



Energy for
generations

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CMA Interim Findings – ESB response

ESB welcomes the opportunity to comment on the CMA's Interim Findings report and the remedies contained therein.

We believe that the CMA has identified some of the key issues that were raised in parties' initial submissions and responses to the update on the theories of harm. These are topics that emerged in the course of industry feedback and featured more or less consistently in the Competition Review. The areas that the CMA has indicated as key failures are of critical importance to a well functioning retail market and should be addressed by improving the overarching industry arrangements.

ESB welcomes the CMA's intention to improve competition through the introduction of proposed remedies to the retail markets and we see the scope of these remedies to be appropriate. However, we are concerned that the CMA has mainly considered market failures in the retail markets and are disappointed with the lack of remedies proposed in the wholesale market and remain unconvinced it is functioning efficiently. As submitted in our previous representations to the CMA, we believe there remain particular features of the wholesale market that point to the need for further investigation.

On balance, we consider that remedies proposed by the CMA for the retail markets are broadly proportionate and could benefit consumers. However, it is our opinion that proposed remedies address immediate concerns in the retail sector whilst positive changes to the wider wholesale market could have delivered greater long-term benefits. In the following section we provide our comments on some of the key findings of the CMA and the proposed remedies that affect our immediate operations in the GB market. A brief summary of our comments can be found below:

- With regard to the CMA's findings on the absence of locational adjustments for transmission losses we support the CMA's analysis and conclusions and believe that the proposed remedy could help promote more effective competition in the generation and supply of electricity and would operate in the interest of existing and future consumers. We are pleased this is one of the areas under scrutiny with the CMA and will be happy to contribute further to the analysis.
- We are generally comfortable with the high-level objectives and the proposed principles of the remedies regarding regulatory decision-making and industry code governance. Clear and consistent regulatory arrangements are essential for a well-functioning market and we would welcome additional transparency and consistency in this area.
- On a more general note, whilst we agree with the immediate areas of concern, it is important that flexible approaches are taken so as to not pre-empt innovative services and solutions that may be delivered by, for example, smart metering which is due for mass roll-out from next year as well as the changes that on-going policies, both domestic and European, may bring in the near future.



ESB views on specific remedies

Locational pricing

We agree with the CMA's conclusion that the absence of locational adjustments for transmission losses could lead to instances of cross subsidisation that distort competition between generators. We believe that the benefit of charging cost-reflectively for transmission losses in GB would promote more effective competition in the generation and supply of electricity and would operate in the interest of existing and future consumers.

Potential benefits of such reforms have been evidenced by various CBAs undertaken as part of previous attempted reforms on this matter. In addition, the net benefit analysis within all of the modifications raised previously showed an overall positive net value.

Whilst there have been some concerns regarding the implications for generators in regions further from demand centres, we see sufficient protection in the market and proposed legislative arrangements to ensure that the market is fair and well-functioning. Furthermore, the introduction of the Transmission Constraint Licence Condition, which will be in force until at least 15 July 2017, into the generation standard licence conditions will provide adequate legal grounds for preventing any abuse of market power arising from the location of the generator.

For these reasons, we agree with the CMA's proposal to introduce new standard conditions to require that variable transmission losses are priced on the basis of location in order to achieve technical efficiency.

Impact Assessment for CfDs

We broadly support the CMA's view on this issue. We believe that the proposed remedy should lead to better transparency, market efficiency and deliver benefits to consumers. A clear and transparent allocation mechanism will ensure that CfDs that are allocated outside the auction mechanism are awarded only when the benefits of doing so demonstrably outweigh the costs.

Adding a robust and transparent framework to this area may have positive impacts on competition and could increase investments in new technologies. It could also allow for increased technological innovation and a more optimal balance between technologies and the overall benefits they can deliver.

Accounting Framework for energy generators and retail suppliers

We support a more transparent and consistent regime for financial reporting. Given the relevant findings leading to this remedy and the objectives it is trying to achieve, we believe the proposed remedy should apply to the firms that are currently under an obligation to provide Ofgem with Consolidated Segmental Statements. The remedy would guarantee there is consistency and clarity in the reporting formats, and would ensure clear separation between various segments of the business.



Regulation and Market Governance

We agree with the CMA's conclusion that occasionally Ofgem's role overlaps with DECC's role leading to sub-optimal decision-making and a lack of clarity about the underlying costs and benefits of various policies. We believe it is important to introduce clear separation and clarification of roles and objectives for DECC and Ofgem, and to communicate these to the wider industry. We also note that Ofgem's competition duty has been progressively downgraded relative to other duties and the rationale behind some of Ofgem's decisions in recent years has conflicted with promoting more effective competition in the various energy markets.

It is sensible to revise Ofgem's statutory objectives and duties in order to increase the emphasis on Ofgem's responsibility to promote competition as a primary objective. Having a more precise focus and being guided by clear objectives will assist Ofgem in regulating the market. While we are generally comfortable with the proposed recommendation, we await further information on how this will be implemented in practice, and whether the proposal allows for an appropriate level of protection for industry participants from any immediate policy changes and retrospective revision of Ofgem's decisions. Specifically, it could be argued that a change in Ofgem's statutory duties could cause a number of industry modifications to be raised simultaneously in order to revise decisions for previously determined modifications. Whilst some of these modifications could deliver some benefits to competition, industry is vulnerable to unforeseen policy changes (particularly those that are retrospective).

Overall, we agree that if the Energy Act allows changes to Ofgem's statutory objectives, the opportunity should be taken to do so.

In regards to Remedy 17, our view is that there should be consistency in the objectives and initiatives of Ofgem and DECC and they should co-operate to achieve the effective and efficient solutions for the industry and consumers. We therefore agree that it could be useful to have clear formal processes for Ofgem and DECC to discuss transparently a strategy for the implementation of DECC's policies. It would lead to the better co-ordination of planned policy changes, better consideration of competition aspects of the market and better overall assessment of impacts on the industry and consumers. As a general observation, it will be important for DECC to ensure that Ofgem interacts at the right level and at the right time with sufficient lead time for discussions and impact assessments.

The proposals in this area appear to be a sensible approach but it remains to be seen how they will work in practice. It would also be useful if whenever Ofgem's assessments differ from DECC's, any differences in views are explained. We would welcome clarity on which party's view prevails in the event of disagreement and what scope the other party has for getting the position reviewed. The process should be transparent and stakeholders should be informed of why a particular decision is being made.

We would also note that this approach would only work if Ofgem has a sufficiently independent status with clear objectives and statutory duties.

Code Governance and administration

Below, we provide views on the remedies presented by the CMA in this area. We would welcome, however, greater clarity on how each of the proposed remedies work (or not) together as it appears



some may not be compatible with others. For example we are unsure as to how remedies 18a, 18b and 18c could work together.

Remedy 18a

It seems that, fundamentally, the purpose of Remedy 18a is to bring consistency of governance and modification arrangements across codes and to promote a level playing field for all stakeholders in the delivery of modifications. We strongly support the objective of the proposed solution and its aim to introduce more efficiency in developing modifications to the codes. However, we are concerned that the unnecessary complexity of the proposal may not be fully justified given the limited potential effects it may have for industry and competition.

We are mindful that there have been several initiatives to promote better arrangements for code governance including CACOP and the Critical Friend requirements introduced under Ofgem's Code Governance Review. Whilst not fully implemented across all codes, some of these initiatives have demonstrated a positive change in code governance practices and modification processes. This has particularly been the case for the CUSC, which we believe is an effective model that should be adopted across all codes. Further alignment of prescribed principles of code governance can achieve the same effect with less burden on the industry.

Remedy 18b

With regards Remedy 18b, we broadly support Ofgem providing indicative timescales with key milestone dates to provide industry with a view of the expected progression for code changes. However, we believe these should remain purely indicative. If enforced timescales were introduced there is a real danger that they would drive incomplete analysis and hurried decisions, resulting in sub-optimal outcomes.

While indicative timescales can often be useful, Ofgem could also contribute to the efficiency of the process by providing more detailed views or early indications of its interim position, where appropriate and possible. This would provide better direction to modification groups and increase the likelihood of the process focusing on the necessary analysis. Consequently, we envisage this delivering more streamlined and efficient development and decision-making processes.

At this stage there is limited clarity on how the proposed process would work. As such, the industry is unable to test the proposals further. However, we strongly believe that Ofgem should not have powers to raise modifications. We have previously identified concerns that such a power may put into question Ofgem's impartiality in the decision-making process for modifications it has raised and developed itself and we believe that this question remains pertinent.

Remedy 18c

We accept that in the event of disagreement there could be a viable role for an independent code adjudicator with appropriate powers to resolve disagreements between parties over code changes. However, a key concern is the additional complexity that could be created for the overall process. Our understanding is that it will require giving powers equal to Ofgem's to another independent body. This has a potential to undermine Ofgem's role and decision-making powers and create duplication of efforts. While well-intended this may lead to additional costs and an extended timeline for code change implementation.