mitigating controls. Departmental risk registers and the company's strategic risk register are 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 receiving particular attention. A risk workshop attended by senior employees was held during the year. Risk management processes are incorporated into the company's management and governance systems at all levels and form a part of the company's day to day operations.
- The audit, risk and assurance committee formally reviews the risk position at each scheduled meeting (in 2016/17, in May and September 2016 and in January 2017) and is updated on any significant risk matter which falls outside its formal review cycle. The committee also undertakes a "deep dive" into a selected risk. The committee considers the risk appetite of the company in relation to the principal risks.
- The board reviews the strategic risk register twice per year (in 2016/17, in June and December 2016). The reports to the audit, risk and assurance committee and the board include a report from management on the status of the risk management and internal control, any significant failings or weaknesses identified during the period and actions taken to remedy any significant weaknesses.
- The board has reviewed, 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 its business model, future performance, solvency or liquidity. Reference is made to the more detailed risk report on pages 17 to 19.

Internal audit

- The company has an internal audit function that provides the audit, risk and assurance committee with independent, objective assurance regarding internal controls and the risk management process as part of the company's 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.

Financial management and reporting

- There is a comprehensive strategic planning, budgeting and forecasting process within the company, with the business plan (including the annual budget) being approved by the board.
- The company's 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 that a robust and prudent annual budget is prepared which also ensures cost control and value for money for consumers. The draft budget is reviewed by the board, subsequent to which it is submitted to the shareholder for further review. The shareholder then undertakes a public consultation on the proposed budget. Subsequently the settlement costs levy, which funds the company's budget, is laid before Parliament in the form of regulations.

- The company operates robust financial management processes to ensure that it manages within its operational budget so as not to exceed the settlement costs levy.
- An update on the company's progress, forecasts and results is reported in the management information report submitted to each board meeting.
- Senior management meet regularly with the Chief Executive and Chief Finance Officer to discuss business progress and review management accounts.
- 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.
- The company is required to comply with the requirements set out in the Framework Document and the Finance and Reporting Letter, including the requirement to comply with the relevant requirements in HM Treasury guidance entitled "Managing Public Money".

Operational

- The senior management team meets on a weekly basis to review the operations of the company, its 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 the 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.
- The company reports on its significant matters relating to its operational activities at each board meeting.
- The board decides on matters falling within the schedule of reserved matters (e.g. financial commitments over the specified threshold) or otherwise raised to it for decision.

Procurement

- The company has in place an effective procurement policy and is required to procure all goods and services in compliance with the relevant requirements in Managing Public Money, certain Cabinet Office controls and the public procurement regulations.
- The company is 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 (e.g. relating to anti-bribery, whistle-blowing, anti-money laundering, health & safety and other legislative and good practice requirements). External obligations are driven primarily by key legal, statutory and regulatory requirements.
- The company expects the highest standards from all employees and delivery partners.

Treasury management

- The 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.

Signed

N McDermott.

Neil McDermott
Chief Executive and Accounting Officer
21 June 2017

Remuneration report

Employees

The company (registered no. 8961281) does not have any employees. The company performs its functions through LCCC.

Non-executive directors

Fees are payable to all non-executive directors (except the shareholder nominated directors). For reasons of synergy, operational efficiency and cost effectiveness, the board of directors of the company and LCCC are identical. The fees paid to directors therefore relate to work for both companies. All fees are paid by LCCC, with a fair and properly allocated amount relating thereto being "recharged" by LCCC to the company under the "recharge" arrangements described in note 2.6 to the financial statements.

Levels of remuneration for those non-executive directors who receive remuneration as directors reflect the time commitment and responsibilities of the role and reflect the advice on remuneration for directors provided in 2014 by Odgers Berndtson (an external recruitment consultancy). Odgers Berndtson has no other connection with the company. No director is involved in deciding his or her own individual remuneration.

In 2016 advice on the appropriate remuneration for the Chief Finance Officer post was received from Satori, an external recruitment consultancy. Sartori has no other connection with the company.

No director is involved in deciding his or her own individual remuneration.

Executive directors

The executive directors are employed and paid by LCCC. They therefore do not receive any remuneration from the company. LCCC charges the company for its services, with an amount relating to full cost of the executive directors to LCCC 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.

Director fees

The company does not directly pay fees to the directors. It has the same board members as the LCCC board. LCCC pays the fees to the directors (with the exception of the shareholder nominated directors, who do not receive remuneration from the company or LCCC), with the allocated portion relating to the company being recouped via the "recharge" arrangements described in note 2.6 to the financial statements. Essentially, 20% of the total fees paid in 2016/17 in relation to each director is allocated to the company. This allocation is illustrated in the table on page 35.

Name	2016/17 Fees £	Principal positions held elsewhere at 31 March 2017
Anne Baldock	20% of £25,000 2015/16: 20% of 25,000	• LCCC – non-executive director • Hydrogen Group Plc – non-executive director • Thames Tideway Limited – non-executive director • 375 Greyhound Residents Ltd – director/shareholder
Tony Bickerstaff	20% of £31,000 2015/16: 20% of £31,000	• Costain Group Plc – Group Finance Director • CBI Economic Growth Board – member • LCCC – non-executive director
Catherine Gan	0 (employed after year end)	• LCCC – Chief Finance Officer and director
Simon Elliston	0 (shareholder nominated director – civil servant)	• BEIS – Director of Finance and Commercial • LCCC – non-executive director
Jim Keohane	20% of £40,000 2015/16: 20% of £40,000	• Gas & Electricity Marketing Authority – non-executive member • Harwich Haven Authority – chairman • LCCC – non-executive director
Marion King	20% of £25,000 2015/16: 20% of £25,000	• Royal Bank of Scotland – Group Director of Payments • LCCC – non-executive director • Payments UK – director
David Long	0 (shareholder nominated director – public servant	• UK Government Investments – Executive Director • LCCC – non-executive director
Neil McDermott	N/A – see above	• LCCC – Chief Executive and director
Simon Orebi Gann	20% of £25,000 2015/16: 20% of £25,000	• LCCC – non executive director • Aspen Technology Inc (NASDAQ: AZPN) – USA – non-executive director
Martin Read	20% of £120,000 2015/16: 20% of £120,000	• Laird plc – chairman • Remuneration Consultants Group – chairman • LCCC – chairman • UK Government Senior Salaries Review Body – chairman • Lloyds of London (Franchise Board) – non-executive director
Helen Turner	N/A – see above	• LCCC – Chief Finance Officer and director
Tony White	20% of £25,000 2015/16: 20% of £25,000	• LCCC non-executive director • Association for Decentralised Energy – Vice President • Green Energy Options – non-executive director • The Ecofin Research Foundation – trustee director • BW Energy Ltd – director • First Utility Trust – trustee

The above fees (paid by LCCC with a proportion recharged to the company) are the only form of remuneration that each relevant non-executive director receives.

Independent Auditor's Report to the sole shareholder of the Electricity Settlements Company Ltd

Opinion on financial statements

In my opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2017 and of the profit for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union; and
- have been prepared in accordance with the Companies Act 2006.

Opinion on regularity

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

Basis of opinions

I have audited the financial statements of the Electricity Settlements Company Ltd ("the company") for the year ended 31 March 2017 which comprise:

- the Statement of Comprehensive Income;
- the Statement of Financial Position;
- the Statement of Cash Flows;
- the Statement of Changes in Equity; and
- the related notes.

The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006. I have also audited the information in the Directors' Remuneration Report that is described as having been audited.

The regularity framework that has been applied is the Companies Act 2006; the articles of association of the company; the Framework Document between the Secretary of State and the company; and HM Treasury authorities and other relevant legislation to the extent they are applicable to the company.

Overview of my audit approach

Key audit matters

Key audit matters are those matters that, in the auditor's professional judgement, were of most significance in the audit of the financial statements for the year ended 31 March 2017 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 the auditor's opinion thereon, the auditor does not provide a separate opinion on these matters.

This is not a complete list of all risks identified by my audit but only those areas that had the greatest effect on my overall audit strategy, allocation of resources and direction of effort. I have not, for example, included information relating to the work I have performed around the presumed risk of management override of controls under International Standard on Auditing (UK & Ireland) 240, the Auditor's Responsibility Relating to Fraud in Financial Statements, an area where my work has not identified any matters to report.

The areas of focus were discussed with the Audit, Risk and Assurance Committee; their report on matters that they considered to be significant to the financial statements is set out on pages 28.

Risk	My response and findings
Litigation and compliance As part of initial risk assessment for the 2016-17 audit of the ESC, I identified the risk associated with litigation and compliance to be one of the most significant assessed risks of material misstatement. The first operational year of the Capacity Market commenced in October 2016, with the first payments being made in December 2016. As this is the first year, there was a heightened possibility of litigation arising due to circumstances unforeseen before the scheme became operational, and due to the value of the payments being made by the company. I also assessed a risk associated with the appropriate accounting treatment and recognition of the award to the company after the conclusion of arbitration relating to the dispute with Sopra Steria relating to the Settlement System intangible asset. Further information relating to litigation claims are discussed in the disclosures made in note 6 to the financial statements.	I assessed the controls and monitoring procedures in place at the company for tracking and monitoring contract management issues. As part of my risk assessment, I also reviewed how the company operated as the Settlement Agent in the Capacity Market. I also reviewed the proposed accounting treatment for the Sopra Steria award to ensure that it was compliant with both the financial reporting framework and the company's framework of authorities. Following this work, I am satisfied that this litigation risk did not crystallise, and that the Sopra Steria award was treated appropriately in the company's accounts.

Application of materiality

I applied the concept of materiality both in 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 at £257,000, which is approximately 2% of gross expenditure. I chose this benchmark as I consider it to be of principal interest to users of the financial statements.

As well as quantitative materiality, there are certain matters that, by their very nature, would if not corrected influence the decisions of users, for example, any errors reported in Directors' Remuneration. Assessment of such matters would need 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 in support of my opinion on regularity, and evaluating the impact of any irregular transactions, I took into account both quantitative and qualitative aspects that I consider would reasonably influence the decisions of users of the financial statements.

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 £5,000 as well as differences below this threshold that, in my view, warranted reporting on qualitative grounds.

There were no unadjusted errors to report to the Audit, Risk and Assurance Committee.

Scope of my audit

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the financial statements.

In addition I read all the information and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

I am also 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.

Other matters which I report under the Companies Act

Directors' remuneration

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

I also report to you if, in my opinion, certain disclosures of directors' remuneration required have not been made. I have nothing to report arising from this duty.

The strategic and directors' reports

In my opinion, based on the work undertaken in the course of the audit, the information given in the strategic and directors' reports for the financial year are consistent with the financial statements and have been prepared in accordance with applicable law.

Based on my knowledge and understanding of the company and its environment obtained during the course of the audit, I have identified no material misstatements in these reports

The corporate governance report

In my opinion, based on the work undertaken in the course of the audit, the information given in the corporate governance statement in respect of internal control and risk management systems in relation to financial reporting processes, and about share capital structures, is consistent with the accounts and has been prepared in accordance with applicable law.

Based on my knowledge and understanding of the company and its environment obtained during the course of the audit, I have identified no material misstatements in this information.

Matters on which I report by exception

Adequacy of accounting records information and explanations received

I report to you if, in my opinion:

- adequate accounting records have not been kept;
- the financial statements and the part of the Remuneration report to be audited are not in agreement with the accounting records and returns; or
- I have not received all of the information and explanations I require for my audit.

I have nothing to report arising from this duty.

Consistency of information in the Annual Report

Under International Standards on Auditing (UK & Ireland), I am required to report to you if, in my opinion, information in the Annual Report is:

- materially inconsistent with the information in the audited financial statements; or
- apparently materially incorrect based on, or materially inconsistent with, the knowledge of the company that I acquired in the course of performing my audit; or
- otherwise misleading.

In particular, I am required to consider:

- whether I have identified any inconsistencies between the knowledge that I acquired during the audit and the directors' statement that they consider the Annual Report is fair, balanced and understandable; and
- whether the Annual Report appropriately discloses those matters that I communicated to the Audit, Risk and Assurance Committee which I consider should have been disclosed.

I have nothing to report arising from this duty.

The directors' assessment of principal risks and future prospects

Under International Standards on Auditing (UK & Ireland), I am required to report to you if I have anything material to add, or to draw attention to, in relation to the directors' disclosures in the Annual Report and financial statements:

- confirming that they have carried out a robust assessment of principal risks facing the company, including those that would threaten its business model, future performance, solvency or liquidity;
- describing those risks and explaining how they are being managed or mitigated;
- on whether they considered it appropriate to adopt the going concern basis, and their identification of any material uncertainties to the entity's ability to continue over a period of at least twelve months from the date of approval of the financial statements; and
- explaining how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

I have nothing material to add, or to draw attention to, on these matters.

Respective responsibilities of the directors and the auditor

As explained more fully in the Statement of Directors' Responsibilities, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and with International Standards on Auditing (UK & Ireland). Those standards require me and my staff to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Matthew Kay
Senior Statutory Auditor

For and on behalf of the Comptroller and Auditor General (Statutory Auditor)

National Audit Office
157–197 Buckingham Palace Road
London, SW1W 9SP

21 June 2017

Financial statement and notes to the accounts

Contents

Statement of comprehensive income for the year ended 31 March

	Note	2017 £'000	2016 £'000
Other income	6	12,875	3,601
Other operating costs	7	(12,875)	(3,601)
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 46 to 54 form part of these accounts.

Statement of financial position as at 31 March

	Note	2017 £'000	2016 £'000
Non-current assets			
Intangible assets	8	2,290	1,546
Current assets			
Levy receivable from electricity suppliers	9	24	3
Prepayments and other receivables	10	801	198
Cash and cash equivalents	11	34,295	6,088
Total current assets		**35,120**	**6,289**
Total assets		**37,410**	**7,835**
Current liabilities			
Levy and capacity payments payable	12	(7,160)	(1,345)
Trade and other payables	13	(27,919)	(4,942)
Borrowings	14	(3)	(4)
Finance lease obligations	15	(507)	(128)
Total current liabilities		**(35,589)**	**(6,419)**
Non-current liabilities			
Finance lease obligations	15	(1,814)	(1,405)
Borrowings	14	(7)	(11)
Total non-current liabilities		**(1,821)**	**(1,416)**
Total liabilities		**(37,410)**	**(7,835)**
Net assets		**–**	**–**
Shareholders' equity and other reserves			
Share capital	16	–	–
Retained earnings		–	–
Total equity		**–**	**–**

The notes on pages 46 to 54 form part of these accounts.
The financial statements were approved by the board of directors on 7 June 2017 and signed on its behalf by:

Neil McDermott
Chief Executive Officer

N McDermott.

Catherine Gan
Chief Finance Officer

Catherine Gan

Statement of changes in equity for the year ended 31 March

	Share capital £'000	Retained earnings £'000	Total equity £'000
As at 1 April 2015	**–**	**–**	**–**
Share capital issued	–	–	–
Total comprehensive income for the year	–	–	–
As at 31 March 2016	**–**	**–**	**–**
Share capital issued	–	–	–
Total comprehensive income for the year	–	–	–
As at 31 March 2017	**–**	**–**	**–**

As at 31 March 2017 the company has one authorised ordinary share issued and fully paid.
The notes on pages 46 to 54 form part of these accounts.

Statement of cash flows for the year ended 31 March

	Note	2017 £'000	2016 £'000
Cash flows from operating activities			
Profit for the year		–	–
Adjustment to reconcile profit before tax to net cash flows:			
Amortisation of intangible assets	8	261	2
Working capital adjustments:			
(Increase)/decrease in receivable from electricity suppliers	9	(21)	1,371
Increase in prepayments and other receivables	10	(603)	(186)
Increase in levy and capacity payments payable	12	5,815	643
Increase in trade and other payables	13	22,977	1,443
Net cash inflow from operating activities		**28,429**	**3,273**
Cash flows from investing activities			
Purchase of intangible assets	8	–	(15)
Net cash outflow from investing activities		**–**	**(15)**
Cash flows from financing activities			
Decrease in borrowings	14	(5)	(640)
Repayment of finance lease obligations	15	(217)	–
Net cash outflow from financing activities		**(222)**	**(640)**
Net increase in cash and cash equivalents in the year		**28,207**	**2,618**
Cash and cash equivalents at the beginning of the year		6,088	3,470
Cash and cash equivalents at the end of the year	**11**	**34,295**	**6,088**

The notes on pages 46 to 54 form part of these accounts.

Notes to the financial statements for the year ended 31 March 2017

1. Authorisation of financial statements

The financial statements of Electricity Settlements Company Ltd (the "company") for the year ended 31 March 2017 were approved and authorised for issue in accordance with a resolution of the directors on 7 June 2017.

The company is a company limited by shares, incorporated and domiciled in the UK. The company's registered office is at Fleetbank House, 2-6 Salisbury Square, EC4Y 8JX. 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.

In last year's financial statements the company was stated as being owned by the Secretary of the State for the Department of Energy & Climate Change. In July 2016 the Department of Energy & Climate Change became part of the new Department for Business, Energy & Industrial Strategy.

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 Financial Reporting Standards (IFRS) as adopted by the European Union and applied in accordance with the provisions of the Companies Act 2006 applicable to companies reporting under IFRS.

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":

i. The Electricity Capacity Regulations 2014 as amended; and

ii. 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:

i. applies prudent financial management in order to ensure that its commitments are accommodated within the timing of its collection of its settlement costs levy;

ii. undertakes a robust and detailed annual business planning and budgeting process to establish its operational costs requirements for each financial year;

iii. has considered the potential impact of credit risk and liquidity risk detailed in note 3; and

iv. is exposed to minimal cash flow risk through Capacity Market transactions as a result of the statutory 'pay when paid' mechanism explained in note 2.4.

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 annually by new regulations. The directors note the low risk that regulations resetting the annual rate may not be made (resulting in the settlement costs levy set in relation to the previous year continuing to apply) or may not be made until after the commencement of the relevant financial year (resulting in the company experiencing a timing mismatch on its funding requirement). The directors are of the view that there is no reason to believe that future re-setting regulations will not be forthcoming.

The directors also 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 BEIS 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 applies to the setting of the annual settlement costs levy. The company can also request a working capital loan from BEIS 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).

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 is re-set annually. 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 under 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.

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

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 under 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 that 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.

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 Business, Energy and Industrial Strategy which is responsible for acting as the CFD counterparty for 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.

The interest free capital loan received by the company from BEIS for capital expenditure is recognised under borrowings and is repayable over the useful life of the assets funded through this loan. The benefit of a below-market rate of interest on the capital loan for capital expenditure, if material, is recognised in the statement of comprehensive income over the period of the loan.

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.

The only financial assets held by the company at the reporting date are other receivables and cash and cash equivalents.

2.9 Financial liabilities

The company classifies financial liabilities as 'other financial liabilities'. Other financial liabilities include trade and other payables, borrowings and finance lease obligations.

The categorisation depends on the purpose for which the financial liability is held or acquired. Management determines the categorisation of financial liabilities at initial recognition and re-evaluates this designation at each reporting date.

2.9.1 Recognition and measurement

Other financial liabilities are initially measured at fair value, net of transaction costs. Other financial liabilities are subsequently measured at amortised cost using the effective interest rate method, with interest expense recognised on an effective yield basis.

2.9.2 Derecognition of financial liabilities

Financial liabilities are derecognised when, and only when, the obligations are discharged, cancelled or they expire.

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, assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are 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 period:

	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 Impairment of non-financial assets

Intangible assets are only subject to amortisation to the extent that they are available for use. Intangible 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.

2.12 Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at the inception of the lease. The arrangement is, or contains, a lease if fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset or assets, even if that right is not explicitly specified in an arrangement.

A lease is classified at the inception date as a finance lease or an operating lease. Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

2.12.1 Finance leases

Company as a lessee

The lease of the settlement system where the company has substantially all the risks and rewards of ownership is classified as a finance lease. Finance leases are capitalised at commencement of the lease at the lower of the fair value of the leased asset and the present value of the minimum lease payments. The present value of the minimum lease payments of the settlement system approximates to its fair value.

The settlement system acquired under a finance lease is amortised over the shorter of the useful life of the asset and the lease term.

2.13 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.

2.14 Borrowings

Borrowings represent a grant in aid capital loan from BEIS. Borrowings are recognised initially at fair value, net of transaction costs incurred (if any). Borrowings are subsequently carried at amortised cost; any difference between the proceeds (net of transactions costs, if any) and the redemption value is recognised in the statement of comprehensive income over the period of the borrowings using the effective interest method.

2.15 Bid bond collateral

In order to enter the Capacity Market Auction, applicants must lodge bid bond collateral with the company where, on Prequalification Results Day, those applicants receive a notice from the Delivery Body 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.

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 BEIS 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. Critical 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 key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below. 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.

4.2.2 Valuation of intangible assets

See financial overview on page 17.

5. New standards, amendments and interpretations not yet adopted

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the company's financial statements are disclosed below. The company intends to adopt these standards, if applicable, when they become effective. The company has not sought early adoption of any standards or amendments. None of these standards are expected to have a significant effect on the financial statements of the company:

IFRS 9: Financial instruments
IFRS 9, 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of IFRS 9 was issued in July 2014. It replaces the guidance in IAS 39 that relates to the classification and measurement of financial instruments. The standard is effective for accounting periods beginning on or after 1 January 2018.

IFRS 15: Revenue from Contracts with Customers
IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15 revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer.

The principles in IFRS 15 provide a more structured approach to measuring and recognising revenue. The new revenue standard is applicable to all entities and will supersede all current revenue recognition requirements under IFRS. Either a full or modified retrospective application is required for annual periods beginning on or after 1 January 2018 with early adoption permitted.

IFRS 16: Leases
IFRS 16 was issued in January 2016 and establishes principles for the recognition, measurement, presentation and disclosure of leases.

The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. The standard is effective for accounting periods beginning on or after 1 January 2019.

Amendments to IAS 7 Disclosure Initiative
The amendments require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. The amendments do not prescribe a specific format to disclose financing activities; however, an entity may fulfil the disclosure objective by providing a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities.

The amendments apply prospectively for annual periods beginning on or after 1 January 2017 with earlier application permitted. Entities are not required to present comparative information for earlier periods.

There are no other IFRS or IFRIC interpretations that are not yet effective that would be expected to have a material impact on the company.

6. Other income

	2017 £'000	2016 £'000
Settlement costs levy income	4,283	3,891
Less: amount repayable to suppliers	(1,373)	(1,181)
Net settlement costs levy income	2,910	2,710
Capacity Market supplier charge income	9,199	–
Settlement system dispute	766	–
Reversal of finance lease obligations	–	891
Other income	**12,875**	**3,601**

As a result of the delay in the build and testing of the original planned system, the contract between EMRS and its then principal subcontractor was terminated on 9 November 2015. Following an agreement between the parties involved, £0.766m was received by ESC as its share of the settlement.

The reversal of finance lease obligations, in 2015/16, relates to the impairment of the settlement system asset. During 2015/16, BEIS released the company from its obligation to repay in respect of the impaired amount. Finance lease obligations equivalent to the impairment of the settlement system asset were released to the statement of comprehensive income to match the impairment charge (see note 7 and note 8).

7. Other operating costs

	2017 £'000	2016 £'000
Capacity payments	9,199	–
Costs recharged by LCCC	1,707	1,382
Operational settlement costs	1,606	1,241
Amortisation	261	2
Insurance	65	62
Auditor's remuneration	30	18
Impairment of the settlement system asset	–	891
Miscellaneous costs	7	5
Other operating costs	**12,875**	**3,601**

8. Intangible assets

	Settlement System £'000	Other IT Software £'000	Total £'000
Cost			
As at 1 April 2015	2,207	–	2,207
Additions during the year	960	15	975
Impairment	(891)	–	(891)
Derecognition of capital accruals	(743)	–	(743)
As at 31 March 2016	**1,533**	**15**	**1,548**
Additions during the year	1,005	–	1,005
As at 31 March 2017	**2,538**	**15**	**2,553**
Amortisation			
As at 1 April 2015	–	–	–
Charge for the year	–	2	2
As at 31 March 2016	**–**	**2**	**2**
Charge for the year	258	3	261
As at 31 March 2017	**258**	**5**	**263**
Net book value as at 31 March 2016	1,533	13	1,546
Net book value as at 31 March 2017	**2,280**	**10**	**2,290**

The company leases the settlement system from BEIS under a finance lease where all the risks and rewards of ownership rest with the company. The settlement system went live in September 2017. The lease term is 5 years which is the period over which the asset will be depreciated.

The derecognition of capital accruals, in 2015/16, was associated with the impairment of the settlement system asset as a result of the termination of the original system development contract. The derecognition of capital accruals reflects the reversal of accrued capital costs which, when aggregated with the impairment charge, reduces the carrying value of the settlement system asset to its recoverable amount. During 2015/16, BEIS released the company from its obligation to repay in respect of the impaired amount. The derecognition of capital accruals and the impairment charge were matched with a reduction in the finance lease obligations (as outlined in note 15).

The settlement system was impaired equivalent to the amount by which the carrying value of the settlement system exceeds its recoverable amount (after reflecting the derecognition of capital costs). An amount equivalent to the impairment expense was recognised as income by releasing the finance lease obligations to match the impairment expense so the net impact in the statement of comprehensive income is neutral.

As the settlement system asset is matched with the associated finance lease obligations, so asset additions during the year are matched with an equivalent increase in the lease obligation and are therefore treated as non-cash transactions in the preparation of the statement of cash flows.

9. Levy receivable from electricity suppliers

	2017 £'000	2016 £'000
Settlement costs levy	3	3
Capacity Market supplier charge	21	–
	24	**3**

10. Prepayments and other receivables

	2017 £'000	2016 £'000
Amounts owed by LCCC	766	177
Prepayments	21	21
Other receivables	14	–
Total prepayments and other receivables	**801**	**198**

Prepayments comprise the insurance charge and software maintenance support relating to the next financial year, 2017/18, which has been paid in advance.

11. Cash and cash equivalents

	2017 £'000	2016 £'000
Cash at bank	6,392	1,168
Suppliers credit cover	1,046	–
Bid bond collateral	26,857	4,920
Total cash and cash equivalents	**34,295**	**6,088**

For the purpose of the statement of cash flows, cash and cash equivalents only comprise of cash at bank, suppliers credit cover and bid bond collateral as stated above. Suppliers credit cover and bid bond collateral is a restricted cash balance and relates 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

	2017 £'000	2016 £'000
Capacity payments	2,826	–
Settlement costs levy	1,573	1,345
Capacity Market supplier charge	2,761	–
Total levy and capacity payments	**7,160**	**1,345**

Capacity payments payable are the amount 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 2016/17, 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 supplier charge payable relates the difference between Capacity Market supplier charges which have been collected from electricity suppliers during 2016/17, 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.

13. Trade and other payables

	2017 £'000	2016 £'000
Bid bond collateral	26,858	4,920
Suppliers' collateral	1,046	–
Accruals and other payables	15	22
Total trade and other payables	**27,919**	**4,942**

Bid bond collateral relates to credit cover provided by the capacity providers.

14. Borrowings

	2017 £'000	2016 £'000
Current		
Grant in aid capital loan	3	4
Non-current:		
Grant in aid capital loan	7	11
Total borrowings	**10**	**15**

The grant in aid capital loan is interest free and repayable to BEIS from funding received through the settlement costs levy collected from suppliers. The timing of the repayment of the loan is in line with the depreciation charged on the assets funded via the loan.

15. Finance lease obligations

	£'000
As at 1 April 2015	2,207
Finance lease acquired during the year	960
Finance lease obligations released	(1,634)
As at 31 March 2016	**1,533**
Finance lease acquired during the year	1,005
Repayment of finance lease obligations	(217)
As at 31 March 2017	**2,321**

	2017 £'000	2016 £'000
Less than 1 year	507	128
Between 1 and 5 years	1,814	1,405
As at 31 March	**2,321**	**1,533**

The finance lease obligation is held in respect of the settlement system asset which has been funded by BEIS through EMRS, a wholly owned subsidiary of ELEXON Ltd.

The finance lease obligations released, in 2015/16, relate to the requirement to write the carrying value of the associated settlement system asset down to its recoverable amount. During 2015/16, BEIS released the company from its obligation to repay in respect of the impaired amount. Of the released amount, £0.891m relates to the impairment of the asset and £0.743m relates to the derecognition of capital accruals to ensure the asset is stated at its recoverable amount and the finance lease obligations match the recoverable asset value.

16. Share capital

	Number
Authorised shares	
Ordinary share capital £1 each	1
	£
Ordinary share capital issued and fully paid:	
As at 1 April 2015	**1**
Ordinary share capital issued £1 each	–
As at 31 March 2016	**1**
Share capital issued during the year	–
As at 31 March 2017	**1**

17. 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 to related parties £'000	Amounts owed by related parties £'000	Amounts owed to related parties £'000
Entities with significant influence:			
2016			
BEIS	960	–	1,548
LCCC	1,382	177	–
2017			
LCCC	1,707	766	–
BEIS	1,005	–	2,331

Services from LCCC comprise of 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. Services received from BEIS relate to the receipt of the settlement system in the form of a finance lease arrangement (see note 15).

18. Financial assets and liabilities

Financial assets

	Note	2017 £'000	2016 £'000
Cash and cash equivalents	11	34,295	6,088
Other receivables	10	780	177
Total financial assets		**35,075**	**6,265**

Financial liabilities

	Note	2017 £'000	2016 £'000
Trade and other payables	13	27,919	4,942
Borrowings	14	10	15
Finance lease obligations	15	2,321	1,533
Total financial liabilities		**30,250**	**6,490**
Total current		28,429	5,074
Total non-current		1,821	1,416
Total financial liabilities		**30,250**	**6,490**

Glossary

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. (for more information see: https://www.elexon.co.uk/bsc-related-documents/)
BEIS	Department for Business, Energy and Industrial Strategy.
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 bid to win a capacity agreement. A Capacity Auction typically relates to delivery of capacity four years ahead (referred to as T-4 Auctions). For instance, the capacity agreements resulting from the 2014 Capacity Auction will require capacity to be delivered in the delivery year commencing 2018/19. Those agreements awarded in 2015 will be required to deliver capacity from 2019/20. The interim periods are covered by Transitional Arrangements.
Capacity Market	The Capacity Market has been designed by BEIS to offer capacity providers who have been awarded capacity agreements with a steady, predictable revenue stream upon which they can base their future investments, with the aim of ensuring security of supply in future years at least cost to consumers.
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 Auction or from a Transitional Arrangements Auction.
Contracts for Difference or CFDs	A CFD awarded under the CFD scheme is a long term agreement between a low carbon electricity generator and LCCC. It is designed to provide the generator with a stable pre-agreed price (the "strike price") for the lifetime of the contract. This is done by paying the difference where electricity prices are less than the strike price (and receiving the difference when prices are higher than the strike price).
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.

EMRS	EMR Settlement Ltd (EMRS) is a wholly owned subsidiary of ELEXON Ltd and is the settlement services provider to ESC and LCCC. The parties have entered into a contract under which EMRS will provide settlement services (including billing, collection and settlement) and provide and manage the operation of the settlement system. (EMRS website: https://www.emrs.co.uk/)
LCCC	Low Carbon Contracts Company Ltd (LCCC) is the counterparty to CFDs and manages them over their lifetime. It is a sister company to ESC.
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. (https://www.electricitysettlementscompany.uk/)
Ofgem	Office of Gas and Electricity Markets, a non-ministerial government department and an independent national regulator.
settlement system	The settlement system used to settle all monies collected from suppliers to make payments to CFD generators and Capacity Market providers, and to settle all monies collected from CFD generators and Capacity Market providers which are payable to suppliers or (in the case of the Capacity Market) BEIS.
Transitional Arrangements	Transitional Arrangements were introduced by BEIS to support participation of potential Demand Side Response providers and generating units of less than 50MW in the Capacity Market during the interim period prior to 2018/19, which is the delivery year relating to the first Capacity Auction. In other words, the arrangements are designed to support the development of this sector in the run up to the Capacity Market being in full operation. Transitional Arrangements Auctions are held one year ahead, with capacity agreements being given to successful applicants.
Transitional Arrangements Auctions	Transitional Arrangements Auctions are one year ahead auctions under the Transitional Arrangements.

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