Consultation on the amendment of the Nuclear Waste and Decommissioning (Finance and Fees) Regulations 2011

Responses to the Consultation

In total eight written responses were received. The respondents to the consultation, listed in alphabetical order, were:

- EDF Energy;
- Dr Bahram Ghiassee;
- Horizon Nuclear Power Limited;
- Institute and Faculty of Actuaries;
- Nuclear Decommissioning Fund Company Limited;
- Nuclear Institute
- Nugeneration Limited;
- Scottish Environment Protection Agency.

EDF ENERGY

Question 1: Reporting requirements

Do the changes in relation to the reporting requirements strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

EDF Energy believes that it would be more effective to deal with the reporting requirements within the appropriate context of the terms of the approved FDP, rather than through regulations. However, our comments below are intended to address the most significant issues.

Financial year end and timescales
EDF Energy welcomes the practical improvements that have been made to the way in which the reporting requirements are dealt with in the consultation regulations. In particular, we welcome the alignment of annual and quinquennial reviews with the Operator's financial year end, and also the more realistic timescales.

However, EDF Energy remains concerned that there may still be circumstances, envisaged in an Operator's FDP, where it will not be possible to produce an annual or quinquennial report to the defined timescales. A particular example of this is where the reason for a delay is due to a dispute between the Operator/fund company/verifiers which is being resolved in accordance with the provisions of an FDP. We propose that the details of any such allowable extensions/suspensions would best be dealt with in the approved terms of the FDP.

Prescription of timings in respect of annual and quinquennial reviews
EDF Energy considers that the proposal to prescribe the timings of quinquennial reviews, pursuant to regulation, is unduly restrictive. We consider that there are benefits to both the Secretary of State and to the Operator in allowing the flexibility to propose FDPs which, in certain circumstances, depart from the standard timetables for the production of reports.

For example, it would be sensible to allow flexibility in order to synchronise a quinquennial review with the introduction of a new power station to the fleet, to reflect a major operational change, or to align with Secretary of State requirements for the Waste Transfer Contract quinquennial reviews and other key milestones. EDF Energy considers that this kind of flexibility would improve the quality/relevance and cost effectiveness of quinquennial reviews. The regulations could address this point by referring back to the approved terms of the FDP.

Reporting arrangements before first criticality
EDF Energy believes that it is unnecessary for there to be an annual review in the period between the approval of a FDP and first criticality. Such reviews would have material costs for Operators. In our view, there would be no benefit in this as no contributions are made into the fund during such a period, and no material Designated Technical Matters (DTM) cost liabilities will have been incurred.

Similarly, EDF Energy would suggest that it is sensible for any quinquennial review in this period to be carried out to reflect the "as built" status of the plant prior to first criticality. This would ensure that all the necessary work to undertake the review would be carried out once. All relevant and up to date technical information on the 'as built' plant could be used and assessments could be made on the basis of expected rates of return close to the time that the first contributions to the fund were to be made. Again, such flexibility could be maintained in the regulations by referring back to the approved terms of the FDP.

Question 2: Verification of an FDP

Do the changes in relation to the verification of an FDP strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities? To what extent is the standardisation approach desirable and/or achievable?

Standard of Verification

EDF Energy considers that any FDP verification regime should have the following characteristics:

a) The standard for verification should be clear, objective and enduring.
b) It should be clear what aspects of the FDP are actually being verified.
c) The verification standard should be realistic – it must be possible to find a verifier who will be able to give the required opinion.

EDF Energy welcomes the recognition by the Government that the requirement, for the verifier to form a view on prudence, in the previous version of the regulations, was problematic. "Prudence" is an undefined term and its use as a verification test would introduce uncertainty for both the operator and the verifier.

Unfortunately the consultation regulations do not completely address this problem. The verifier needs an objective test to verify against, and should not be required to make a judgement over what is "prudent".

EDF Energy believes that the closest that one can get to a definition of "prudence", in the context of the FDP, is the initial approval of the FDP arrangements by the Secretary of State. By definition, the Secretary of State may only approve an FDP if it meets the Statutory Objective i.e. that the operator is making prudent provision. Therefore, an approved FDP represents prudent provision. This is recognised in the consultation text attached to the proposed regulations, but is not reflected in the drafting of the regulations themselves.

EDF Energy considers that the most effective approach to verification would be to deal with it within the more appropriate context of the terms of the approved FDP and not have anything in regulations about the matter. However, a simple reference in the regulations stating that the Secretary of State may rely on independent expert verification in accordance with the approved terms of an FDP could also be workable.

Clarity on what is being verified
The draft regulations are helpful as they are clear on the scope of the technical verification, based on the DTM cost estimates. However, in relation to financial verification, it is unclear what the subject matter of the verification is i.e. what is meant by "financing of the DTM costs" and "changes to the financing of the DTM costs"? The terms are undefined in the regulations, and any attempt to do so would risk developing a definition that could be contrary to the structure and operation of an Operator's FDP.

Again EDF Energy considers that a reference back to the scope of financial verification as set out in the approved terms of an FDP would address the issue and be workable. It would allow the Secretary of State to more closely tailor the scope of financial verification so that it was appropriate to the detailed form of the Operator's FDP arrangements, rather than attempting to rely on an ambiguous definition of scope set out in regulations that would need to cover all Operators' FDPs. For this reason, we are sceptical of the value of a standardised approach to verification as discussed in the consultation document. This would only work if all Operators' FDPs were the same. However, the Government has already made it clear that it does not wish to be prescriptive about the form or arrangements within an Operator's FDP.

EDF Energy considers that without explicit reference in the regulations to objective verification tests within the FDP there is a serious risk that it will not be practically possible for operators or funds to instruct verifiers.

Question 3: Modifications

Do the changes in relation to the modifications regime strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

Definition of a modification
EDF Energy considers that matters that would be considered a "modification" to the approved FDP under the Energy Act 2008 (rather than the ordinary operation of the FDP through application of its provisions) could benefit from greater clarity.

Based on our interpretation of the law, the only things that constitute modifications under the Act (and therefore may come under the ambit of an exclusion regime) are (i) changes to how the FDP is operated (i.e. changes to the actual terms of the FDP) and (ii) changes to cost estimates and associated changes to the Decommissioning and Waste Management Plan (i.e. due to inflation and to real increases and decreases in the underlying costs). Matters arising from the operation of the FDP in accordance with its terms would not constitute a "modification" to the FDP. These would include, for example the calculation of the contributions required in each year according to the provisions of the FDP.

For example, if the terms of an approved FDP contained a formula for calculating contributions payable by the Operator in response to changes in DTM costs, fund value and financial assumptions, then any changes to contributions as a result of

applying that formula would simply be the operation of the approved terms of the FDP, and not a modification.

However, if the Operator wanted to amend the formula in the approved FDP, then clearly this could only be done via a modification proposal which would require the approval of the Secretary of State. EDF Energy considers that the above is the case as a matter of law. In order to provide the greatest degree of certainty, we would propose that the regulations should make this explicit by excluding such changes, for the avoidance of doubt, from the requirement for the Secretary of State's approval without further complicating the regulations.

Exemptions to Secretary of State Approval for modifications
EDF Energy welcomes the wording in Regulation 10 (1) A, which gives the Secretary of State the ability to define, by reference to an approved FDP, which modifications will require the consent of the Secretary of State. This approach allows flexibility to both the Secretary of State and the Operator to tailor the Secretary of State's oversight role to the particular detailed circumstances of the Operator's FDP. We would propose that the regulation should refer to the exemption of modifications "of a description" set out in the approved FDP.

We note the proposal to exempt modifications to the DTM costs from approval if the changes are less than 5%. However, it remains unclear whether this figure is a nominal or inflation adjusted figure. It is EDF Energy's strong view that this should be an inflation adjusted figure, otherwise modifications requiring approval would be triggered purely by high rates of inflation. We note in the consultation language that this is DECC's intention but the regulations should make this explicit.

Modifications arising from proposed changes to the DTM costs
Proposed Regulation 11 would currently allow upwards amendments to cost estimate, provided that the security provided in accordance with the FDP is equal to the value of the revised liabilities calculated in accordance with the FDP. However, we note that there is currently no definition of security in the regulations. This is another area where the intent of the regulations is unhelpfully ambiguous and subject to a range of interpretations. There are two ways in which this could be remedied. One would be to use Regulation 10(1) (a) to exempt such cost changes within the FDP and define security within the FDP. The other would be for the regulations to explicitly define security as being in accordance with the approved terms of an FDP.

We note in Regulation 11 (4)(a) that a downwards amendment to costs does not require the Secretary of State's approval if it corresponds to a reduction in the fee for the disposal of waste arising under the Waste Transfer Contract. This is helpful as far as it goes, but EDF Energy believes that the exemption should be extended to cover the post decommissioning waste management costs which are also ultimately determined under the Waste Transfer Contract with the Government. We find it anomalous that a cost arising out of a contract with the Secretary of State should also be subject to a requirement for further approval by the same Secretary of State. We do not believe that this is in the spirit of simplifying regulations to reduce the administrative burden on industry."

DR BAHRAM GHIASSEE

Question 1: Reporting requirements

Do the changes in relation to the reporting requirements strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

The alignment of the reporting timeframes for (i) Funded Decommissioning Programme (FDP) and (ii) annual financial reports may be regarded as logical, and a positive step in reducing regulatory burden and costs to the operator, and in increasing public confidence in the reporting process, in general.

Equally, The proposed amendments to the 'Reporting' requirements in relation to both the Annual Report and the Quinquennial Report are welcome. It is most likely that the proposed amendments would result in improvement in the quality of the said reports, and enhancement of public confidence in the process.

Question 2: Verification of an FDP

Do the changes in relation to the verification of an FDP strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities? To what extent is the standardisation approach desirable and/or achievable?

By and large, the proposed amendments to verification of an FDP strike the right balance. However, in my view, the term 'prudence' is rather vague. Hence, the decision of the Secretary of State, in approving an FDP, might be legally challenged in the High Court.

In view of the similarity of reactor technologies to be adopted in England & Wales, standardisation would be beneficial to the Operator, the Verifier, the Secretary of State, and the public. However, the onus would be on the relevant Departments (eg, DECC & DEFRA) and Statutory-based Regulators (eg, EA & ONR), and, perhaps, input from OECD-NEA to draft the requisite blueprint.

Question 3: Modifications

Do the changes in relation to the modifications regime strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

Yes, the proposed amendments do strike the right balance. The regulatory & financial burden on the operator would be reduced, without affecting public confidence in the process. It is, indeed, reassuring to note that there shall be "sufficient financial security to meet the revised liabilities" for "modifications that increase estimated costs by more than the 5% materiality threshold.

HORIZON NUCLEAR POWER LIMITED

Question 1: Reporting requirements

Do the changes in relation to the reporting requirements strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

The Government proposal at paragraph 1.8 ("…to require the operator to synchronise the FD reporting year with its own financial year") is sensible and welcome. However, the proposed regulations do not achieve this aim, as public companies have 9 months after the end of the financial year to file their accounts and the regulations only allow 6 months for annual reports.[1]

It is not clear what additional benefit the Secretary of State would receive from requiring the annual reports to be submitted on a quicker timescale than quinquennial reports, and therefore simply having one reporting deadline for reports, either annual or quinquennial, would seem sensible.

Reporting prior to operation

There should be a separate reporting requirement in the period after first approval of the operator's FDP and before start of operation (i.e. during construction of the plant). It should not be necessary to produce quinquennial (or major) reports during this period. Any additional reporting that was required could be proposed and agreed by the Secretary of State through an operator's FDP.

Major reports

We believe that, particularly for quinquennial reports, the Secretary of State would be better served by providing time limits for the period that the report must cover. So rather than referring to quinquennial reports, an operator should have to produce a major report *within* five years of the previous major report. This would mean that the Secretary of State would receive reports no less frequently than the proposed regulations would require, but would allow the operator to better coincide major reports with activities at the station. Clearly an annual report would not be required in the year when a major report was produced.

The recently published draft Energy Bill (clause 43(1) and 43(2)) contains a similar structure which may provide useful drafting.

Regulation drafting

The reporting regulations have become confused and are very difficult to follow. Rather than attempting to revise the regulations piecemeal they may benefit from redrafting. For example, the structure could be as follows:

i. The site operator must make a report each year to the Secretary of State within 9 months of the end of the period it relates to.

[1] See section 442(2) of the Companies Act 2006, http://www.legislation.gov.uk/ukpga/2006/46/section/442

ii. That report can be a major report, and must be a major report if it is five years since the last major report. If the report is not a major report, it is considered to be an annual report.
iii. [Requirements of an annual report]
iv. [Requirement of a major report].

Extension to reporting timescales

It is not clear what the reporting process would be if there were disputes between, for example, the Operator and the independent fund, or the operator and the verification body. There are no provisions allowing an extension to be agreed should it be required and acceptable to the Secretary of State. A provision similar to that found at s442(5) in the Companies Act 2006 might be appropriate for inclusion.

'If for any special reason the Secretary of State thinks fit he may, on an application made before the expiry of the period otherwise allowed, by notice in writing to a company extend that period by such further period as may be specified in the notice.'

Question 2: Verification of an FDP

Do the changes in relation to the verification of an FDP strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities? To what extent is the standardisation approach desirable and/or achievable?

Whilst the consultation refers to "[reducing] the need for the Secretary of State to procure his own detailed advice" (paragraph 2.2), it may well be that the operator thinks this is a less risky approach than attempting to second guess the Secretary of State's needs. Particularly, as paragraph 2.16 of the consultation states, "… it is expected that the Secretary of State would commission his own expert advice in reaching his view on whether or not the FDP as submitted could be approved as prudent", the need for a verification report is less certain, and the operator can have no confidence in assuming that additional costs will not be incurred after submission of the FDP.

It would be sensible for DECC to work with the operator when procuring verification services to ensure that suitably qualified verifiers are appointed and that they are appropriately tasked. This would reduce the risk on all parties that an inadequate verification report is produced (see also subsequent, related comments [above]).

Recognising that there are likely to be two distinct verification reports is sensible and a welcome step.

Prudence

The proposed regulations have DTM verifiers assessing whether the "operator's evaluation of the prudence of the DTM costs… is reasonable", but it is not clear why DTM cost estimations should be assessed for prudence. A verifier of DTM costs should be able to form a view on whether the operator's estimate of DTM costs, rather than the operator's evaluation of the prudence of those costs, is accurate, or

reasonable. This would be consistent with s55(2)(a) of the Energy Act 2008 ("the Act") which allows the Secretary of State to "rely on estimates of costs verified by an independent third party" and makes no reference to prudence.

s55(2)(b) of the Act, however, does refer to prudence. It allows the Secretary of State to "rely on an independent third party's assessment of the prudence or otherwise of any provision made for the financing of the designated technical matters". In relation to the financing of the designated technical matters, we agree with DECC's assessment that it is unlikely that verifiers would want to commit themselves to judgements about prudence.

s46 of the Act ("Approval of a programme") gives the Secretary of State powers to approve a submitted FDP, and s46(4) says that the Secretary of State's powers "must be exercised with the aim of securing that prudent provision is made for the technical matters (including the financing of the designated technical matters)".2 We would contend that, contrary to the DECC's position in the consultation that prudence is not defined in the Act (paragraph 2.8), it is this section that defines prudence in relation to an FDP as what the Secretary of State approves: once the Secretary of State approves an operator's FDP, that defines what prudent provision is.

Accordingly other organisations may have views which may in turn inform the Secretary of State's views, but ultimately it is the Secretary of State who defines prudence by approving, subject or not to conditions, an operator's FDP.

Standard form of verification reports

It is clear that the Operator would like, and should be able to expect, that the verification services it procures should be acceptable to the Secretary of State. The operator is in an uncomfortable position where it is responsible for defining the verification role and finding a suitable supplier, whilst the product that supplier produces has to satisfy a third party (the Secretary of State). It is unclear whether the Operator would have recourse to compensation from the verification body should the verification report be unacceptable to the Secretary of State; and if that were the case, then the verification body would be unlikely to agree to such a clause without clarity from the Secretary of State of what is expected of the report. Some standard terms, or a list of "expectations" or tests, possibly included in the relevant regulations, would help to provide clarity.

The content of such a report will, largely, have to be established between providers of the service and the Secretary of State. For the operators' part, they will either have to pay for it when they commission work from the verifier, or when they pay the Secretary of State for commissioning his own expert advice: in either case it becomes another cost of producing an approved FDP and the operator will want to ensure that this cost is minimised where possible.

[2] http://www.legislation.gov.uk/ukpga/2008/32/section/46#section-46-4

Question 3: Modifications

Do the changes in relation to the modifications regime strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

It is unclear from the regulations as proposed whether broad, non-financial modifications to an operator's FDP would be permissible without the necessary oversight of approval from the Secretary of State. For example, if an Operator wished to modify the constitution of the independent organisation it had established to hold waste management and decommissioning funds: as drafted the operator could make a Section 48 modification proposal and claim that, under regulation 10(1)(b), claim that it does not relate to the financing of the DTM costs and that the 'relevant change in A' is less than 5%, and therefore Section 49 does not apply. This could allow the Operator to make very broad changes to its FDP without Secretary of State approval and is not, we expect, the intention of the regulations.

INSTITUTE AND FACULTY OF ACTUARIES

Question 2: Verification of an FDP

Do the changes in relation to the verification of an FDP strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities? To what extent is the standardisation approach desirable and/or achievable?

Our references to paragraph numbers are to those contained in the consultation document dated 27 April 2012.

We welcome the proposal to separate verification into two reports (paragraph 2.5). This should facilitate the involvement of scientific and engineering experts, on the one hand, and advisers such as ourselves who are expert on long term financing. However, this change requires an effective and open relationship between the verifiers to ensure that the financial verifier has a full understanding of future costs, their incidence and likely variation (including the approach taken to assessing prudence). Such a relationship between verifiers may be facilitated by DECC guidance.

As one particular aspect of this relationship, it appears that Designated Technical Matters (DTM) costs are required to be reported in the Funded Decommissioning Programme (FDP) in present money terms but the FDP will explain how those costs will be increased to reflect inflation. Actuaries are accustomed to working with inflation as financial modellers, but are not experts on its impact in the nuclear area. It may be helpful if DECC guidance could possibly comment on what is expected from scientific verifiers in terms of the particular effect of inflation on these nuclear costs, so that actuaries can take this into account in valuing liabilities. We note that the inflation of nuclear costs should not necessarily reflect inflation in the economy as a whole. We appreciate that DTM costs are to be assessed without regard to possible technological developments, so this factor may need to be ignored in considering future inflation.

A crucial aspect of the verification process is the approach to prudence, a criterion which we are accustomed to dealing with in our work on the long term stability of various financial institutions. As a general comment, we note that the prudence and resilience of this regime should ultimately be assessed as a whole, in terms of whether it ensures that sufficient monies are properly set aside on a timely basis for these liabilities whilst stations are still operating. In other words, all aspects of the funding regime need to be considered from this standpoint, including, for example, the arrangements for holding and investing funds.

We believe that prudence as such is a subjective concept and we do not think that the proposed wording mentioned in paragraph 2.8 obviates the need for a verifier to form a view as to the prudence of the approach taken. It would be helpful if the

financial verifier could rely on guidance from DECC, for example in advising that, in the following areas:

a) a market related approach should be used in assessing the value of future payments by operators;
b) the assets of the Fund should be valued at market value;
c) the liabilities should be valued on a “risk free” basis. In other words, the amount required to meet the liabilities would be determined as if the funds were retained in Government stock.

The above suggested guidance only briefly indicates an approach and would need careful consideration and drafting. Our professional body has worked with other Government departments and regulators in developing guidance and practice in the application of prudence in insurance and pensions matters. Guidance along these lines could reasonably be described as prudent in our view.

We agree that it would be helpful (paragraph 2.11) for a standard verification certificate to be developed but we suggest that different versions might be appropriate as between scientific and financial verification. Standardisation would help to ensure consistency and focus.

Question 3: Modifications

Do the changes in relation to the modifications regime strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator’s liabilities?

Turning to modifications, it appears that the 5% threshold is in relation to the total liabilities in present money terms. This means, for example, that a change in say 50 years’ time is given equal weight to a change of the same money value this year, even though the former has much less significance because of the effect of discounting. Perhaps operators could be allowed to use discounted values for testing against the threshold on the basis that they provided evidence of the calculation of such discounted values.

In paragraph 3.11, we suggest that the condition mentioned therein should be certified by independent verification rather than by the operator.

NUCLEAR DECOMMISSIONING FUND COMPANY LIMITED (FUNDCO) RESPONSE

Introduction

Dear Sir/Madam, I am submitting this response to the Consultation on behalf of The Nuclear Decommissioning Fund Company Limited ("FundCo"), which is proposed to be the custodian of the fund assets relating to NNB Generation Company Limited's ("NNBGenCo") funded decommissioning programme ("FDP"). I am the chairman of FundCo and confirm that this response represents the views of FundCo's board of directors and has been reviewed by FundCo's solicitors, Ashurst LLP.

FundCo is a party to the FDP and has been structured so as to be "associated" with NNBGenCo for the purposes of the Energy Act 2008 (the "Act"). As a result any breach by FundCo of its obligations under the FDP (when effective) could result in criminal sanctions for FundCo under section 57 of the Act. FundCo and its directors therefore have a keen interest in the proposed changes to the Regulations, and in particular that they do not make it difficult or impossible for FundCo to perform its obligations under the FDP.

FundCo generally welcomes the principles underlying the majority of the proposed changes to the Regulations and accompanying notes in the Consultation. However, FundCo has a number of serious outstanding concerns which are set out below in response to the three Consultation questions. As a general point, FundCo does not consider that the Regulations are necessary under the Act, except for (a) sections 10 and 11 which set out where the Secretary of State's consent to a modification of an FDP under section 49 of the Act would not be required and (b) section 6 which sets out certain fees payable to the Secretary of State. FundCo considers all other issues covered by the Regulations would be better dealt with within the FDP itself as otherwise any inconsistency between an approved FDP and the strict terms of the Regulations might lead to a breach of one of them.

FundCo also notes that there are differing possible interpretations of sections 45(7) and 48(1) of the Act as to which changes to an FDP, or to numbers or estimates calculated in accordance with mechanisms set out in an FDP, are "modifications" of an FDP for the purposes of section 48. For example, FundCo does not consider that a change in the value of the Fund Assets or the estimate of DTM costs, both of which are inevitable at every review, would be such a modification. FundCo's firm view is that changes to values, costs and other variables that occur purely within the established mechanisms set out in an approved FDP (and which do not amend any of the terms of an FDP) should not be considered modifications to that FDP, both as a matter of legal principle and of practical application. It is in no-one's interest for a genuine change in DTM cost estimates or the value of Fund Assets to be an automatic breach of an FDP (and criminal offence) unless such change is "approved" by the Secretary of State. FundCo is however cognisant that a feasible interpretation of the Act (espoused wrongly as the only interpretation at the start of paragraph 3.2) does mean that even these changes are "modifications" and so it is essential that sections 10 and 11 of the Regulations provide sufficient certainty to operators and fund companies (a guiding factor in the official guidance for FDPs) that a specified group of "modifications" to an FDP will be permitted without requiring

the Secretary of State's consent (which would otherwise create serious uncertainty for FundCo as to whether it can properly fulfil its obligations under the FDP).

References in this response to:

a) paragraphs, are to paragraphs in the Consultation;

b) sections, are to sections in the updated draft Regulations contained at Annex 1 to the Consultation; and

c) capitalised terms, have the meanings given to them in the Consultation, unless defined in this response.

This response may be made public by the Government and is not confidential.

Question 1: Reporting requirements

Do the changes in relation to the reporting requirements strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

FundCo welcomes the increases in the periods within which annual and quinquennial reports must be submitted to 6 and 9 months respectively, along with the requirement to synchronise the FDP reporting periods with the accounting year for an operator. However still concerned that the reporting periods could be exceeded if:

a. there is an unusually extended period of discussion between FundCo and NNBGenCo (and potentially verifiers) in relation to aspects of a report which is in accordance with the terms of the FDP; or

b. there was an ongoing dispute in relation to a report, and the dispute resolution process in the FDP was being followed to its conclusion.

FundCo would therefore expect the Regulations to allow for extensions of time for these, in particular where the sole reason for delay is due to a dispute which is being resolved in accordance with the provisions of the relevant FDP. FundCo considers it more important for the reviews to be undertaken properly, producing the correct figures for DTM costs, rather than for them to be concluded to meet arbitrary deadlines. believes it to be in the interest of taxpayers that DTM costs are kept as up to date as possible.

FundCo also notes that section 8 does not allow sufficient flexibility for reporting if a Quinquennial Review was proposed to be undertaken earlier or later than required for any reason which was in accordance with an FDP (for example, more regular reviews during the final period of the operational phase). In such a case the next Quinquennial Review should be at the time required by the approved FDP, not a fixed five years after the previous review. Similarly, section 8 does not acknowledge that there might sensibly be no reviews in the period from FDP approval until the first reactor achieves criticality. FundCo queries whether reviews serve any significant purpose in this period, which is before any contributions are made to the Fund. This

example illustrates how overly prescriptive Regulations are unhelpful in the context of a need for flexibility in the FDP."

Question 2: Verification of an FDP

Do the changes in relation to the verification of an FDP strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities? To what extent is the standardisation approach desirable and/or achievable?

FundCo welcomes the change of approach such that a verifier now needs to assess whether the operator's proposals for prudence are reasonable rather than making its own assessment of prudence. FundCo did not consider the existing regime workable. both because a verifier would be uncomfortable taking on such a role, and because an operator would be uncomfortable letting a verifier have such a role because it would arguably give a verifier sufficient power to derail an operator's original investment case and create uncertainty for a fund company.

However, as drafted, such a "reasonable" test requirement would be in addition to whatever an FDP specified that a financial or DTM verifier had to do. The provisions, including the definitions of "DTM verification report" and "financial verification report" therefore need to be clarified to ensure that compliance by a verifier with the relevant requirements of an FDP(which is of course approved by the Secretary of State) would be deemed to satisfy the relevant requirements in the Regulations. While the Consultation notes that the verifier is anticipated to have regard to the relevant FDP (at the end of paragraph2 .9 and in paragraph2 .10), this needs to be made explicit in the Regulations themselves. The FDP effectively records what both the operator and the Secretary of State (through his approval of the FDP before it can become effective) consider to be prudent.

FundCo is unclear on the scope of the new proposed verification report definitions and would appreciate clarification, in particular on whether the words "prudence of the financing of the DTM costs" in the definition of "financial verification report" require a verifier to consider the credit risk on an operator in relation to likely contributions due under an FDP.

FundCo also welcomes the official split of verification into technical and financial matters and recognition that FundCo might appoint a verifier, which is how FundCo envisaged verification working in practice.

Regarding paragraph 2.11, FundCo does not consider it appropriate for the form of a Verification statement t be standardised for all FDPs as the form will necessarily have to differ to cater for the individual needs of each FDP.

FundCo also welcomes the recognition in the Consultation that verifiers need to operate under indemnity cover (at paragraph2). However, we note that no reference is made to this in the Regulations. Is it anticipated the Secretary of State will (a) enter terms of engagement with a verifier, (b) otherwise agree to respect any

caps on liability agreed between a verifier and the party to an FDP appointing it or (c) clarify that a verifier had no duty of care to the Secretary of State or other legal liability, notwithstanding section5 5 of the Act. It would be helpful if this was addressed in the Regulations themselves otherwise FundCo considers this will be an issue in finding persons willing to take on the verifier role.

Question 3: Modifications

Do the changes in relation to the modifications regime strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

FundCo welcomes the recognition in paragraph 3.6 of the Consultation and, presumably, the definition of "DTM costs" in section 4, that inflation would not be counted when considering whether increases in the DTM costs reached the 5% threshold, however, this could ideally be more clearly set out in the Regulations.

While FundCo generally welcomes the new proposals expanding the range of "modifications" which can be made to an FDP without requiring the consent of the Secretary of State under section 49 of the Act, it has concerns over whether these will work as intended.

The most important exception from FundCo's perspective is that referred to at paragraph 22 of the Consultation and contained in section 10(1)(a). Please clarify the drafting in order to make it clear that this is intended to mean that pre-agreed matters in an FDP, i.e. changes to e.g. cost estimates and required contributions to the Fund made in accordance with mechanisms set out in an FDP, would not need the approval of the Secretary of State. FundCo is confused by the current drafting which refers to "an item which was specified by the Secretary of State". What is this intended to mean, if not any mechanism set out in an FDP? FundCo is concerned by paragraph 3.25, among others, giving, as an example of FDP "modifications" this exemption is intended to cover, the value of the Fund Assets. This could theoretically change on a minute by minute basis if held in listed shares and FundCo does not agree as a basic legal principle that the value of the Fund Assets changing would constitute an FDP "modification". Furthermore, the reference to the contributions by the operator changing in accordance with the terms of the FDP being a "modification" is, in FundCo's view, incorrect.

Another important exemption from FundCo's perspective is that set out in sections 11(2) and 11(3). The meaning of 11(2)(a) is critical in establishing whether the exemption works. It appears to have been drafted with the provision of a parent company guarantee as security in mind. It needs to be clarified that "other security" includes the operator's present and future payment obligations under an FDP, aside from monies already in the Fund and those available under any other funding proposals. It is FDP Co's view that this is the correct interpretation if "security" has the meaning which would be ascribed to it in section 45(7)(c) of the Act, i.e. anything contained in or referred to in the FDP, but FundCo would not be comfortable relying on such an interpretation under the proposed drafting of the Regulations unless further clarified. The wording "is of a value greater than or equal to the value of the

revised liabilities" also requires further thought. Presumably the revised liabilities is the NPV of the DTM costs, but on what assumptions/probability basis? The soft guidance in paragraph 3.15 is helpful in as far as it goes but the Regulations themselves should be clear. And the use of the present tense ("is") does not sit well with the Fund being anticipated to grow over many years to match anticipated DTM costs, not to match them earlier than the expected time for decommissioning nor with the possibility that an operator may be permitted/required by the terms of an approved FDP to make up a deficit over a number of years. FundCo is concerned by the uncertainty regarding the time allowed to make up the Fund. The end of part 3, paragraph 3.12 says "within a short, defined time period" whereas section 11(3) implies there is no time at all. Finally, the reference to security "provided when the FDP was approved" should be deleted - the relevant value is that of the security that will be in place as required by the specific terms of the approved FDP as a consequence of the proposed change in DTM costs.

FundCo welcomes the new exception relating to changes in the waste disposal charge under a waste transfer contract between government and an operator in section 11(4). However, FundCo queries whether this exception should be limited to such a specific reason for an increase or whether other increased, or indeed decreased, costs under a waste transfer contract should also be capable of being taken into account.

Additional Comments

The definition of "associated person" in section 4 is potentially confusing because it refers to any person other than the operator with obligations under an FDP. Section 57 of the Act uses the term to apply to persons "associated" with the operator (i.e. the 20% control rule) who have FDP obligations and is therefore narrower. FundCo suggests the definition in the Regulations is changed, for example, to "FDP party".

Finally, the Regulations contain a number of drafting inconsistencies and errors which require correction before final publication, for example:

a) Regulation 7(2)(b)(ii) - the word "designated" is mis-spelled;

b) Regulation 8 (general) – the various definitions in this Regulation should all be moved to (6), following the words "In this regulation";

c) Regulation 8(4)(d) – in the definition of "period 1" limb (a) the second line should have "of the site operator's funded decommissioning programme" added after "on the date of approval" and in limb (b) "site operator's" should be added after "the date of the approval of the", in both cases for consistency with the expressions used elsewhere in the Regulations;

d) Regulation 10(2)(d) – this paragraph should be merged into 10(2)(c);

e) Regulation 10(3) – in the definition of "relevant estimate", "later" in the first line should be replaced with "latest"'; and

f) Regulation 11(2)(a) – the words "is for a modification that will cause an increase in" should replace the words "is to increase". This is again to ensure consistency with similar wording used in Regulation 11(4).

NUCLEAR INSTITUTE

Question 1: Reporting requirements

Do the changes in relation to the reporting requirements strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

It may be considered logical and rational to synchronise the reporting timeframes for FDP and the end-of-year financial reporting by the Operator, as required under the Companies Act 2006. This would (i) reduce costs to the operator; (ii) reduce regulatory burden; (iii) enhance transparency; and (iv) could result in the enhancement of public confidence in the financial reporting of the operator in general.

The current period of 3 months for submitting an 'Annual Report' may be regarded as too short, noting that it needs to be accompanied by the 'verification reports'. Amending the period for submitting an annual report from 3 months to 6 months would reduce unnecessary burden on the Operator, and could enhance the quality of the report. It could, equally, enhance public confidence in the process.

The same may be argued in relation to amending the period for submitting a quinquennial report from 6 months to 9 months, which would, indeed, be more onerous than an annual report. "

Question 2: Verification of an FDP

Do the changes in relation to the verification of an FDP strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities? To what extent is the standardisation approach desirable and/or achievable?

Government proposals to separate the verification report into a Technical Verification Report and a Financial Verification Report are most welcome. It would be rather difficult to find a 'verifier' who has the requisite financial & technical expertise & competency. However, there needs to be a 'Lead Verifier' to ensure that the two Reports are complementary and in synergy.

It would be, also, helpful should the Government offer further clarification as to the criteria which would render a given entity (an independent third party, as stipulated in section 55 of the Energy Act 2008) an acceptable verifier. Separate criteria would, of course, be needed in relation to a 'Technical Verifier' and a 'Financial Verifier'. As it stands, it is not clear as to who would qualify as a verifier.

It would, equally, be helpful to have clarification as to whether "an independent third party" - a private or public body/entity - from outside the European Union (EU) or the European Economic Area (EEA) could qualify as a verifier.

As regards the proposed revision to the definition of a verification report in the current Regulations, one may argue that the notion of 'prudence' is still vague, if not redundant. This may, also prove problematic, should the decision of the Secretary of State in approving a given FDP be challenged by third parties in the High Court - under the Judicial Review procedure – on the grounds that 'prudence' is vague, and not subject to quantification. Perhaps, one may suggest the following definition:
'A written report which contains an assessment by a verifier as to whether or not the operator's evaluation of the estimations or projections, either in relation to the Designated Technical Matters (DTM) costs or the financing of the DTM costs, is reasonable.'

As regards standardisation of the verification process, it should be noted that the number of potential operators submitting an FDP would be limited to 2 or 3 (EDF, Horizon, and NuGen) as it stands. Hence, standardisation may not be warranted. Notwithstanding, it would be constructive should the Government (DECC) offer further guidance as to the contents of an FDP, enabling the operator, the verifier, the Secretary of State, and the public to have a better understanding of the scope and extent of an FDP in advance.

Question 3: Modifications

Do the changes in relation to the modifications regime strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

The Government proposals that "in addition to the exemptions from approval in the Current Regulations, there should be three further classes of modification that will not require approval by the Secretary of State" are logical & rational. This would reduce regulatory and financial burden on the operator. Also, public confidence in the process would not be adversely affected, as the proposals stipulate, inter alia, that there should be "sufficient financial security to meet the revised liabilities" for "modifications that increase estimated costs by more than the 5% materiality threshold."

NUGENERATION LIMITED

Question 1: Reporting requirements

Do the changes in relation to the reporting requirements strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

Nugeneration Ltd believe the proposed change is both sensible and pragmatic.
We welcome the proposal to make the operator synchronise the FDP reporting year with its own financial year. This makes eminent sense and is likely to reduce administrative costs as well as avoiding procedural difficulties.

We also welcome the proposed extension for submitting an annual report to the Secretary of State within 6 months of the end of the relevant period and submitting a quinquennial report within 9 months of the period to which it relates. We agree with the Government's view that these changes would not have any impact on the Secretary of State's ability to ensure that an FDP continues to make a prudent provision.

Question 2: Verification of an FDP

Do the changes in relation to the verification of an FDP strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities? To what extent is the standardisation approach desirable and/or achievable?

Nugeneration Ltd welcomes the proposed changes to the FDP verification arrangements. We believe that the proposal for having 2 separate verification reports covering technical verification of the Designated Technical Matters (DTM) and financial verification makes a great deal of sense and should help a prospective new operation like Nugeneration Ltd to secure competent verifiers.

We also agree that the original requirement on verifiers to form their own conclusion on prudence looks problematic to operate in practice. We consider that the proposed test by the respective verifiers of the reasonableness of the operators evaluation of the prudence of the DTM costs or of their financing costs strikes an appropriate balance of rigour and feasibility.

On standardisation we have no strong views on the alternatives set out in the consultation document. But as the verifiers will have a role in verifying the FDP before it is submitted to the Secretary of State for approval we think that aspects of the verification report used could then become the model for reports in respect of annual and quinquennial reviews. However we would not be opposed to the use of a standard verification certificate.

We have continuing concerns about whether there will be a market for DTM verification work. There are a relatively small number of organisations that would

have the necessary competencies and capabilities required to perform such a task, and those that do have the requirements may not find this work attractive since it is unlikely to be economically rewarding (compared say to other roles they could perform for an operator). This view was borne out of the complete lack of technical verifiers attending the consultation event on the 14th May.

We do not have the same reservations about financial verifiers where there appears to be an abundance of potentially interested parties. It may be necessary to consider clarifying the independence criterion so as to maintain safeguards against bias, while ensuring that potential DTM verifiers do not feel that performing this role would exclude them from an uneconomic amount of other work.

Question 3: Modifications

Do the changes in relation to the modifications regime strike the right balance in setting a framework which is achievable at reasonable cost to the operator while enabling the Secretary of State to have confidence that the FDP continues to represent prudent provision for the operator's liabilities?

Nugen welcomes the principles of the proposed amendments to Regulations 10(1a), 11(2) and 11 (4) and believe they strike the right balance in setting an effective framework with reasonable costs. However there are tow areas where we would seek further clarification or change:

- The first area is how the 5% materiality threshold will be affected by general inflation in the economy. It is possible for a change in the FDP to have a relatively small impact on costs (say 1%) but if inflation in the period since the last quinquennial review has been higher than expected , the combined impact could easily exceed the 5% threshold. We suspect the references to costs in Regulation 10(3) are intended to be construed in real terms but we would be grateful if this could be clarified or an appropriate amendment made.

  In fact we clearly identify this purpose from the Government statement in s.3.6 of the consultation document – "FDP will be able to provide for the escalation of the DTM costs for inflation without this being regarded as a modification to the FDP" but we haven't found this intention in the new text of the 2011 Regulations. As we mentioned before we suggest clarifying it through an explicit amendment in 10 (3).

- The second area is the precise criterion in Regulation 11(3) whereby an operator can enhance the funding rather than seek Secretary of State consent. It seems to us possible that the SoS would consider as prudent an FDP built up over time and which therefore might have less than 100% coverage in the early years. When such an FDP is changed it seems sufficient that any addition to the fund to compensate for the change should be enough to remedy any deterioration in the coverage arising from the change. In this case Regulation 11 (3) (a) might read along the lines:

a) The fund, together with any other security provided when the funded decommissioning programme was approved, either

   i. Is of greater than or equal to the revised liabilities, calculated in accordance with the approved funded decommissioning programme; or

   ii. Falls short of the revised liabilities so calculated by an amount less than or equal to the amount by which the fund fell short of those liabilities immediately before the change.”

SCOTTISH ENVIRONMENT PROTECTION AGENCY

We note that this consultation is limited in scope and sets out the changes that the Government is proposing to the original Funded Decommissioning Programme (FDP) for financing of new nuclear power stations.

We also note that the consultation is sponsored by DECC and covers regulation of nuclear energy which is a reserved matter to the UK Parliament.

Generally, SEPA is supportive of the requiremement for operators of nuclear power stations to have secure financing in place to meet the full costs of decommissioning and their full share of radioactive and non-radioactive waste management costs. For civil nuclear sites in Scotland, funding is administered through the Nuclear Decommissioning Authority. For private operators, funding is usually through a segregated decommissioning fund. Currently, these arrangements are working well in Scotland.

We have no comments on the consultation as it extends only to amendments to the original FDP arrangements in England and Wales for new nuclear power stations.