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ENERGY RETAIL Association

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Energy Retail Association Response to "Ofgem Licence Modification Appeals" consultation

The Energy Retail Association (ERA) welcomes this opportunity to comment on the proposed reforms to the licence modification appeals process as part of the broader consultation on the EU Third Energy Package.

The Association of Electricity Producers (AEP) has led the industry response to this consultation and the ERA supports the more detailed comments on the proposals made in their response.

In line with the AEP response, we do not support DECC's proposals to change the existing licence modification process. It is clear that DECC's proposals go far beyond the scope of the Third Package, and are therefore not suitably enacted through secondary legislation under the European Communities Act.

In its impact assessment DECC provides three reasons for proposing these fundamental changes to the existing arrangements:

I. The regulator must have powers enabling it to perform regulatory tasks in an efficient and expeditious manner
II. A suitable right of appeal must be available to all parties affected by a decision of the regulator
III. The regulator must be able to implement binding decisions

With regard to the first reason, the requirement for the regulator to have powers to perform tasks in an efficient and expeditious manner was also a feature of the 2003 Second Package. Given that the UK is deemed to have effectively implemented that set of legislation the existing process already complies with this requirement meaning that no change is necessary.

With regard to the second reason, the existing arrangements strike the appropriate balance in terms of appeal rights. Directly-affected licencees have the right to have a decision

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referred to the Competition Commission, while indirectly-affected licencees - or any other affected party - have the right to mount a Judicial Review.

While DECC consider that a Judicial Review may not be a suitable right of appeal for indirectly-affected parties, European case law defines a "suitable right of appeal" as Judicial Review. Moreover, the procedure and remedies of British Judicial Review would comply with the requirement for appeal as outlined in the Commission's interpretive note on regulatory authorities.[1]

With regard to the third reason, although DECC suggest that the regulator must be able to implement binding decisions, the Directives actually state that the regulator must be able to *issue* binding decisions.

The existing arrangements do not prevent the regulator from issuing binding decisions but instead allow for additional independent scrutiny by way of a Competition Commission reference, prior to implementation of the decision if licensees express an objection. In this case, issuing and implementation are two distinct actions and it is entirely appropriate that any appeals are heard after the issuing of the decision but prior to implementation of the decision, as is provided for in the existing arrangements.

In light of these considerations, it is clear that the three reasons DECC cites for changing the existing arrangements fail to justify an alteration to the existing framework.

While we do not accept that the proposals are necessary, we would like to comment on particular aspects of the proposed reforms from suppliers' perspective:

1. The current arrangements have been flexible, and have generally struck a good balance between the regulator's independence and a constructive relationship with the regulated energy companies which has minimised expensive and legalistic appeals.

2. The proposed reforms would result in a significant shift in power in the licence modification process to Ofgem. This could lead to Ofgem having broader scope to impose regulations on the industry which have not fully taken into account industry views or impacts on customers or competition. This less consensual approach to licence modification may lead to poorer quality licence modifications, more appeals and increased investor uncertainty. A proliferation of appeals would be both time consuming and costly for the industry, the regulator, and ultimately the consumer.

3. The new balance in decision making, coupled with Ofgem's broad statutory remit, could result in Ofgem adopting a policy-making role in establishing regulation that is more appropriately performed by the legislative branch of government. This was not the intention of the underlying Gas and Electricity Directives in the Third Package.

4. The proposed "loser pays" principle for costs arising from Competition Commission hearings could present a significant deterrent to appeals. In its

[1] *European Commission,* Interpretive Note on Directive 2009/72/EC Concerning Common Rules for the Internal Market in Electricity and Directive 2009/73 Concerning Common Rules for the Internal Market in Natural Gas; "The Regulatory Authorities", *22nd January 2010*

impact assessment the DECC estimation of likely Ofgem costs is £600,000. This seems grossly disproportionate to the estimated costs to the appellant of £175,000. It will be important that provisions are made for award only of reasonable costs; £600,000 in costs for Ofgem per appeal would not appear to be reasonable.

5. "Materially affected parties" should be able to appeal non-pricing licence modifications not directly affecting them. For example, suppliers or generators should be entitled to appeal modifications to transmission or distribution licences that have an impact on their business. It will be important, however, that the term "materially affected" is well defined, and that the appeals permission process is properly designed in order to ensure that the litigation floodgates are not opened to unnecessary, trivial, or vexatious appeals.

6. The cost of making system adjustments in response to licence modifications that may then be subject to further costly reversals or alterations in the event of a successful appeal, require the lodging of any appeal to have a suspensory effect on the related licence modification.

We support a strong and independent regulator. However, if DECC choose to implement these unnecessary proposals, the regulator would be given greatly enhanced powers which were not envisaged by the Third Package and go far beyond its scope. The regulator would be able to unilaterally issue and implement changes impacting the core of the licencee's business without there being sufficient checks and balances in place.

This would force the licensee along only one route to recourse – an expensive and onerous ex-post appeal to the Competition Commission. This seems fundamentally inappropriate as policy ought to seek to minimise rather than increase litigation.

The ability of the regulator to make policy decisions and "move the goalposts" as they see fit, is certain to damage investor confidence in the UK energy sector.

We would urge DECC to reconsider the consequences of their proposals and adopt a minimum-change approach to implementation.

This issue is very important to our members and we would welcome the opportunity for further discussion. For more detailed, technical input on the design of the appeals process we would like to refer DECC to the AEP submission.