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Ofgem
9 Millbank
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Dear Mark,

Re: Review of Ofgem's Impact Assessment Guidance

This response is submitted on behalf of SSE plc and Scotia Gas Networks Limited (SGN) who welcome the opportunity to respond to this consultation. As regulated companies with interests covering generation and transmission of electricity, distribution of gas and electricity, and supply of gas and electricity, we have observed the development of Impact Assessments across a wide range of subject areas and this experience is reflected in our response to the questions posed in Appendix 1.

In summary,

- we welcome the move to a more iterative approach to developing Impact Assessments, allowing Ofgem to revise and refine the assessments as policy develops;
- we welcome the intention to move towards a more consistent approach and standard in Impact Assessments, with flexibility to reflect the aspects particularly affected by the policy in question;
- to support users of the Guidance (both internal to Ofgem and externally), we recommend that greater depth to how analysis should be carried out will support the intention to achieve a more consistent standard, as well as informing stakeholders' expectations;

- we welcome the intention to consider the totality of impacts and recommend that, to fully capture these, greater consideration of parallel policy developments and how these interact should be provided;
- we encourage Ofgem to remember the importance of diversity when carrying out Impact Assessments, to avoid an over-reliance on average costs, and consider using total costs in certain circumstances to ensure outliers are not overlooked; and
- we recommend a greater involvement of a wide range of interested parties in the initial development of Impact Assessments to broaden the range of evidence available to Ofgem and thus avoid inherent bias.

We appreciate the importance of Impact Assessments to Ofgem's decision-making processes and are willing to discuss any of the points raised in this response in further detail. If this would be beneficial or you have any questions in relation to this response, please feel free to contact me as above.

Yours sincerely,

Aileen McLeod
Head of Regulation, Networks

Appendix 1: SSE and SGN response to Consultation Questions

Question 1: Do you agree with our approach / emphasis?

Yes, we do agree with the proposal to make the Impact Assessment a continuous, iterative process. Given that a significant number of policy areas developed by Ofgem evolve over a period of time in response to changing environment, other policy developments and stakeholder feedback, it is essential that the associated Impact Assessment also evolves to reflect policy developments and increased information being available to Ofgem.

We welcome the increased clarity around the role of consultation in developing Impact Assessments and the proposed timescales seem reasonable. Where the Impact Consultation in question arises from a Code Modification, we believe that shorter consultation periods are appropriate as such proposals will normally have been subject to a full consultation through the Significant Code Review process or similar. Prompt assessment by Ofgem will enable the industry to deliver the identified change in a timely manner.

We welcome Ofgem's desire to ensure a consistent quality or standard to the Impact Assessments that it develops, whilst retaining sufficient flexibility around the application of this Guidance to reflect the policy area under development. We suggest that to assist transparency of how such flexibility is being applied, a statement could be provided within the introductory section setting out the elements of the Guidance of particular relevance to the policy area that have been focussed on during the development of the Impact Assessment and Ofgem's reasons for this focus.

To ensure consistent quality in the Impact Assessments produced, we suggest greater detail in terms of how the Impact Assessments are to be carried out, particularly in relation to the analysis of impacts (discussed further below in response to question 2). This will assist both internal users, in terms of carrying out the analysis, as well as external users in understanding the approach being adopted.

In addition to the proposed approach set out in the consultation document, we suggest that Ofgem may wish, at least for some matters, to consider holding an Impact Assessment workshop where stakeholders are invited to contribute to the impacts to be assessed and also the evidence to be used by Ofgem in assessing these impacts. We believe that such sessions would ensure that initial Impact Assessments are more informed and based on a broader range of evidence than might otherwise be available to Ofgem acting in isolation.

It is our understanding that Ofgem may use Peer Review (both internally and externally) to further develop Impact Assessments. We support this approach but suggest that 'Peer' is interpreted in a broad sense to include a wide range of informed parties who could

constructively contribute to this process, including (but not limited to) academics, consultants, NGOs, statutory consultees, consumer representatives and industry parties. Such review may also assist to avoid any inherent, institutional bias by drawing out other views and perspectives on the evidence available.

Question 2: Do you agree with our approach to assessing impacts?

It is our understanding that the revised guidance is intended to drive a greater focus on the totality of impacts, rather than the current approach of considering impacts against specific categories. We welcome this revision and, whilst it is likely to result in a slightly more complex assessment, we believe it is essential that the impacts of proposals are assessed in such a manner to ensure that the full implications are properly considered and understood.

To ensure such assessments truly capture the totality of the potential impacts, we recommend Ofgem ensure that whole system impacts are considered. The development of a policy related to electricity transmission, for example, should consider the consequences for generation, distribution, wholesale and retail markets, and end consumers.

We also suggest that Ofgem may wish to extend this approach slightly further to take into consideration other related policy areas that may also be in development. We do appreciate the inherent difficulties of incorporating other policy areas that are also subject to further evolution. However, given the increasing complexity of the sector and the consequential implications from other policy developments, we believe it is only possible to truly understand the aggregate impacts and avoid any perverse outcomes by extending the assessment to cover such related developments.

We recognise that Ofgem's approach to conducting Impact Assessments does vary from other public bodies, such as DECC, BIS, and the Treasury. However, it would be beneficial if this was explicitly stated within the Guidance document to ensure that all readers understand that Ofgem's approach to decision making does differ from such other bodies.

For policy areas that are developed in conjunction with other public bodies, the agreement of a consistent basis that analyses will be conducted against will assist all parties to understand the development that the policy undergoes. Additionally, a common approach will increase transparency and clarity around how such joint or follow-on assessments are conducted.

Common, referenced, and publically available sources of data to populate such assessments will assist readers in reviewing the analyses and providing constructive feedback through the consultative approach discussed above. Where there is a variance in the assumptions that

are applied by different public bodies, it would assist if a detailed discussion of such variance was provided in the narrative. This will draw out where issues associated with carrying out the cost-benefit assessment, for example, are not clear cut and allow all parties to appreciate the range of potential variables.

At the high-level provided within the consultation document, we agree with the three aspects identified, namely monetised, aggregate cost-benefit analysis; distributional effects; and long-term, hard-to- monetise considerations. Further information on how such analysis will be conducted would be beneficial for both internal and external users of the guidance. Alternatively, greater sign-posting of the approaches identified by Ofgem as best practice would increase the transparency and understanding of how these aspects will be analysed.

In carrying out cost-benefit analysis, we urge Ofgem to avoid an over reliance on average costs. In our experience, there are no such things as 'average costs' and total costs may be more applicable to consider in some situations. We also recommend that Ofgem don't dismiss outliers in its analysis. Not all companies active in the energy sector are homogenous and even companies within the same licence class can have very different cost bases. As raised during discussions on the Retail Market Reform, for example, costs faced by parties to implement some of the proposals will vary significantly dependent on the nature of the IT system that respective organisations have implemented. Whilst we appreciate the additional complexity that such data points can introduce, it is essential that such outliers are properly understood and considered (even if the detail of such consideration is only briefly referred to in the published Impact Assessment).

In a similar way, we support Ofgem's inclusion of distributional effects within the aspects to be assessed and stress the importance of diversity within such assessments. However, we suggest that such effects shouldn't be limited to the effects on consumers. The diverse geography and climate of Great Britain, for example, can mean that a policy that is applicable for south-east England may not be appropriate in the Highlands and Islands of Scotland. For example, the time required to physically travel and identify a fault in remote areas tends to vary significantly from the time in an urban environment. Similarly, in areas where mains gas is not available, policy measures to promote dual fuel offers will not be applicable and may have unintended consequences.

Question 3: Do you agree with our approach to considering long-term, complex and hard-to-monetise issues?

We support the proposed approach. However, we recommend that Ofgem does not limit what can be considered under each of the assessments as changes in future priorities or specifics of a given policy area may require further elements to be considered. Whilst the proposed components seem appropriate at present, changes to policy at a local, national, European, or international level may present other areas that the implications of a given policy should be assessed against.

In considering strategic and sustainability issues, we suggest Ofgem may wish to draw out the potential choices that a given policy may trigger. Undergrounding of electricity networks, for example, requires consideration of issues including visual amenity, biodiversity / impacts on habits, removal of peat (particularly in Scotland) or other materials and financial costs. Greater narrative to illustrate the range of impacts of a policy on such matters will allow the reader to more fully understand the long-term implications and the difficult choices that Ofgem and industry parties are required to make.

Question 4: Are there any other substantive changes that we should consider incorporating in the guidance, as appropriate to our statutory duties and functions?

As discussed above, further detail on how the respective assessments will be carried out, common sources of data for compiling evidence, and examples of best practice in conducting the three elements of an Impact Assessment would be beneficial for both internal and external users of this document.

Within each of the categories of the assessment (i.e. cost-benefit analysis, distributional effects, and longer-term considerations), we recommend Ofgem should give consideration to the implications on investment within the sector in line with its statutory duty to secure that licence holders are able to finance the activities subject to obligations under the Gas and Electricity Acts.

In line with the principles of better regulation, consideration of whether the development of policy in a given area can lead to a reduction of regulatory obligations in a related area should be incorporated into the Impact Assessment. The greater use of Outputs in network regulation as part of the RIIO framework, for example, shifts the nature of reporting that Ofgem requires from Network Operators to focus on performance against such Outputs, rather than the historic approach of looking at Inputs.