

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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| 1 | 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. |
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AEP accepts that price controls represent a distinct type of licence condition in that they set the economic framework for network businesses and incorporate a broad package of measures. Other licence conditions, while they may have a major economic impact, will almost always be more limited in scope. AEP therefore acknowledges that a more detailed investigation and longer timescales will be needed for price controls appeals.

What should be the structure of the appeal?

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| 2 | 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? |
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AEP believes that a rehearing is the right approach for dealing with appeals on licence modifications (other than price controls). The appeal body should be able to review the economic and technical arguments deployed so far in the process and reach an independent decision on them.

In general, market players will have made their main arguments during the consultative process with a view to influencing the regulator's decision. However, there should be scope for introducing new evidence if, for instance, circumstances have changed significantly since the original Ofgem proposals were made.

If new evidence cannot be introduced, this will tend to make the consultation phase more legalistic and onerous for all parties, as companies will have to ensure a more comprehensive legal input at this stage.

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| 3 | Do you agree there should be a full investigative hearing for price controls? |
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AEP agrees that there should be a full investigative hearing for price controls.

Grounds for appeal

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

AEP regards it as essential that any mechanism should allow an appeal on the merits of the case and not simply on process or factual issues. Complete reconsideration of the decision should be permitted.

While the 2004 Energy Act code modification appeals process in some ways provides a good model, AEP believes that the appeal body should be able to take into account public interest grounds, as is currently the case in Competition Commission inquiries.

The Energy Act process allows Ofgem to exclude appeals on security of supply grounds. In AEP's view, as Ofgem is being given increased powers to amend licences, it should not also be able to reject appeals against such decisions. This would be tantamount to acting as judge and jury. Decisions on the admissibility of appeals should be left to the Competition Commission.

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

AEP agrees with the grounds for appeal set out in para 2.10 but believes that these need to be augmented. In particular, the appeal body should be able to take into account the wider public interest, as mentioned above. In some other respects the appeal grounds proposed appear to be narrower than those of the 2004 Act, though this may be because the full legal drafting is not provided. We would welcome clarification on this point.

The Third Package provides for a right of appeal against regulatory decisions (e.g. Electricity Directive Art. 37.17). We do not see any way in which such an appeal mechanism could undermine the regulator's independence. Any regime containing no checks on the regulator's ability to act would not meet the principles of better regulation, in particular regulatory accountability and proportionality.

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

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| 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. |
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Leaving aside the issue of price controls, AEP believes that materially affected licensees should have a right of appeal on licence changes. This is particularly the case in relation to the Transmission Licence, where changes which have a substantial impact on electricity generators can now be imposed by Ofgem at the end of the Significant Code Review process. The changes in question may be acceptable for the network business affected, which would therefore not appeal, but might have a substantial adverse impact on generators or suppliers. Network users should therefore in our view have a right of appeal in such a case.

AEP accepts that materially affected licensees would have to demonstrate their standing to the appeal body and acknowledges that the latter should have the ability to reject vexatious or trivial appeals.

The appeal body

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| 7 | Do you agree the CC is the most appropriate appeal body? Why/ why not? |
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As economic issues would need to be considered in depth, AEP agrees that the Competition Commission should be the appeal body.

Outcome	
8	<p>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.</p> <p>AEP agrees that the appeal body should have the ability to confirm or quash Ofgem decisions and to issue binding recommendations to Ofgem. We accept that the appeal body may not be best placed to undertake the detailed drafting of licence conditions and that this task should therefore be remitted to Ofgem. However, this must not provide a route for the regulator to refuse to implement a decision of the appeal body. The appeal body should therefore have the power to reject the revised drafting.</p>
Time Limits for the process	
9	<p>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?</p> <p>AEP believes that the suggested period of four weeks for lodging an appeal is insufficient. This timescale would mean that licensees would have to do preparatory work on the appeal before the regulator's decision had been made. This would be a particular obstacle for smaller players without in-house legal staff.</p> <p>A four-week period would be consistent with the current timescale for raising objections to a licence change, but this is not a valid comparison, as the current process does not require extensive legal input. AEP would regard two months as a more appropriate timescale.</p> <p>Four months appears to be a reasonable period for most appeals to be heard. However, as suggested in the consultation document, there should be some flexibility for more complex cases. One example could be proposals to regulate conduct in the wholesale market, e.g. the case of MALC. We believe that the</p>

appeal body should have the discretion to lengthen the timescale if necessary.

In general, AEP would like to see elements of the timetable clarified. In particular, we assume that the appeal body would be given a period of two weeks to accept or reject the appeal, and that the four months would run from the time this decision is taken.

10	Do you see any circumstances in which an appeal may need to be subject to a faster timeline? If so can you provide examples?
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AEP regards these timescales as already very short and notes that, if the appeal process is compressed too much, this could result in bad decision-making, which will ultimately be more costly.

EU Guidelines and Network Codes will need to be implemented in the UK, usually by a specific deadline set out in the legislation. This could in theory be shorter than the decision-making and appeal timescales set out in DECC's document. However, the UK has a well-established process for making detailed rule changes via licences and industry codes and should encounter fewer problems in this area than most other Member States. AEP would emphasise the need for the Commission and ACER to set reasonable timescales for the implementation of EU legislation and decisions. If this is done, faster timelines should not be required.

Can Ofgem's decisions be suspended?

11	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?
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AEP agrees that the appeal body should have discretion to suspend the regulator's decision. Ideally, suspension of the appealed decision should be automatic unless there are clear security of supply implications. Many licence and industry code changes require expenditure on IT systems or software, and an appeal could become pointless once the expenditure has been incurred.

How will the costs be recovered?

12 What will be the likely costs and benefits of these changes on your organisation?

AEP as a trade association is unlikely to incur costs as a result of these proposals. We would, however, like to emphasise the extent to which legal costs are a barrier to appeals, particularly from smaller players. Apart from having to meet their own legal costs (and £175k is a substantial amount), appellants if they lose could potentially have to bear Ofgem's costs as well. This represents a major asymmetry, as Ofgem is able to recoup legal costs without difficulty via licence fees. DECC's own estimates show Ofgem's legal costs (excluding in-house costs) are more than three times greater than those of a typical company appealing. We understand that in the recent past at least one small player has abandoned an appeal because of the risk that it might have to bear Ofgem's costs.

AEP therefore agrees that the appeal body should be able to award costs on either side of an appeal. The level of legal costs incurred by the two sides should be one of the factors considered in this decision.

13 How do you recommend potential costs could be reduced? How could we maximise the potential benefits to the regulatory regime as a whole?

The proposed changes are likely to increase the regulatory costs imposed on electricity and gas businesses and these could be significant. However, our major concern is that allowing the regulator to change licences more readily will increase risk in the GB market and damage investor confidence. This seems to run counter to the UK Government's efforts to reduce regulatory risk and, at a time when huge investment is needed throughout the electricity chain, could be extremely costly. AEP therefore thinks it crucial that the Government should set clear boundaries to Ofgem's ability to amend licences.

Impact Assessment Questions

These are partial Impact Assessments containing our initial qualitative assessment of the costs and benefits. We therefore would welcome any quantitative evidence to support the further development of these impact assessments. Any information provided will be treated with sensitivity and anonymity.

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| 14 | Are the assumptions made in the Impact Assessment correct and have we correctly identified the costs and benefits associated with this measure? The Government would welcome any information that could improve our analysis of the costs and benefits highlighted in the Impact Assessment. |
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15	What would be the likely costs and benefits of the 'minimum implementation option' of having two parallel separate regimes; one for those relating to regulatory tasks and Third Package duties, and one for Ofgem's domestic tasks? How would these compare to the costs and benefits of the proposed implementation option?

Additional Comments