

**Corporate Response Form 'Ofgem Licence Modification Appeals' Consultation**  
**URN 10D/807 Open: 01/10/2010 Close: 29/10/2010**

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**Consultation Questions**

**What should be the scope of the appeal mechanism?**

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| <b>1</b> | <b>Does the fundamental nature of price controls require they be subject to different treatment from other licence modifications? Please explain what changes you consider are required, why you consider they are required and how they would be compatible with the Third Package.</b> |
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Whilst not advocating change to the existing licence modification process, we do recognise that changes to special licence conditions relating to price controls are currently handled differently to the standard licence condition modification process. This difference reflects the significance and uniqueness of the fundamental decisions in respect of price controls for each individual network company. We therefore consider it appropriate that price control licence conditions are subject to different treatment from other licence modifications given the complex economic nature of price control reviews. We also note that price control reviews typically result in an integrated package of modifications to both standard and special conditions. It would clearly not be appropriate for different appeal mechanisms to apply to parts of such a package.

As set out in the covering letter, we do not believe the existing arrangements are incompatible with the requirements of the Third Package. We therefore believe that individual network licensees should be able to refuse regulatory price control proposals and have the issue referred to the Competition Commission for a full in-depth investigation and determination.

## What should be the structure of the appeal?

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| <b>2</b> | <b>Do you agree that a rehearing approach to appeals for modifications other than price controls strikes the right balance between appropriate economic scrutiny of the regulator's decisions and a timely appeals process that controls potential costs for the parties?</b> |
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It is vital that any appeal mechanism allows for an appeal on the merits of the case and not simply one that looks at process or factual errors. In addition, the process should be one that is efficient, timely and cost effective with a view to reducing any potential increase in regulatory uncertainty. We consider a rehearing approach would appear to best meet these objectives compared to the other possible options.

However, this approach would be very similar to that which was adopted for the industry code appeals mechanism. One of the concerns of this process is that it requires potential appellants to incur front loaded legal costs in anticipation of the likely regulatory decision. This is because a rehearing is one where the arguments presented to the regulator at the time of its decision are reconsidered and no new evidence is generally accepted. Consequently, potential appellants are required to incur significant legal costs in advance in order to ensure that all the evidence and legal arguments are presented. This could arguably be a barrier for parties to raise valid appeals, particularly for small players. Consideration is therefore needed to ensure the balance is right between avoiding parties withholding relevant information or presenting new arguments and analysis and that of avoiding the need for parties to incur significant cost up front.

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| <b>3</b> | <b>Do you agree there should be a full investigative hearing for price controls?</b> |
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See question 1.

The current mechanism puts significant pressure on the regulator to properly consider the merits of any proposed change before subjecting it to the collective voting process, or individual consent in the case of special licence conditions. Under DECC's proposals, this incentive on the regulator would be significantly weakened unless the right of appeal truly allowed a merits appeal. We are therefore concerned that the proposed constraints set out in p2.10 of the consultation are overly narrow, and in fact resemble more the narrow grounds for judicial review under the current arrangements (an approach which falls well short of a merits approach).

Ofgem's statutory duties are framed in a way which permits a wide range of outcomes which, nonetheless, may inappropriately damage the interests of an affected party. An appeal on the merits should be about finding the best solution

given the circumstances, not just one which fits within the broad remit of Ofgem's duties.

DECCs proposals would represent a significant and damaging change unless it truly allowed merits appeals.

## Grounds for appeal

### 4 Do you agree with our proposal for an appeal on the merits?

As set out in our response to question 2 and 3, we consider any proposed appeal mechanism must involve an appeal on the merits. We see no reason why at the very least the mechanism should not be similar to that implemented for the industry codes.

### 5 Would our proposed grounds allow for consideration of legitimate legal, factual and economic issues, without undermining regulator independence? If not, please state why.

No. Whatever the appeal process, regulators should be able to objectively justify their decisions. An independence that permits unjustifiable decisions is not worth having.

## What who are the affected parties who should have right of appeal?

### 6 Do you see any case for extending the right of appeal in relation to an Ofgem decision to any licensees or other materially affected parties beyond directly affected licensees? Please explain which and why.

On balance we believe there are merits in allowing materially affected 3<sup>rd</sup> parties the ability to appeal licence modification decisions. There are many occasions whereby changes to network licences have a significant commercial knock on effect to users of transmission and distribution networks. Consequently, allowing such affected parties the right to challenge such decisions would introduce greater transparency and accountability to the licence modification process.

## The appeal body

7	<b>Do you agree the CC is the most appropriate appeal body? Why/ why not?</b>
Yes. We see no reason to change the appropriate appeal body from that which is used now for modification references and industry code appeals. Because appeals are likely to involve complex economic issues we believe the Competition Commission is the only body with the appropriate relevant expertise and resource.	
<b>Outcome</b>	
8	<b>The Government would welcome views on whether the appeal body should have the power to vary Ofgem's decisions on matters, other than price controls, or whether such cases would be better handled by remitting decisions back to Ofgem to re-take, with any necessary binding recommendations.</b>
We support the Government's minded to approach whereby the appeal body will have the power to confirm or quash a decision, remit the matter back to the regulator, and give specific recommendations. However, there is danger that if the appeal body is given to wide a power, they in effect become the regulator. In addition, we believe the regulator is best placed to actually draft licence conditions. However, we do believe that where matters are referred back to the regulator with recommendations the appeal body should have a right of veto on any revised proposals in order to ensure that their recommendations have been interpreted and implemented appropriately. To do otherwise may lead to further appeals which would be timely, costly and involve further regulatory risk.	
<b>Time Limits for the process</b>	
9	<b>Do you think the Government's suggested timescales of 4 weeks to lodge an appeal, and a period of 4 months for the hearing of most appeals will ensure appropriate scrutiny and efficient decision making?</b>
A standard period of four months for the hearing of the majority of appeals would appear to allow for appropriate scrutiny of the potential appeals envisaged. We note that the Competition Commission appear comfortable with such a timeframe. However, we do believe there to be merit in providing the appeal body some flexibility in the setting of the appeal timetable. As indicated there may be circumstances where a shorter or longer period is justified. However, where the standard timetable is amended this should be accompanied with a robust and sound justification,	

particularly in circumstances where the timetable is shortened.

As drafted we oppose the suggested timescale for lodging an appeal of four weeks. In the consultation document comparisons are made with the current four week period for raising objections. However, lodging an appeal and raising objections are two distinctly separate activities that involve different amounts of resource, cost and time. Objecting to a licence modification proposal involves a simple notification of a formal statutory objection, whereas lodging an appeal involves significant resource as formal legal documentation is required to be served by the parties including permission applications and statements of case. This process can be timely and the proposed four week period could be particularly onerous for small players. We therefore propose that changes are made to this timeframe. One option would be to extend the four week period, however, this leads to an extension of the period of regulatory uncertainty. Alternatively, a period could be provided for formal notification of an appeal by a party of say two weeks with a further four weeks provided for the serving of the relevant legal documentation. This provides an appropriate balance between allowing valid appeals to be raised in an efficient and cost effective manner and keeping to a minimum the period of regulatory uncertainty.

<b>10</b>	<b>Do you see any circumstances in which an appeal may need to be subject to a faster timeline. If so can you provide examples?</b>
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At this stage we don't foresee any particular types of modifications that may require appeals to be progressed within shorter timeframes. However, as set in our answer to question 9, we believe there may be merit in allowing the appeal body flexibility in setting the timetable provided robust justification is presented.

### **Can Ofgem's decisions be suspended?**

<b>11</b>	<b>Do you agree the appeal body should be given the discretion to suspend Ofgem's decisions on application if they could lead to significant and potentially unnecessary expense and/or disclosure of confidential information?</b>
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Yes. We believe appellants should be provided with the ability to seek, from the appeal body, the suspension of a licence modification decision from the regulator. In exercising its discretion on suspension, the appeal body will need to consider a number of issues including whether there is a risk that a particular party or class of parties will be materially affected by the implementation of the proposals or unnecessary expenditure would be incurred on for example IT system changes and/or the disclosure of confidential information. Ideally, suspension of the appealed decision should be automatic unless there are clear security of supply implications.

### **How will the costs be recovered?**

<b>12</b>	<b>What will be the likely costs and benefits of these changes on your organisation?</b>
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Costs of appeals can be substantial and arguably can deter parties from raising valid appeals. Under the current licence modification regime there is a tendency for a proportion of the costs of the appeal body to be smeared across the class of licence holders directly affected by the appeal decision. It is unclear at this stage what the arrangements will be for the recovery of the costs of the appeal body and the regulator under these proposed arrangements. There is a risk that parties could potentially face significant uncertainty and costs dependent on the options available. There is clearly a need for transparency in the cost recovery method in order for parties to appreciate their potential cost exposure in the event of raising an appeal. We also believe that some form of cap should be applied so that, for example, the regulator is not able to incur significant and excessive legal costs that may need to be recovered from appellants in the event that the regulator is successful. We believe that only "reasonable" costs should be capable of being recovered from other parties to an appeal.

Notwithstanding the above, we believe that the changes generally will lead to additional costs being faced by licence holders given that ultimately their only recourse to challenge is at the end of the process and through a statutory legal route. The current arrangements contain robust accountability provisions that incentivise the regulator to effectively engage with the industry much earlier in the process leading to more optimal solutions being efficiently developed without the need for a formal challenge.

<b>13</b>	<b>How do you recommend potential costs could be reduced? How could we maximise the potential benefits to the regulatory regime as a whole?</b>
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See above.

