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Dear Andy,

Major Policy Reviews and Self-Governance, BWEA Response

BWEA is pleased to respond to your initial proposals on Major Policy Reviews (MPRs) and self-governance. Our comments, structured by subject headings which are broadly in line with the headings in the consultation document, are as follows:

The overall case for reform

Ofgem's case for reform is expressed in Chapter 2, "Key issues and objectives". In general, BWEA welcomes the principle of some kind of oversight or guidance of major policy reform. We welcome the move to a more strategic approach rather than the existing, usually piecemeal, approach of the existing code modification process. BWEA also tends to agree that strategic reform does require some leadership where there are some rather intractable issues.

Finally, we agree that strategic and wide-ranging reform such as smart metering and European-wide code issues would be likely to benefit from a more strategic approach to code modifications. Coherence and convergence (rather than a 'silo'-type treatment of issues) will be essential for areas such as this.

BWEA is very heartened that in identifying and assessing MPRs, Ofgem is giving priority to issues impacting on sustainable development. In and of itself this heightened emphasis is very welcome.

The TAR process is highlighted by Ofgem as an example of why reform is needed (2.5). BWEA's take on the TAR process differs from Ofgem's. We acknowledge that there were some naturally strongly-held differing views expressed during the TAR process. This is the nature of a market which relies on competition, and in many terms it is its strength. There were also some significant areas of agreement across industry.

We do not share Ofgem's view, expressed elsewhere, that TAR failed to deliver results. BWEA would stress that the TAR process was a good example of trialling dual consideration of access and charging: this was very productive and lays some of the groundwork for the type of reform that Ofgem is trying to achieve via MPRs. TAR also encompassed some carbon-related costs in some impact assessment-type analysis, even

though this was not strictly necessary under the CUSC at that time – again these kinds of wider considerations are a feature of the proposed MPRs.

Furthermore, the volume and duration model, which Ofgem appeared to favour towards the end of TAR, evolved from industry discussion and debate during the TAR process. The discussion was wide-ranging and resulted in a capacity and duration model going forward as an alternative to price-based auctions. It was ultimately the Working Group's decision on the volume and duration Alternative Modification which was a source of frustration for Ofgem.

Therefore, it appears simply to be a difference of opinion, and the ability of industry to influence what does and does not go forward to Ofgem for a decision, that is the source of Ofgem's frustration with TAR. To the extent that the MPR process addresses this by giving Ofgem the ability to unilaterally impose its own opinion, and itself decide what does and does not get considered, then of course that will accelerate and streamline the process.

BWEA notes that someone has to make a decision, and an impartial Regulator is, on the face of it, an appropriate decision-maker. However, we believe that participation in the MPR process will be enhanced only if participants feel that participation is worthwhile. For the MPR process to be effective, Ofgem must be seen as genuinely willing to change its opinion and be open to challenge. BWEA has mixed views and experiences on whether this is, and has been, the case. We acknowledge that Ofgem is in a state of flux on its guiding principles and duties, and that it will take some time for the new emphasis on sustainable development to permeate everything that Ofgem does.

BWEA might be more comfortable if, for instance, there was some meaningful oversight or a power of veto from, say, a Panel of impartial expertise appointed jointly by Ofgem and the industry. This might encompass a peer review role for decision-making, as well as formulating and overseeing analysis and impact assessment work. The term "major policy review" implies a strong emphasis on implementing high level government-framed policy objectives, and so we would query whether there should be a stronger guiding force from Government in the MPR process.

The MPR process

In general the process seems reasonable and we agree that the process should be flexible for what is now a fast-growing and fast-changing market.

As noted above, we are concerned that a lot of important decision points in the process are essentially a judgement call by Ofgem. We appreciate there is a balance between inflexible rules and allowing some room for judgement based on the context. But we do need some assurance that judgement will be exercised appropriately and will be fully and properly justified.

Some specific points are:

- **Initiating MPRs**

Ofgem is proposing that it is the sole initiator of an MPR, albeit that it will take into account other views. It is not clear what would happen if there was an industry code modification that Ofgem deemed to be of MPR material/impact, but with which Ofgem disagreed. At this point would Ofgem block the modification? If Ofgem accepted the proposal as an MPR despite its reservations, then Ofgem is not really the sole initiator of MPRs.

BWEA cannot see how Ofgem can be the sole initiator of MPRs, and not at the same time prevent some issues from being debated as an MPR. As Ofgem has strongly criticised the existing arrangements and the events around CAP 171/2 (which Ofgem believes resulted in proposals not being properly debated) we cannot see how an MPR process can work satisfactorily without other parties being able to initiate an MPR.

- **Foresight of MPRs**

The plan to indicate proposed MPRs in Ofgem's Corporate Strategy and Plan is helpful (2.32) and will give early notice to some studious stakeholders. However, not everyone reads Ofgem's Corporate Strategy, and so a more concerted effort to engage stakeholders via some more popular media outlets would be very much appreciated. We would also stress the need to frame policy proposals in accessible language.

Foresight of MPRs raises the question of whether MPRs should be raised 'off-plan' as and when circumstances require. There could be issues that do not qualify as urgent but which have nonetheless not been anticipated. BWEA would support some flexibility, but would again stress the need to have effective communication channels for all forthcoming MPRs.

- **Filtering process – path 2 or 3**

Ofgem proposes that the relevant industry panel should filter proposals into either a Path 2 "reformed status quo" arrangement, where industry develops and debates the proposal and Ofgem makes the decision; or a Path 3 self governance route, where industry develops, debates and decides. Ofgem is, however, proposing to give itself the power to redirect proposals from Path 3 to 2, right up to the decision time on the modification.

These provisions effectively allow Ofgem to intervene in the event that it perceives the industry will come to a conclusion contrary to what Ofgem might decide, had it been the decision-maker. This arrangement is really not self-governance. It has the potential for industry to waste a lot of time developing proposals which could be derailed or altered at the last minute. BWEA would in this context question whether the self-governance route is worth pursuing at all if Ofgem cannot relinquish control over anything. BWEA's concern here is not who makes the decision, it is the uncertainty created around the self-governance route. If there is to be any self-governance, we would prefer a time-limited window for Ofgem to re-direct proposals.

- **Filtering criteria**

BWEA agrees that in broad terms the criteria are reasonable but we also agree with "*the majority of respondents*" who thought that "*the criteria needed to be more detailed to reduce the scope for subjectivity or creative interpretation*".

- **Justification for decisions**

Ofgem has in the past been tautological in its justifications for decisions – using its own views as self justification, rather than objective, pre-agreed criteria and/or hard evidence. Therefore, BWEA would be supportive of some pre-agreed guidance and criteria for the main decision-making points, such as what constitutes an acceptable "Alternative" modification.

- **Altering MPR decisions**

Ofgem says that "*the Authority should have the ability, where necessary, to revise its policy or reconsider its MPR conclusions and issue new directions, for example, as policy detail develops or if new information comes to light that has a bearing on them.*" (4.60)

BWEA cannot support a catch-all power that would allow something that has been openly debated in an MPR to be changed via a process that has not been described in this

consultation and which may or may not be open and consultative. In any event, surely any absolutely essential changes of emphasis could be covered by the urgent modifications process – we see no need for any additional powers in this respect.

Furthermore, consistency and stability is important to market participants, more so than the constant refinement of market arrangements in pursuit of someone's definition of perfection. Changes in policy should never be undertaken lightly, and especially so after an extensive process of debate and decision-making.

- **Urgent modifications**

BWEA agrees that there is a time and a place for urgent modifications, and that matters subject to an MPR should not be excluded. Again, we note that the definition of "urgent" has in the past been debatable and we believe that this process merits some improvements.

- **Safeguards and appeal mechanisms**

BWEA agrees that the provision of an appeal mechanism is important but notes that appeals can be difficult and resource-intensive. We understand the Competition Commission (CC) route to be relatively well defined and expedient, but note that the costs will probably still be prohibitive for smaller players. BWEA also has concerns that the CC route is only available where Ofgem's decision differs from the majority recommendation of the relevant Panel. This is especially so where Ofgem has the power – as proposed in another Code Governance consultation – to appoint the Panel chair (combined with existing powers to nominate some other Panel member(s)). Either Ofgem should relinquish its influence over the Panel make-up to, for instance, Government, or the CC appeal route should be irrespective of the Panel's recommendation.

- **Time-window for code modifications after the completion of an MPR**

We welcome the opportunity to put forward Alternative modifications (4.56-4.58), but consider that this should be allowed during, rather than after, the MPR has concluded. The MPR process is not very well defined in this consultation, but we would envisage that each MPR would tackle a certain problem to which there would be a number of solutions. There should be scope during the MPR which would allow industry some meaningful influence on the nature of any solution. It is difficult to see why this influence should be brought to bear after Ofgem has already made up its mind, especially as Ofgem will be making the decision on the MPR conclusions and any Alternatives proposed.

Furthermore, the "*time window*" of opportunity to propose Alternatives is in stark contrast to the power that Ofgem is proposing to give itself to change an MPR decision at any time in the light of new information. To reiterate BWEA's position, if the MPR is run properly, and considers everyone's views openly and fairly, there should be no need for anything other than an urgent process after the event – this goes for industry as well as for Ofgem.

Ofgem's proposal to turn down alternative proposals (within the time-window) (4.59) if they are '*insufficiently developed*' needs to be further defined in order for us to have a view. It is also interactive with Ofgem's Code Governance proposals in support of participation of smaller players who may need support in developing Alternatives.

- **Determining the outcome of an MPR**

Ofgem describes in 4.17 to 4.28 its rationale for proposing that Ofgem develops high level principles via an MPR which it then directs industry to codify and implement. BWEA finds it difficult to understand Ofgem's rationale for these proposals. We believe that developing the conclusions of an MPR, and stating these clearly, is paramount. It should then be incumbent on the code administrators to implement these changes in an

appropriate legal form. In the new world where code administrators are independent critical friends, this really should not be a problem.

The key question is who bears the cost of preparing the legal text. BWEA believes that it would be inappropriate for Ofgem to pass on this cost – and responsibility – to individual licensees. This is because Ofgem, through the MPR, has removed ownership of any major reform from individual licensees. Rather, the code administrators should have the necessary resources allocated to them. We see absolutely no merit in making the conclusions “*binding*” on those preparing the legal text. This presupposes that Ofgem does not trust the independence of the code administrator. If this is the case, then there is little point in the code governance reform.

Similarly, we see no merit in a backstop power for Ofgem to prepare draft code modifications. It seems much more sensible to simply resource the code administrators appropriately, and ensure that they act independently.

In general this aspect of the proposals reads as if Ofgem wants to take entire control over major policy reform and implementation, but does not have the appetite in-house for preparation of the legal text. We would suggest either bringing legal text expertise in-house or trusting the code administrators to do their job. Ofgem’s proposals for retaining control but not taking the responsibility are bureaucratic and unwieldy.

Timescales

BWEA also notes that there appear to be no set timescales for Ofgem to come to a decision on an MPR. We appreciate the need for some flexibility but we would be supportive, at the very least, of some guidelines and monitoring of Ofgem’s performance on timely decisions.

Design of the self-governance arrangements

BWEA believes that there is merit in a streamlined self-governance process that deals with non-contentious, sensible changes to the codes. We would envisage this being very useful, especially for renewable projects which present new situations and challenges for the codes. If it is an efficient process, it could allow codes to be modified to fit project circumstances rather than asking projects to sign up to requirements which are really not suited to them.

Our major reservation, as noted earlier, is the prospect of Ofgem altering the path of a modification at the last minute.

We would imagine that most of the changes would be housekeeping, quite technical or legalistic. As such we would not envisage any major battles on Panel representation – it may even be difficult to find representatives willing and able to debate these kind of changes. Representation is fuelled by commercial interest and the likelihood of differences of opinion. By design, there should not be this kind of motivation to join the self-governance panel. As such, perhaps representation should be through some kind of pooled fund for expertise rather than direct representation of individual companies.

BWEA supports a right of appeal to Ofgem, but notes that the expressions “*frivolous, vexatious or no reasonable prospect*” will be not be a sufficient explanation for declining an appeal (5.25). A time-frame for requesting an appeal of 10 working days is quite short. In any event it will be important to ensure that the modifications going through the self-governance process are well publicised.

We are not supportive of the proposal to require parties to bear the costs incurred by Ofgem through an appeal “*under certain circumstances.*” This runs somewhat contrary to

encouraging participation by smaller players, unless the circumstances are clearly defined and exclude small parties. We also cannot understand what circumstances might merit this, if Ofgem can already decline to hear an appeal in the first place. It also raises the question of whether industry parties should be able to claim costs from Ofgem should it re-direct a Path 3 modification at the last minute.

We believe that Ofgem's effort would be better spent in minimising the likelihood of appeals through a non-combative make-up of the self-governance panel. This could also negate the need for an additional "forum" to consider appeals.

Impact Assessment (Appendix 2)

BWEA agrees that reform of the existing piecemeal approach to code modifications is a desirable change for major policy reform. Whilst we understand and agree that there will probably be cost savings for Ofgem, we are not assured that this will be the same for industry.

BWEA would note for instance the potential costs to industry of Ofgem's ability to re-direct modifications from Path 3 to 2 right up to the last minute, and those of allowing Ofgem to change an MPR Direction under as yet unspecified circumstances. Uncertainty and change costs money and this should be considered in the impact assessment. Furthermore, some of Ofgem's costs are simply being re-distributed, such as the proposal for certain parties to pay unsuccessful appeal costs under self-governance.

We are also not convinced that there will be benefits for competition of the MPR process (1.59-1.60). As noted, we believe there is the potential for parties to disengage if inclusivity is window-dressing of the process rather than a genuine prospect of influencing Ofgem's thinking. There are also resource and complexity issues for small players which are not addressed by the MPR process in of itself. Therefore, the impact on sustainable development (1.61-1.62) is too vague.

We acknowledge though that the subject matter of some of the envisaged MPRs – such as smart metering – is in support of sustainable development objectives. We would hope that prioritisation of this kind of reform, combined with Ofgem's enhanced sustainable development duties, would deliver significant improvements.

Ofgem proposes a "*post-implementation review*" of the "*effectiveness*" of the proposals. BWEA would strongly urge a definition now of the measures by which effectiveness will be judged – for instance, a satisfaction survey of small players, the number of new players that have been engaged in the process, modification timescales, carbon abated by approved modifications, etc.

BWEA hopes you find these comments useful. If you wish to discuss any aspect of this response, please don't hesitate to contact me.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Gordon Edge', written over a light blue horizontal line.

Dr Gordon Edge, Director of Economics & Markets, BWEA