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Dear Andy

AEP response to your Major Policy Reviews and Self Governance initial proposals consultation

Thank you for the opportunity to respond to your consultation on initial proposals for major policy reviews (MPR) and self-governance. As you are aware the Association of Electricity Producers represents generating companies in the UK with our membership comprising a wide range of technologies utilising fossil, nuclear and renewable sources of energy. Our members include some of the largest through to the smallest UK energy producers many of whom actively participate in the development of all industry codes. We provide regular updates through our association committees for those who are unable to participate directly.

This consultation response has been compiled following discussions between our Electricity & Gas Committee, Electricity Trading Committee and Electricity Networks Committee. We have had presentations from Mark Feather, input from various industry code panel members and members of the DECC Better Regulation Team.

Whilst we agree in principle that the holistic consideration of the wider major policy issues prior to implementation of any solutions in the industry codes would be a good idea, we do not support the approach as outlined. In particular we have reservations about the desire of Ofgem to extend its remit to include the ability to mandate binding direction on the industry to raise code changes. We also have reservations about Ofgem developing proposals itself. These raise concerns around the capability of the Regulator to maintain the independent status mandated by primary legislation. These concerns are made significantly worse through the limited appeal rights that currently exist. We believe that it would be timely to review the current appeals process in light of these consultation proposals, particularly in order to provide comfort that they remain fit for purpose, are accessible to all and are not overly expensive. We view

updated wider appeal rights as a pre-requisite for any change to the existing governance processes.

Ofgem could play a vital role as facilitator for industry debate. The development of the New Electricity Trading Arrangements and British Electricity Trading and Transmission Arrangements showed that Ofgem, and its predecessor Offer, is able to carry out this role. Engagement in this facilitation role is important in order to ensure that all relevant issues have been considered including impacts on the environment, sustainability and not least consumers.

A further example of the value of this facilitation role is the joint initiative between DECC and Ofgem which provided industry with a strong steer towards development of proposals on which to base enduring transmission access arrangements. Industry then undertook the detailed development of these proposals including a 'Connect and Manage' approach which now appears to be the preferred government approach to deliver enduring arrangements.

This valuable role, developed and enhanced since the launch of the new electricity trading arrangements should not be discarded and replaced by a more interventionist regulatory regime. The uncertainty this would introduce would be a retrograde step at a time when the UK needs to attract long term investment in low carbon technologies and transmission networks.

It is unfortunate that Ofgem believes that the recent transmission access review process failed. We believe that all parties can learn something from the difficulties encountered in the review, but that, fundamentally, the process followed is the right one for major energy policy issues. Once DECC has set policy, providing clear views of the government targets and ambitions for the future UK low carbon energy supply profile, the industry should then develop proposals on how best to deliver the policy. It is the industry which has the capital to invest, the knowledge and experience of operating within the prescribed framework and the ability to ensure they fulfil mandated security of supply obligations.

We note that Ofgem's proposals do not sit within the framework of other industry regulators. The proposals are far wider than any other regulatory organisation and dilute parliamentary powers. Policy decisions should originate with Government and not within an industry independent regulatory body. As this is such a fundamental shift in duties does it require primary legislation in order to legally support it?

Whilst we welcome the fact that Ofgem have acknowledged consultation response views and have introduced some minor refinement against their initial proposals, we are still surprised at the lack of detail around what has been outlined within the consultation.

In summary, whilst we agree in principle that the holistic consideration of the wider major policy issues prior to implementation of any solutions in the industry codes would be a good idea, we do not support the approach as outlined. Our concerns relate to Ofgem's proposed role in directing the industry to raise changes or for Ofgem to raise changes itself and would view updated wider appeal rights as a pre-requisite for any changes to the existing governance processes.

Questions for clarification around the ‘rules of engagement’ include:

1. An explanation of the process prior to the announcement within the Ofgem Corporate Plan of what MPR’s will be conducted

The Government White Paper did not mention a requirement to change the basis upon which Ofgem carries out its statutory duties with regard to the future regulation of the Gas and Electricity Markets. Our members seek clarification round the trigger that leads to identification of a Government Policy issue to be addressed solely by the MPR route. Is there a register of reserved items for example? In addition we would seek details of the internal Ofgem process that then follows, including an overview of the Ofgem assessment of areas where, in their view, the current code governance arrangements lack the capability to ensure delivery of that policy and identification of industry inputs to this debate. Is this an area reserved for GEMA to make a decision? Is Ofgem planning to consult on this aspect of the arrangements? We also request clarity on the definition of the various significant, trivial and non trivial items and criteria against which Ofgem or the relevant panel would be required to make an assessment to determine which path a modification would take.

2. An explanation of the expected timeframe for the whole process. The MPR has been proposed in order to improve the timeliness of operation under the codes to deliver change more quickly.

An initial assessment of the process looks as though it could easily extend the development of proposals, particularly if Ofgem were to exercise the ability it reserves to itself to alter the direction the industry was initially instructed to take right up to final decision if it believes there is new information. The current code governance processes ensure that industry develops and assesses all change proposals in accordance with defined timescales. Any future arrangements should include defined timescales for Ofgem as well in order to improve regulatory certainty around future baseline arrangements.

3. An explanation of the triggers and controls re the use of Ofgem flexibility to reroute a proposal part way through development/assessment or even change ‘direction’.

Members wish to understand more fully the process and scenario’s under which this provision would be used by Ofgem. This should include how much notice would be provided and how much additional development time the industry would be allowed to develop and assess a new approach. We expect Ofgem to provide a full explanation of why a change in direction is deemed necessary and offer industry an opportunity to comment. We suggest that this redirection is limited to one per proposal.

4. An explanation of why the MPR and self governance proposals have to be a package.

To date Ofgem has not provided a full explanation why the MPR and self-governance proposal can progress only as a package. Unfortunately the paperwork submitted to the Authority which presumably contained the rationale for this approach is not publicly available. The Authority minutes do not provide an insight into the debate that took place amongst Authority members to test this rationale. As the consultation states that the self governance route is more efficient it is difficult to understand why implementation is tied to the MPR. It would be helpful to share principles debated by the Authority to improve general understanding

5. Three options for the outcome of a MPR are retained with a preference for Option 1 – High level binding conclusions and Option 2 – detailed binding conclusions with a back stop power in Option 3 for Ofgem to prepare modification proposal and legal text. A question was asked of the Ofgem representative at the BSC Panel as to what expertise National Grid would have to raise modifications on, for example, smart metering. The Ofgem representative stated that they are also looking at inserting provisions within Supply, Generator and Shipper licences to cover all eventualities, including requiring them to raise modifications. However, the Ofgem representative appeared to retract from this approach when further clarification was requested at the CUSC Panel. In order to be able to support the proposals, members need to see the draft text of the proposed amendments to their licences. Members would also like to see more details of the rationale behind this approach and register of reserved items for implementation linked to specific licences.

In addition the BSC Panel questioned provisions made within the consultation regarding Ofgem's conduct during the modification process where it has used Option 3 to raise the modifications itself bearing in mind that normal process invites the proposer to attend Panel meetings and become full members of modification groups in order to advocate their proposal. A clear distinction is required between the roles of Ofgem staff here in order to ensure that the discretion of The Authority is not fettered.

6. The impact on the current change management timetable requires clarification.

It is envisaged that the panels initially hear a presentation regarding a new change proposal and then, presumably taking into account views from the proposer and code administrator, decide that their proposal follows the normal or self-governance modification route. Ofgem then has the opportunity to veto that decision. No indication has been provided regarding how long it would take Ofgem to make this decision. Will Ofgem ensure that their panel representative at the meeting will be appropriately empowered to make that decision at the meeting? Where Ofgem use its veto provision is there a right of appeal by either the proposer or the panel?

7. Clarification is sought regarding the complexity proposed around use of the self governance route.

8. Members questioned why there are three appeal options within the self governance path and only one in each of the other two paths when self governance has been promoted to handle trivial issues of low consumer impact. In addition, as previously stated, Members believe that it would be timely to review the current appeals process in light of the consultation proposals, particularly in order to provide comfort that they remain fit for purpose, are accessible to all and not overly expensive
9. Clarification is sought regarding how Ofgem impartially balance the role of being Judge, Jury and Executioner?

Is it proposed that there be a separation of roles within Ofgem to address this peculiarity with regard to the design of the MPR route?

Answers to your specific consultation questions are included in APPENDIX 1. If you have any enquiries regarding this response please feel free to contact Barbara Vest, Head of Electricity Trading on 07736 107 020

Yours sincerely

David Porter OBE
Chief Executive

(By email)

APPENDIX 1

Answers to the consultation questions are as follows:

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?

We do not think that the proposals form a proportionate response to what Ofgem perceive as a problem with the industry codes. Specific examples relating to TAR are included in the consultation which unfairly report TAR governance issues and indeed it has subsequently been revealed that not only the industry but also DECC are not in accord with Ofgem with regard to the most appropriate way forward. Members have previously raised concerns about the validity of Ofgem acting as Judge, Jury and Executioner. These concerns have still to be addressed.

Question 2: Would the MPR process enable key strategic issues to be progressed more effectively and efficiently with consequent consumer benefits?

The Transmission Access Review is actually an example of good governance in that DECC and Ofgem conducted their Transmission Access Review alongside industry and then when there was an understanding of what was required modifications were raised. Although this time around it fell to National Grid to raise the original proposals, in future industry should be free to respond as appropriate. As currently proposed we believe the arrangements will only add to code complexity, costs and regulatory uncertainty

Question 3: Would a self-governance route be suitable for a significant proportion of modification proposals?

Yes for housekeeping and whatever Ofgem determine to fall within the definition of 'trivial, low consumer impact' proposals. It is hard to imagine that this would be a significant proportion of modification proposals

Question 4: If both the MPR and self-governance routes were implemented, is there a case for retaining an improved *status quo* path?

As currently defined there is not enough detail to provide a view, though we do not favour the introduction of MPRs

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

We require clarification as to why these changes can only be implemented as a package. If the self governance proposals would be an efficient and economical approach to progressing industry change, which would operate in the interests of customers' interests, it is not clear why the change could not be made on a stand alone basis or why it should not be applied to all codes?

Chapter 3: Determining the code modification pathway

Question 1: Do you agree that, once a modification has been raised, the filtering decision should be taken by the relevant panel, subject to an Ofgem veto that could be deployed at any point before a final decision on the proposal has been made?

This requirement should only be invoked where Ofgem believe it appropriate to downgrade a proposal from the normal governance path towards the self regulation approach if it does not use its power to veto at the initial panel stage. To do so any later in the process only increases regulatory uncertainty without commensurate benefit. Ofgem is currently required to give its views regarding the urgent treatment of proposals within five working days. The same approach could be adopted for decisions regarding self-governance therefore providing a window for industry to make their views known to Ofgem regarding such decisions. In addition the proposer of any change proposal should be required to make a case for use of the self governance route at the time they submit their change proposals. Code Administrators should also be required to make their views known during the initial presentation of proposals to the relevant panel.

It would be useful if Ofgem could clarify what criteria and analysis it would use in order to reach a decision on whether to support or veto a panel decision in this area and, if the right of veto is retained as proposed. For example, if the modification development is almost complete, there should have to be a much stronger reason for vetoing at such a late stage when all of the work has been done.

Question 2: Do you agree with the proposed criteria that should be applied to assessing whether a modification falls into Path 1 or Path 2? Is further guidance necessary?

We do not support the Ofgem proposals for MPRs as we do not believe it is within the Authority's gift to mandate or raise change proposals. Further clarification and guidance on the procedure to be adopted by code panels to use when deciding on whether a proposal is developed via the current or self governance route would be helpful

Question 3: Do you agree with our proposals for redirecting modification proposals between Paths 3 and 2?

See our response above

Question 4: Should code parties be able to make requests to Ofgem at any time that they can raise an urgent modification proposal to existing arrangements that are the subject of an MPR?

In a democratic process industry should not be constrained regarding the ability to raise change proposals. This would run the risk of postponing appropriate developments and delaying possible innovations. It is unlikely that the case for an urgent modification during an MPR would arise often, but if it does, it would be wrong and potentially dangerous to remove the ability for such a proposal to be raised

Do you agree that there should be a moratorium for non-urgent modifications to existing arrangements that are the subject of an MPR?

We do not support the MPR proposals as currently outlined

Chapter 4: Major Policy Reviews

Question 1: Do you agree that Ofgem should retain the flexibility to vary the MPR process according to the complexity of the issues involved?

We do not support the MPR proposals as currently outlined

Question 2: What are your views on the options for determining the outcome of an MPR?

It would be most helpful for Ofgem to share its legal advice to assist industry in understanding how these changes can be made. In addition clarification of how it will engage in the process when promoting its own proposals is required. We have concerns about the outcome of an MPR being legally binding and as such imposing the views of Ofgem into the overall design of the market as raised in responses to the previous consultation.

Question 3: Do you support our proposal that the industry should be given the responsibility of drafting appropriate MPR-related code modifications, with Ofgem having a power to draft them only if the industry fails to do so within as specified time period?

See answer to Question 2 above. In addition we do not agree that any licence changes are required. If industry desire change they are well capable of raising change

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

Members have expressed concern about the costs associated with any appeal making it out of the reach of most participants

Question 5: Do you support our proposal for a time-window in which subsequent code modifications could be proposed after the completion of an MPR?

No. The current modification regime allows for modifications to be raised at any point and this provision should not be removed. A two month period appears too short if Ofgem are only going to accept fully worked up proposals. It is often the case that during the assessment of a proposal an alternate approach is only identified after a considerable amount of discussion and assessment has occurred. This is not always the case during the first two months of assessment of a proposal. Transposing restrictions imposed during a competition commission appeal are impractical as it is possible that serious flaws in the market arrangements may be identified

Question 6: Do you agree that Ofgem should be able to revise its MPR conclusions in the light of subsequent new information?

How does this deliver regulatory certainty to this complex regime? More details are required regarding the process to be adopted here including whether the proposal provides for reassessment of analysis, further industry consultations, modification group meetings, panel deliberation and the ability of the panel to change their original recommendation?

Chapter 5: Self-governance

Question 1: Do you agree that the industry should draw up proposals for panel and voting arrangements and submit them as part of a self-governance package to Ofgem for approval?

We would appreciate guidance from Ofgem on any major concerns it would wish to see addressed before the industry begins this work

Question 2: Do you agree with our proposals for redirecting modifications from Path 3 to Path 2?

If the panel have made a judgement then Ofgem should have been engaged in that process in the first instance and should not therefore require any redirection. In addition Modification/Amendment proposal forms should be amended to include a recommendation from the proposer on their preferred route which should include evidence to back up their preference. It would be good practice to intervene only when proposals should move from the current governance path into the self governance regime

Question 3: Do you agree that there should be general appeal rights equally applicable to all code participants? Do you agree with the proposed grounds for appeal?

Yes. Treat all industry participants equally

Question 4: Do you agree that Ofgem should hear appeals of self-governance modification decisions? Do you support the proposals in respect of interim forums, time limits and frivolous or vexatious appeals?

Ofgem should hear all appeals. However a better idea about the time and costs incurred under the interim forum approach is required

Appendix 2: Impact assessment

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

No. We can only see the process as outlined adding significant cost, regulatory uncertainty and complexity to the current arrangements which have worked well since their introduction at NETA Go Live

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

No. The added complexity and potential for redirection must add costs and time to the whole process

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

No. The added complexity and potential for redirection must add costs and time to the whole process

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

Ofgem state that 'the risk of inappropriate decisions being taken through self-governance is a real one'. What evidence has Ofgem examined in order to reach this view?