

# Summary of responses: Consultation on changes to our Guidance on Impact Assessments

## Final decision

**Publication date:** 1 October 2013

**Contact:** Mark Wagstaff

**Team:** Better Regulation

**Tel:** 020 7901 0500

**Email:** Mark.Wagstaff@ofgem.gov.uk

### Overview:

Impact Assessments (IAs) are a vital part of our decision-making process and provide a valuable framework for assessing the impact of important regulatory policy proposals.

We consulted on proposed revisions to our IA guidance during March–June 2013. The proposals incorporated:

- developments in government guidance (eg Better Regulation Executive, HMT Green Book guidance)
- changes to our statutory responsibilities (eg Equality Act 2010, the Third Package)
- approaches to protecting the interests of future as well as existing consumers, as elaborated by our thinking on strategic and sustainability considerations.

We received responses from 30 organisations, representing industry (suppliers, transmission/distribution operators and their representative bodies), consumer groups and other NGOs, government and academic perspectives. Overall, we received high levels of support from stakeholders (across all sectors), with feedback mainly comprising suggestions for improvement. This document summarises the responses to the consultation questions and sets out our subsequent views.

Based on the high levels of stakeholder support, we intend to proceed with the main proposed changes and incorporate a number of enhancements suggested by stakeholders to improve the final guidance, where these are consistent with our objectives and statutory duties.

# 1. Consultation responses

---


- 1.1. During March–June 2013, we consulted on proposed revisions to our Impact Assessment (IA) guidance. We received public responses from the following organisations, alongside a number of informal responses:

- Consumer groups and other NGOs: Centre for Sustainable Energy, John Muir Trust, Consumer Futures, CPRE (South Yorkshire) and Friends of the Peak District, Fuel Poverty Advisory Group
- Transmission and distribution companies: National Grid, Electricity North West Limited, UK Power Networks
- Representative networks: Renewable UK, Energy Networks Association, Energy UK
- Suppliers: RWE npower, SSE, Scottish Power
- Government and regulators: Ofwat, Scottish Environment Protection Agency, Scottish Natural Heritage
- Academic: Prof Michael Power (LSE)

- 1.2. The responses are published on our website. Below we summarise the responses to the consultation questions and set out – in italics – our subsequent views and approach.

**Question 1: We are proposing to revise the structure of the guidance to place greater emphasis on Impact Assessment (IA) as a continuous, iterative process. Do you agree with our approach / emphasis?**

- 1.3. The majority of respondents agreed with this approach. However, several respondents called for greater clarity and consistency over the format and presentation of our IAs.
- 1.4. These comments included adding a preliminary consideration of why we are undertaking an assessment (eg justifying the regulatory intervention), and ensuring that the iterative approach did not lead to the 'double-counting' of impacts (eg where carbon costs are already embedded in prices)
- 1.5. *We have attempted to clearly describe the IA process (eg in Chapter 2: What format an IA will take and Chapter 3: The IA process). We have also reflected these changes in the 'flow diagram' in the guidance (Figure 1) to help illustrate this process.*
- 1.6. In commenting on the IA format, several respondents indicated that whilst a flexible approach to IA is sensible, there is merit in adopting a standardised presentation so that stakeholders develop familiarity with the format and come to expect information to be presented in a consistent manner. Views differed on the best way to achieve this, ranging from adoption of the




## Summary of responses: Consultation on changes to our Guidance on Impact Assessments

government/BRE template through to all IAs having an introductory text setting out the particular factors under consideration.

- 1.7. We also received comments in relation to the length of IAs (with preferences for shorter, less repetitive IAs) and requests for more inclusive, non-technical language.
- 1.8. *We envisage IAs and policy documents as being developed simultaneously, with the IA analysis informing and influencing thinking throughout the policy development process. To this end, we do not envisage IAs forming a separate document in every instance – instead, the IA analysis will often be embedded within the policy/decision document, with key headings cross-referenced to a template in the annex or presented as an executive summary drawing together the key features of a proposal. We may however still choose to produce a standalone IA where this is helpful.*
- 1.9. Some respondents commented that IAs should not be waived on the grounds of 'urgency'. This concern was based on a perception that 'urgency' could lead to certain impacts not being considered (eg environmental issues).
- 1.10. *This option is provided for in legislation (Section 5A of the Utilities Act (2000)) and we would expect to use it only in exceptional circumstances. We have clarified this in the guidance, and should these exceptional circumstances arise we would expect to learn from the situation in order to mitigate / avoid the possibility of similar circumstances arising in the future.*
- 1.11. Several respondents highlighted the importance of IA consultation as a key mechanism to ensure Ofgem informs and engages with its key stakeholders and wider constituents, and called for longer consultation timescales to be applied to IAs. There were also suggestions relating to the timing and sequence of IA consultations, including that informal consultation should begin before initial proposals are published. Conversely, some stakeholders supported shorter consultation periods for particular IAs (e.g. Code modification IAs).
- 1.12. *In relation to consultation, we have recently clarified our approach to consultation periods and stakeholders are now also able to plan their engagement using our consultations webpage.*

**Question 2: Our proposed approach to assessing impact, costs and benefits is to develop an iteration of options between three aspects. These are: monetised, aggregate cost-benefit analysis; distributional effects; and long-term, hard-to-monetise considerations. These assessments are informed by a consideration of our principal objective to protect consumers (existing and future) and our other statutory and EU duties, including considerations of competition (EU and domestic). Do you agree with our approach to assessing impacts? We welcome any views on this approach, and the specific content within each category.**




## Summary of responses: Consultation on changes to our Guidance on Impact Assessments

- 1.13. The majority of stakeholders agreed with the iteration of cost-benefit analysis with consideration of distributional effects and hard-to-monetise aspects, in order to arrive at a more robust set of regulatory policy options. However, some respondents called for greater detail in relation to our approach to CBA, including choice of discount rates.
- 1.14. *We have been more specific about our approach to CBA, including clarifying use of discount rates and time periods.*
- 1.15. In particular, suggestions were made regarding a more explicit recognition of interactions of impacts between projects (a 'whole system' approach) and requests for an explicit statement that quantification of impacts will always be attempted. Respondents also called for a consideration of the impact of options on investor confidence and the needs of new market entrants, and greater transparency in relation to underlying data and assumptions used in the IA process.
- 1.16. *We agree that, where possible, our approach to IA should incorporate consideration of 'whole system' impacts, including interaction effects (both positive and negative). To this end, we have also widened the scope of issues considered under distributional analysis (proportionate to the project in question).*
- 1.17. *We will also, where feasible and respecting commercial confidentiality, seek to engage with stakeholders over the underlying data/assumptions within our IAs.*
- 1.18. Stakeholders sought clarification over weightings applied during analysis, querying whether CBA was a decisive factor or whether distributional and sustainability issues could take precedence in some circumstances.
- 1.19. *Although we will make all efforts to quantify the likely costs and benefits of a proposal, there will still be important areas that are challenging to quantify and monetise, such as distributional effects and strategic and sustainability aspects. CBA is not determinative, and the IA is intended to present evidence for decision makers, with responsibility for decision-making ultimately resting with the Gas and Electricity Markets Authority.*
- 1.20. Many respondents supported the references to Real Options theory, but highlighted (as did the original consultation) the resource implications and data availability necessary to inform any such modelling.
- 1.21. *We have retained the reference to Real Options but wish to make clear that its use will be guided by the requirements of the project in question, and note that a more qualitative consideration of optionality can still provide important information.*

**Question 3: We have interpreted our duty to have regard to sustainable development by considering a mid-term stress and security assessment and a long-term natural asset and greenhouse gas assessment. For more detail on this approach, please see our recent discussion paper “Strengthening strategic and sustainability considerations in Ofgem decision making” (June 2012). Do you agree with our approach to considering long-term, complex and hard-to-monetise issues? We welcome any views on this approach.**

- 1.22. A number of respondents questioned the use of ‘long-term’ in relation to strategic and sustainability considerations, arguing that sustainability impacts can manifest in the short, medium and longer-term.
- 1.23. *We have amended the guidance accordingly, and now make clear that the distinction between ‘short-term’ and ‘long-term’ is not rigid, recognising that hard-to-monetise considerations (eg strategic and sustainability factors) can occur in all assessment periods.*
- 1.24. Several respondents also proposed that consideration of biodiversity impacts could be more effectively framed as consideration of impacts on ecosystem functioning, and therefore the maintenance or degradation thereof of the services supplied by the ecosystem.
- 1.25. *We have incorporated consideration of wider ecosystem functioning within the guidance, and this point also relates to consideration of ‘whole system’ impacts addressed in response to Question 2.*
- 1.26. Several respondents suggested we should avoid duplicating assessments already undertaken by competent authorities (such as Environment Agency permits).
- 1.27. *In the majority of cases we would concur with this approach and would adopt the assessment/conclusion of another regulatory body/competent authority. However, the type of environmental assessment we propose tends toward more of a complementary assessment (rather than a specific investigation into a particular environmental impact), which is designed to incorporate and build on existing assessments, and help to reveal previously-unforeseen impacts (such as might arise through cumulative effects, and/or through interaction effects of specific transmission or distribution assets with the natural environment). It is important to note that, although other regulatory bodies/competent authorities have specific environmental mandates, we also have obligations under our secondary duty and DECC’s Social and Environmental Guidance which we will seek to apply in a thorough yet proportionate manner.*
- 1.28. Several respondents identified key references / documents to help inform and support future Ofgem IAs. These included:
- UK National Ecosystem Services Assessment (NEA)
  - European Landscape Convention



## Summary of responses: Consultation on changes to our Guidance on Impact Assessments

- DECC/HMT Supplementary Guidance on Valuation of Energy Use and GHG Emissions.

1.29. *Where appropriate we have incorporated these suggestions into the annex of the guidance (which is intended to be regularly updated). In addition, we have also utilised many of the references as part of our internal implementation programme.*

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

1.30. A number of respondents requested greater clarity over the treatment of proposals with overlapping implications (GB, EU and devolved administrations).

1.31. *Where a proposal is likely to have European cross-border effects, we will assess it, in so far as it is in the interests of existing and future consumers, against the requirements of the Third Package (when carrying out our Third Package regulatory tasks). In addition, although Ofgem operates under GB legislation, we note that environment and climate change (for example) are important policy areas for the devolved administrations and we will continue to engage with them in developing our policy.*

1.32. Some respondents suggested that a panel of experts be established (as in DECC's Energy Market Reform process) to monitor and oversee the IA process, and there were also suggestions that we should institute an *ex post* evaluation of our IAs, in order to assess the degree to which actual impacts matched predicted impacts (or at least fell within an anticipated range).

1.33. *This proposal aligns with our internal thinking in relation to peer-review of Ofgem IAs. We have engaged an independent IA expert to review a sample of Ofgem IAs on an annual basis. Taken together with an internal peer-review process, these measures should help ensure that Ofgem continues to produce high quality IAs consistent with our guidance.*