

Reference:



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Dear Mark

BSC Panel Response to Ofgem Code Governance Review: Major Policy Reviews and Self Governance

The BSC Panel welcomes the opportunity to respond to Ofgem's proposals to change the existing code governance arrangements. The present governance of the BSC went live in March 2001 and the BSC Panel has successfully overseen the change process in the intervening period within the framework it was given. However, the electricity industry itself has evolved over the same timeframe, and Ofgem's review of whether the code governance remains appropriate is timely. The BSC Panel itself has identified flaws with the BSC change process, most of which are reflected in the consultation and our response. The BSC Panel is therefore broadly supportive of the introduction of the new Major Policy Review arrangements, but notes that any new process should be accompanied by appropriate checks and balances to avoid eroding the existing rights of the industry, for example, in relation to appeals.

The individual consultation questions are set out in detail below and the responses represent the formal BSC Panel view. However, this does not preclude individual Panel Members responding directly with additional points they wish to make.

All references in the response are to the BSC change process and no comparison of the relative merits of the industry codes is intended.

Chapter 2: KEY ISSUES AND OBJECTIVES

Question 1: Do you agree with our assessment of the deficiencies of the codes governance arrangements and do you agree that there is a case for reform? Are the proposed reforms a proportionate response to the problems with the status quo that we have identified?

The BSC Panel has coped well to date with the BSC modification process but agrees that the lack of an holistic approach to improvements and the submission of a number of incremental changes to the same area can give rise to an increase in complexity with the consequent disbenefits in terms of the efficiency of the process. Two such illustrations under the BSC are the credit arrangements and the pricing calculations. We agree that the lack of strategic reforms can result in competing modifications, and also a duplication of assessments for Ofgem, participants and code panels, all of which result in an additional burden in terms of workload and delays to the delivery of benefits to the consumer.

The BSC Panel notes that the both the Major Policy Review and the self-governance proposals would result in shifts of authority from the present arrangements so must be accompanied by a proportionate level of checks and balances to avoid disadvantaging any sector of the industry.

Question 2: Would the Major Policy Review process enable key strategic issues (e.g. electricity cash-out or transmission access reform) to be progressed more effectively and efficiently with consequent consumer benefits?

For the reasons provided above, the BSC Panel welcomes a strategic approach to major reforms but notes the lessons learned from previous experience of significant changes to the BSC. The implementation of BETTA, where the outcome was clearly defined, was achieved successfully and within the desired timescales. The success of the cash-out review is questioned by Ofgem and the industry but the review itself provided little guidance as to any preferred solution. The BSC Panel therefore believes that the effectiveness of the Major Policy Review process would depend on the clarity of the intended solution. We would also welcome greater clarity as to the Panels' role in the development of major policy, e.g. would Ofgem take the opportunity to rationalise the consultation process, perhaps suggesting that the BSC Panel collates all the information necessary for Ofgem's final decision, including that relating to Ofgem's wider statutory obligations? This may lessen the consultation burden on both the industry and Ofgem.

Finally, the BSC Panel believes that the industry would find it helpful in managing its own resource if Ofgem issues a plan in advance (perhaps in the context of the Ofgem Corporate Strategy) of those areas it intends to target with a policy review.

Question 3: Would a Self Governance route be suitable for a significant proportion of modification proposals?

The BSC Panel agrees that subjecting housekeeping and lower level changes to the same full modification procedures that may be appropriate for more complex proposals unnecessarily ties up the resources of both the industry and Ofgem. However, it would be helpful if the introduction of any new process should be accompanied by a clear definition of the types of modifications which would be progressed under the different procedures. It is possible that as the new process becomes familiar, and confidence grows in the ability of the industry and the panels to cope with self-governance modifications, the scope of the changes that can use this route can be expanded. Any definition, therefore, should be capable of being amended to accommodate this.

The BSC Panel notes the importance of maintaining transparency and would like the new procedures to be equally flexible to allow for any operational improvements that are identified as the process evolves.

The BSC Panel is also mindful of the possible implications to its process and the implementation timetable of the self-governance route. Under the present procedures, when considering mutually exclusive changes impacting the same area, the BSC Panel judges each of them against the Applicable BSC Objectives and leaves it to Ofgem to assess their relative merits and to manage the sometimes varying implementation dates.

Finally, the BSC Panel DSO Representative notes his concern that Distributors' objectives are different from those of the BSC, and DSOs have sometimes to rely on this difference being taken into account by Ofgem at the end of the change process. The checks and balances accompanying the self-governance route should therefore incorporate some comparative protection for Distributors.

Question 4: If both the Major Policy Review and Self Governance routes were implemented, is there a case for retaining an Improved Status Quo path?

An improved status quo path will still be necessary, although the precise numbers will depend on the criteria applied to modifications which could be progressed under the self-governance route. Not all changes could currently be described as either relating to major policy changes or as 'housekeeping' amendments. It seems to us to be necessary to keep the third option to progress changes that still require significant industry debate on alternative solutions.

The BSC Panel would also like to understand the implications for the urgent process.

Question 5: If this package of reforms is implemented, should it apply to all codes? If not all, which? Should the introduction be phased?

No comment.

Chapter 3: FILTERING CRITERIA

Question 1: Once a modification has been raised, should the filtering decision be taken by Ofgem (with a panel recommendation) or by the relevant panel with an Ofgem veto?

The proposal that the industry panel allocates the modification to the appropriate process, with Ofgem maintaining the right to veto the choice, may be more efficient in terms of timescales. It is likely that if Ofgem has to exercise its right to veto it is because there is a lack of clarity around which category would apply to a proposed change, which endorses the need for a clear and agreed set of criteria. It would also be helpful if Ofgem indicates early when it is unlikely to agree with the BSC Panel's choice for those more borderline modifications.

Question 2: What criteria should be applied to assessing whether a modification falls into Path 1 or Path 2?

The BSC Panel will work to any set of criteria but would request that these are agreed beforehand and, as noted previously, be clearly defined. It is possible that not all changes will fit comfortably into one of the proposed categories and in those circumstances the BSC Panel would seek clarification from Ofgem.

The BSC Panel would also note the implications of introducing a new assessment process at the start of a proposed Modification which may require significant initial analysis and may thus negate any efficiencies gained from the changes being suggested elsewhere by Ofgem.

Question 3: How should we treat modifications that fall within the scope of an existing Major Policy Review?

It is the BSC Panel's view that it would help the industry in deciding whether to submit a proposed change, if the full scope of Ofgem's policy reviews, containing all the areas it will consider, is published in advance.

Chapter 4: **PROPOSED 'MAJOR POLICY REVIEW' PROCESS**

Question 1: What process should be adopted for Major Policy Reviews?

Whichever process is adopted, the BSC Panel would like to see the detail clearly set out. While the BSC Panel agrees that the current governance arrangements restrict the development of more than incremental changes, it may be that with the industry, code administrators and panels working together, the need for a full Major Policy Review could be pre-empted and only have to be initiated on a 'by exception' basis.

Question 2: What are your views on the Options for determining the outcome of a Major Policy Review?

The BSC Panel has stated its belief that Ofgem providing a more detailed solution is likely to result in a more effective outcome and, as a minimum requirement, would like to see the broad principles of what the change was seeking to achieve and would prefer a clear description of the solution. In respect of drafting the accompanying modification and legal text, ELEXON has the relevant expertise and the optimum solution must be to utilise this where it is appropriate to do so. The BSC Panel would note, for example, that for BETTA, Ofgem stated the requirements and ELEXON drafted the legal text. Should Ofgem decide that these are more appropriately drafted by Ofgem itself, the BSC Panel would seek to understand Ofgem's view on whether this would negate the need to convene a modification group.

Question 3: How ought the outcomes of a Major Policy Review to be implemented?

See the response to Question 2.

Ofgem also seeks views on whether it should have backstop powers to reject a modification. If a modification is developed through industry, the ability for Ofgem to reject it in line with its present powers seems to the BSC Panel to remain appropriate, although we would still like to see the accompanying rationale for any Ofgem decision. In line with the BSC Panel's view of the importance of checks and balances, it seems sensible if panels also had the option to recommend rejection of changes proposed by Ofgem if, in the opinion of the BSC Panel, a major flaw was identified with Ofgem's intended solution.

Question 4: What safeguards and appeal mechanisms should be in place?

The BSC Panel would hope that if the change process was right to start with, the number of appeals to decisions would be minimal. However, as long as the panels' recommendations remain unconstrained by Ofgem's development of modifications through the Major Policy Review process, then in the BSC Panel's view, the existing criteria for an appeal to the Competition Commission, under the Energy Act 2004, would remain equally appropriate in the case of modifications that are aimed at implementing Ofgem policy in the wake of a Major Policy Review.

The BSC Panel notes the importance of not eroding the rights of BSC Parties to appeal decisions.

Question 5: Should there be a moratorium on subsequent code modifications following the completion of a Major Policy Review?

The BSC Panel agrees that the efficiencies gained by the introduction of the Major Policy Review process may be undermined if further incremental changes can then occur. However, we also agree that there are instances when adjustments to newly introduced arrangements are required and this must be accommodated in the new arrangements. If this is only possible at Ofgem's discretion then any moratorium must allow for a clear process for issues that are identified after implementation to be fed back and raised, urgently where necessary.

Chapter 5: PROPOSED 'SELF GOVERNANCE' PROCESS

Question 1: Which model is optimal (Independent Panel, Representative Panel, signatory voting)?

The BSC Panel strongly believes that the current independent BSC Panel structure has served it, and the industry, well to date.

Question 2: Should it be mandatory for panels to have a consumer and a small market participant representative?

The BSC Chairman has written in a previous consultation response of the value of having consumer members on the BSC Panel and this applies equally to the smaller market participants (the BSC Chairman has recently exercised his ability to appoint an additional industry member and the BSC Panel as a result now also has the benefit of a member with a background in renewable energy). This structure has worked effectively, given the wide scope of the change proposals that the BSC Panel is required to consider.

Consumer Panel Members, however, have previously made the point that their usefulness would be increased if they were able to take into account the direct impact from any change on consumers.

Question 3: What voting procedures should apply governing code decisions?

The BSC Panel believes that its present procedure of a quorate majority vote is appropriate. The Panel Chairman simply has a casting vote and has rarely had to exercise this.

Question 4: What appeal mechanisms should be in place? Should defined appeal arrangements be set out or should Ofgem have discretion over whether or not to hear an appeal?

The BSC Panel would request that the introduction of any new appeals process be accompanied by clear criteria and be in line with good regulation guidelines.

Question 5: Should a consumer and small participant representative have an automatic right of appeal?

If the appeals process is fair and appropriate for all participants, there appears to be little benefit to be gained from granting special rights to any one constituency.

The BSC Panel believes that the outcome of an automatic right would depend on the cost associated with an appeal, and notes the caution exercised by the Government when an automatic right of appeal was not granted to BSC Parties in the Energy Act 2004. Should an automatic right have no costs associated with it, there would be a risk of opening the doors to vexatious appeals, designed to frustrate the process and delay the implementation of changes already adjudged to better facilitate the Applicable BSC Objectives. Conversely, if the associated costs were too high, that might dissuade smaller participants from appealing, irrespective of the strengths of their arguments. One alternative may be to extend the BSC Panel's obligations to consider the consumer and small party impact when making its recommendations.

In any event, such an automatic right would be dependent on a clear definition of the criteria to be applied in determining what qualified as a consumer group and who could be considered as a small party for this purpose.

Chapter 6: IMPACT ASSESSMENT

Question 1: Do you agree with our assessment of the package of reforms against the Review Objectives?

The BSC Panel notes that it is only appropriate for it to assess issues that fall within its jurisdiction.

The BSC Panel would like to reiterate its concern that, should Ofgem not identify and address all the relevant issues within the scope of each Major Policy Review, a subsequent moratorium on further modifications could be problematic should something significant be identified later.

Question 2: Do you agree with our quantitative assessment of the potential cost savings of reform?

The BSC Panel agrees that it would be more efficient in terms of the outcome if a set of coherent policy principles was agreed prior to the development of detailed modification proposals emerging from a Major Policy Review. However, in terms of an overall saving of time and resource for the industry, any assessment of costs must be speculative. The BSC Panel notes that some of the proposals introduce further requirements in the provision of data and analysis on the part of the industry, and potentially more work for ELEXON and the BSC Panel, that may impact such savings.

Question 3: Do you agree with our assessments of the potential impact of reform on consumers, competition and sustainable development?

No comment.

Question 4: Do you agree with our assessment of the potential unintended risks and consequences?

The consultation asks whether self-governance is likely to result in a smaller or greater number of appeals. As participants usually require the approval of their company boards to fund what can be an expensive process, it is the BSC Panel's experience that only changes which significantly impact costs are appealed. It would be our assumption that changes progressed under self-governance would not have such an effect.

The BSC Panel would also like to reiterate its view that the effectiveness of the proposed major policy review process is likely to be undermined unless the desired outcomes are expressed clearly, and to stress again the need for checks and balances to be in place.

Summary

The BSC Panel believes that the review of the change process is a timely exercise and will work under whatever new governance structure Ofgem determines but we would note that both the BSC Panel and ELEXON have considerable experience of the BSC and it would seem inefficient not to incorporate this expertise into any new process.

The BSC Panel would be happy to discuss any of the comments made in this response further, either at a BSC Panel meeting, or through contacting the BSC Panel Chairman directly (0207 3804251).

Yours sincerely

A handwritten signature in black ink that reads "Nick Durlacher". The signature is written in a cursive, slightly slanted style.

Nick Durlacher
BSC Panel Chairman