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Dear Mark,

The “timing-out” of Authority decisions on modification proposals

Thank you for this opportunity to provide our views regarding the “timing-out” of Authority decisions on modification proposals.

This response largely mirrors the views expressed in our response to the Elexon consultation on the same subject in September 2008. However, Drax believes the views contained within this document are relevant to the decision processes for the BSC, CUSC and the UNC.

Ofgem’s Consultation Letter

As indicated in Ofgem’s consultation letter, it is Ofgem’s belief that if a modification were to “time-out” prior to the Authority being in a position to make a decision, this would not only be a waste of resource for both the Authority and the industry, but consumers could also directly suffer if the modification was in the public interest and could not be legally implemented. However, Ofgem have failed to identify the potential risk of a decision working against the interests of consumers, and the industry alike, should the Authority unilaterally make a change to the implementation timetable without considering the validity of the analysis prior to the delayed approval.

The consultation letter stated that “Ofgem fully understands the need for efficient and timely decision making on modification proposals and that this directly impacts on industry certainty and stability as well as bringing benefits to consumers.” The letter goes on to state “In addition to our key performance indicators, we also have, as a public body, a requirement to act reasonably in everything we do, including in setting our timetables for decisions we make.”

It should be noted that our comments on this subject have not questioned the Authority’s timeliness of decisions, they have questioned the ability to simply change the implementation timetable without a process to quantify the potential consequences of such a change, including (a) ensuring the continued validity of the analysis, (b) taking into account the change to the required resource of the relevant code administrator when implementing the modification, and (c) quantifying the potential risks to both consumers and the industry as a whole when changing such dates. The later the final determination of a modification takes place, the greater the need for a validation process to ensure that the analysis contained within the final Modification Report is still appropriate.

It should also be noted that the perceived risk identified by Ofgem is based upon an issue that has only arisen on an extremely small number of occasions. In fact, Drax is unaware of any occurrences of this issue in any of the industry codes, other than with the Zonal Transmission Losses modifications under the BSC.

Ofgem must realise that the introduction of any such power to change an implementation date should not be introduced without a process to identify the potential consequences of changing such dates; the associated procedures must be present from the outset in order to avoid an increase in risk to stakeholders, including consumers.

Ofgem's Proposed Options

Drax is perplexed as to why Ofgem has not considered an option where the regulator would pass the final Modification Report back to the relevant code panel for the report to be reviewed as part of the process for determining a new implementation date.

Option A is a unilateral decision process whereby the Authority could make changes to the implementation timetable after a consultation process. Whereas Option B performs exactly the same task, but it is the relevant code panel that sets the new implementation date (with the Authority's guiding hand).

Again, neither of the options takes into account the potential of approving a modification where *the analysis is no longer valid or is detrimentally affected* by the delay in reaching a decision. This scenario may introduce an increased potential for legal challenges, also effectively causing a waste of industry resource and a potential delay in benefits to consumers. A simple validation exercise, performed by the relevant code panel, would seem an appropriate measure in any proposed option prior to changing any implementation timetable.

With regards to Option B, we are further mystified by the comment "To avoid any risk that the Panel could simply replace one decide-by timetable that is not viable with another one that is also not viable, the request could include binding directions setting out a minimum length of time for which the new decide-by date(s) must be valid." Just as the regulator is expected to act reasonably and in good faith, so are the relevant code panels. Any change in 'decide-by' and implementation dates should be completed after a robust consultation period and via an auditable decision process. It would also seem reasonable for the relevant code panel, with input from industry, consumer, network operator, code administrator and regulator representatives, to decide whether a requested revision to the implementation timetable is a valid request given the current validity of the analysis and the scope of any analytical input required before a new implementation timetable can be determined.

As the options currently stand, neither of them appear reasonable, given that the associated consequences of changing the implementation date(s), and the potential risks to stakeholders (including consumers), are not fully taken into account. We refer you to paragraph 83 of the Judge's comments in the Judicial Review Judgement, dated 25 June 2008¹, which states:

"The justification for a Proposed Modification put forward by the Panel might be dependent upon a very time sensitive analysis of costs and benefits, and the Panel timetable for implementation might accordingly be tailored to that time sensitive analysis. If for any reason there were then a long delay before the Authority could take a final decision, a question might arise whether the Authority was in substance and reality considering the same modification as had been submitted by the Panel, or was considering an altogether different modification, putatively predicated on a cost benefit analysis that the Panel did not, and could not have, evaluated. In such circumstances a power to remit the matter to the Panel for complete reconsideration, rather than a power in the Authority to change the timetable for implementation of what had in substance become by lapse of time a different modification, might better preserve the institutional balance between the Panel and the Authority and better serve the objectives of the BSC."

We consider this concern to be particularly relevant to the proposals in the consultation letter, although it is yet to be addressed by Ofgem.

¹ Paragraphs 81 to 83 of the Judgement can be found in Appendix 1.

The Elexon Consultation

As the consultation letter recognises, the industry has recently provided comment on this very subject in response to an Elexon consultation letter. We would like to take this opportunity to reiterate the thoughts contained in our response dated 30th September 2008.

Drax broadly agrees with the concerns highlighted in the Elexon consultation document² concerning the discussions that took place in 2004 with regards to “timing-out” issues and the BSC. It is our firm belief that the Authority needs to provide timely decisions, as circumstances do change and analysis does become less relevant over time. This was particularly demonstrated by the Zonal Transmission Losses modifications³, where much of the benefit was shown to occur in the early years. The economic and regulatory environments have moved on since the proposals were first tabled, which would have made the analysis less reliable had Ofgem made a decision during the summer of 2008. An open-ended ‘decide-by’ and implementation date structure could potentially leave modifications pending decision for many years, which would be hugely undesirable due to the associated increase in regulatory risk.

It is our understanding that Ofgem currently have the opportunity to attend all Modification Group meetings; therefore, Ofgem have the opportunity to ensure that any further analysis that is required to help the Authority form their final decision can be performed prior to the development of the final Modification Report. Ofgem also have the ability to provide feedback to the BSC Panel, both before and after the final consultation, allowing them to influence the debate on ‘decide-by’ and implementation dates.

The current date structure of modifications allows a degree of flexibility, but in a way that ensures decisions are made in a timely manner. Whilst hugely flexible date structures, such as ‘open ended’ dates, avoid the ‘timing-out’ of analysis performed by a given Modification Group, they also have the potential to cause greatly increased regulatory risk should the timeliness of decisions not be maintained. There may also be the potential of modifications being approved based upon outdated analysis, as the date structure itself would not call upon the expertise of the relevant code panel to advise on the validity of the report’s content at the time of the decision.

Further to this, the Elexon consultation document stated that “Only in the instance of the losses Modifications has the Authority been unable to meet the ‘decision by’ dates” (paragraph 4.1). As mentioned earlier, it should be noted that both the Elexon consultation and this consultation are based upon an issue that has only arisen on an extremely small number of occasions. The Elexon consultation went on to state that “the remaining risk of the inability to revise Implementation Dates associated with ‘Pending’ proposals where *unforeseen circumstances* arise and where the open-ended construction was not initially adopted” (paragraph 4.3, *emphasis* added). It is our opinion that ‘unforeseen circumstances’ should not be confused with ‘difficult decisions’.

The Elexon consultation went on to give examples of potential Open Ended and Long Stop date solutions. The Drax response to the consultation document put forward the view that:

(a) An Open Ended date structure⁴ would:

- create uncertainty as to ‘whether’ and ‘when’ a modification will be approved, and possibly ‘what’ the outcome will be, particularly in circumstances where more than one modification proposal has been developed to address the same issue;
- in theory allow modifications to remain on the table for many years if there is no associated Long Stop date; and
- not take into account that the system changes over time: the considerations that are relevant in analysis performed today are not necessarily relevant one, three or even five years from now.

² Elexon Paper: Panel 144/08, Implementation Dates for Modification Proposals, http://www.elexon.co.uk/documents/Consultations/Consultation_on_Setting_Implementation_Dates_for/Attachment_1_Panel_Paper.pdf.

³ P198, P198 Alternative, P200, P200 Alternative, P203 and P204

⁴ Elexon Paper: Panel 144/08, Implementation Dates for Modification Proposals, paragraph 5.7 examples (a) and (c).

(b) A Long Stop date structure⁵ would:

- provide the Authority with greater flexibility;
- provide greater certainty to the industry than an open-ended date;
- ensure that the Authority will make a decision whilst the relevant code panel still considers the analysis to be valid; and
- be the relevant code panel's responsibility, as a panel of industry experts, to ensure that the date allows the required window for implementation and that the 'decide-by' date is relevant to the validity of the analysis.

Any such 'fall-back' date mechanism should have set criteria in order to avoid further regulatory risk and to completely separate the 'implementation date' decision from a 'merits of the case' decision. The key principle should be that the relevant code panel is the only body that should set the dates; as mentioned earlier, Ofgem have an input at the Modification Group and the relevant code panel meetings, but only the relevant code panel itself, with advice from the Modification Group, after consultation with industry and after advice from Ofgem, should decide whether the analysis contained within the Modification Report would be valid at the point of a third 'decide-by' date.

The Way Forward

As detailed in our recent consultation response to Elexon, and for the reasons set out above, Drax believes that an open-ended date structure would not be appropriate for many modification proposals, and that if any action is required to change the date structure for future modification proposals, a final 'decide-by' date should still be used that is relevant to the issues and analysis contained within the report. Drax proposes that in any case, a Long Stop 'decide-by' date should be no longer than six months after the second 'decide-by' date. As a result of this, the period between the associated implementation date and the Long Stop 'decide-by' date (the 'implementation period') may need to be longer, in order to allow the implementation to take place at the beginning of a financial year (if required); the length of the implementation period should be at the discretion of the relevant code panel, as advised by the relevant Modification Group and taking into account comments from an industry consultation. There should be a robust argument for using a Long Stop date and an industry consultation for the modification should address both (a) the need for a Long Stop date, and (b) the potential consequences of a delayed implementation date.

We firmly believe that the incentive must remain upon Ofgem to provide input to Modification Groups and to the relevant code panels, so that the implementation and 'decide-by' dates specified in the final Modification Report can take account of any issues that Ofgem or the Authority foresees. The current process requires the Authority to make timely decisions; this is a function of the modification processes that should be praised, as it helps to ensure greater stability for the industry (therefore consumers too). If new processes are introduced to the industry codes, they must take into account the consequences of changing implementation timetables; unilateral action by the Authority to change timetables without regard for validity of analysis, the resources of the code administrator or the associated consequences to stakeholders (including consumers) would not be sensible.

Drax recognises that the potential for analysis to be lost is a valid issue, but not a greater issue than the consequences of approving a modification containing analysis that may no longer be valid. Therefore, we believe that provided there are robust processes that ensure (a) reasonable, timely 'decide-by' dates and (b) the validity of the analysis, Long Stop dates would appear to be a more appropriate way to allow extra time for decision making in exceptional circumstances, as opposed to either of the options described in the Ofgem consultation letter. Open-ended date structures cause huge uncertainty; therefore their use is not an appropriate way to address this issue.

⁵ Elexon Paper: Panel 144/08, Implementation Dates for Modification Proposals, paragraph 5.7 example (b).

It is important that any decision to make a change to licence conditions or to change the processes contained within the industry codes with regards to implementation dates is not taken lightly. Any action taken by the Authority to introduce arrangements for the modification of implementation dates must be based upon sound judgement of the considerations raised by the Authority, the code administrators, the relevant code panels, industry parties and other relevant stakeholders.

Please do not hesitate to contact me should you wish to discuss our views further.

Yours sincerely,

Stuart Cotten

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Appendix 1: Paragraphs 81 to 83 of the Judicial Review Judgement (Case No: CO/11010/2007)

81. The second reason for not taking the course outlined earlier is this. It seems to me that on any view I am being asked to imply a power that is not expressly to be found in what on its face, and according to its terms, is intended to be a comprehensive code, on the ground that such a power is a necessary adjunct to the power of the Authority to control its own timetable for decision making. However, the question whether such a power is necessary or appropriate raises difficult and contentious considerations of industry policy, some of which compete with others. This aspect was recognised when the Panel and the Authority were considering whether the Panel should have a power to change its own timetable before the Authority made a decision on a Proposed Modification. At the time the Authority decided in unequivocal terms that, first, no such power was necessary for the efficient administration of the BSC and, secondly, that in the interests of regulatory certainty, the Panel should not have such a power: see paragraphs 46-47 above. It has not been suggested that there has been any material change in circumstances since the Authority rejected Proposed Modification P93.
82. It is correct that the relevant Proposed Modification then under consideration concerned a proposed power that the Panel, rather than the Authority, would enjoy, and that that power would be a general one, not limited in the way that I have put forward. Nonetheless it seems to me that the question whether the Authority itself should have what would be a somewhat more limited power raises in principle similar considerations of efficient administration and industry policy. I am not well placed to weigh those considerations, and certainly do not have sufficient grounds to conclude that the power claimed is necessary or would, on balance, advance the objectives of the BSC, particularly taking due account of the reasons for the Authority's strong rejection of a not dissimilar power in the Panel, and the absence of any material change in circumstances since that rejection.
83. Thirdly, and this point is connected to the second, I anticipate serious difficulties in this context if the Court were to embark upon what would be a legislative role in formulating the precise terms of the limited power to which I have referred. Such a power might need to be carefully crafted to cater for a number of contingencies that I am not in a position to foresee. One possible contingency has, however, already struck me on reading the evidence in this case. The justification for a Proposed Modification put forward by the Panel might be dependent upon a very time sensitive analysis of costs and benefits, and the Panel timetable for implementation might accordingly be tailored to that time sensitive analysis. If for any reason there were then a long delay before the Authority could take a final decision, a question might arise whether the Authority was in substance and reality considering the same modification as had been submitted by the Panel, or was considering an altogether different modification, putatively predicated on a cost benefit analysis that the Panel did not, and could not have, evaluated. In such circumstances a power to remit the matter to the Panel for complete reconsideration, rather than a power in the Authority to change the timetable for implementation of what had in substance become by lapse of time a different modification, might

better preserve the institutional balance between the Panel and the Authority and better serve the objectives of the BSC. I offer this as no more than an example of the potential hazards of judicial legislation in what is undoubtedly a technical and sometimes contentious field.