

Title: Smart Meters Bill - half-hourly electricity settlement powers Lead department or agency: Department for Business, Energy and Industrial Strategy (BEIS) Other departments or agencies: Office of Gas and Electricity Markets (Ofgem)	Impact Assessment (IA)
	Date: 06/02/2018
	Stage: Final
	Source of intervention: Domestic
	Type of measure: Primary legislation
Contact for enquiries: smartenergy@beis.gov.uk	
Summary: Intervention and Options	RPC opinion: n/a ¹

Cost of Preferred Option				
Total Net Present Value	Business Net Present Value	Net cost to business per year (EANCB in 2014 prices)	In scope of One-In, Two-Out?	Measure qualifies as
n/a	n/a	n/a	Yes	Zero- net cost

What is the problem under consideration? Why is government intervention necessary?
 Competition, consumer choice and consumer engagement is currently constrained by the existing electricity settlement process. To help overcome this barrier, Ofgem intends to open up opportunities for time-of-use tariffs and demand-side response by reforming the existing electricity settlement processes. However Ofgem's existing powers to deliver reforms through Significant Code Review (SCR) processes² have been prone to delays and lack of coordination across codes, hence new primary powers are needed to enable Ofgem to deliver these reforms in a more timely, coordinated and cost-effective manner which ensures a better outcome for consumers.

What are the policy objectives and the intended effects?
 The overarching objective is to reform the electricity settlement process to enhance competition and increase consumer choice/engagement. The primary policy objective associated with the new powers is to establish a new (time and scope limited) regulatory regime which enables Ofgem to facilitate the implementation of the settlement reforms in a timelier, more coordinated and more cost-effective manner which ensures better outcomes for both consumers and industry, relative to the existing arrangements.

What policy options have been considered, including any alternatives to regulation?
 Two options were considered:
 - Option 1: **'Do Nothing'** and use existing code modification powers, including SCRs, to deliver the changes required. This option was ruled out on the basis that it is unlikely to achieve the policy objectives outlined above i.e. implementation of the reforms in a timely, coordinated and cost-effective manner.
 - Option 2: The **'Preferred Option'** is time and scope limited primary legislation. This is considered the preferred option as it will ensure that settlement reform is delivered in a timelier, more coordinated and more cost-effective manner that ensures better outcomes for both consumers/industry relative to the existing arrangements.

Will the policy be reviewed? It will be reviewed. Review date: 2022					
Does implementation go beyond minimum EU requirements?			N/A		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	Micro: Yes	< 20: Yes	Small: Yes	Medium: Yes	Large: Yes
What is the CO2 equivalent change in greenhouse gas emissions? (Million tonnes CO2 equivalent)			Traded: n/a	Non-traded: n/a	

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister:  Date: 07/02/18

¹ This measure qualifies for de minimis and therefore does not require RPC scrutiny.
² The SCR mechanism enables Ofgem to direct licensee(s) to make changes to relevant industry codes to deliver outcomes specified in an SCR Direction made by Ofgem.

Summary: Analysis & Evidence

Policy Option 2

Description: Introduce time and scope limited primary powers to enable Ofgem to facilitate the delivery of half-hourly electricity settlement.

FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: n/a	High: n/a	Best Estimate: n/a

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	n/a	n/a	n/a
High	n/a	n/a	n/a
Best Estimate	n/a	n/a	n/a

Description and scale of key monetised costs by 'main affected groups'

There are no immediate monetised costs associated with the proposed primary legislation as it will not affect the nature of regulation in the sector until the scope of its use has been defined by Ofgem following consultation with interested parties. However consideration has been given to the potential costs to business of this time and scope limited change to the code and licence modification process. Under the central case the current assessment suggests that there should be no additional costs to business as a result of the proposed powers relative to the existing regulatory arrangements. The proposed powers will require Ofgem to conduct an impact assessment when enacting code modifications for the purposes of settlement.

Other key non-monetised costs by 'main affected groups'

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	n/a	n/a	n/a
High	n/a	n/a	n/a
Best Estimate	n/a	n/a	n/a

Description and scale of key monetised benefits by 'main affected groups'

There are no immediate monetised benefits associated with the proposed primary legislation as it will not affect the nature of regulation in the sector until the scope of its use has been defined by Ofgem. However, consideration has been given to the potential impacts. In the central case the potential resource savings (discounted, 2015 prices) for industry are expected to be around £1.3m for the settlement reform programme and for Ofgem the resource savings are expected to be around £0.70m. The proposed powers will require Ofgem to conduct an impact assessment when enacting code modifications for the purposes of settlement.

Other key non-monetised benefits by 'main affected groups'

In addition to the monetised savings outlined above, as a result of the enhanced coordination of the process there could potentially be additional resource savings (for both Ofgem and industry) associated with the delivery of the reforms due to increased efficiencies relative to the existing arrangements. The proposed powers could also bring the delivery date of the reforms forward by 13.5 months. This change is expected to be net beneficial to consumers and industry relative to the counterfactual.

Key assumptions/sensitivities/risks

3.5%

A full list of assumptions underpinning the indicative monetised costs and benefits and risks is detailed in section 5 below. The analysis uses a NPV base year of 2017 (3.5% real discount rate) and all values are expressed in 2015 real prices. Ofgem's use of the new powers will be subject to a consultation carried out with interested parties. At this stage, there is still a high level of uncertainty around the incremental impact of the proposed powers.

BUSINESS ASSESSMENT (Option 2) (n/a Prices, n/a NPV base year)

Direct impact on business (Equivalent Annual) £m:			In scope of OITO?	Measure qualifies as
Costs: N/A	Benefits: N/A	Net: N/A	Yes	Zero Net Cost

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Evidence Base (for summary sheets)

1. Problem under consideration

1. The UK government supports Ofgem's intention to use the opportunities provided by the roll-out of smart metering to ensure better outcomes for consumers by reforming the current electricity settlement processes.
2. Competition, consumer choice and consumer engagement are currently constrained by the existing electricity settlement processes. To help overcome these barriers, Ofgem intends to open up opportunities for time-of-use tariffs and demand-side response by reforming the existing electricity settlement processes.
3. While Ofgem have existing powers to deliver the settlement reforms through the SCR process, past experience shows that this process has been prone to delays and lack of coordination across codes. In light of this, Ofgem is considering longer term reforms to the current code modification arrangements, which will also be shaped by the Competition and Markets Authority's (CMA) investigation into the energy market.
4. It is considered that whilst there is a longer term objective to reform the SCR process, there is a need for a short term solution for the purposes of delivering the settlement reforms to ensure that the benefits of the reforms (increased customer choice and enhanced competition between suppliers) are achieved sooner rather than later. The new time and scope limited primary powers included in the Smart Meters Bill are intended to enable Ofgem to deliver the settlement reforms in a more timely, coordinated and cost-effective manner which ensures better outcomes for both consumers and industry relative to the existing regulatory arrangements.³
5. This section outlines the following:
 - a. Background on the proposed settlement reforms;
 - b. Background on Ofgem's existing powers to deliver these reforms, namely the SCR process and the shortcomings of this process; and
 - c. Overview of the proposed primary powers.

1.1 Background: Electricity Settlement Reforms

6. Ofgem intends to use the opportunities provided by smart and advanced meters that can record half-hourly consumption and be remotely read to improve the accuracy and timeliness of the electricity settlement process. This in turn will open up opportunities for time-of-use tariffs and demand-side response. Ofgem's intention to reform the settlement process is driven by the consideration that this will increase consumer engagement and consumer choice, and will also promote more effective competition between suppliers.
7. The settlement process was initially designed to support the introduction of competition in the retail market in the late 1990's. Electricity settlement currently operates on a half-hourly basis, however half-hourly capable metering is not currently available in all homes and smaller non-domestic premises. Consequently, at present the majority of consumers are settled 'non-half hourly', whereby estimated consumption profiles are used to allocate energy used to each half hour period.

³ A draft version of these powers, alongside similar measures relating to faster switching, were published for pre-legislative scrutiny in 2016. See: <https://www.gov.uk/government/publications/draft-legislation-on-energy>. This included an impact assessment covering the faster switching and half-hourly settlement powers, which forms the basis of the current document. See: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/493713/Impact_Assessment_-_Draft_Measures_-_Fast_and_Reliable_Switching_and_Hal_.pdf

8. On the 4th of April 2014 following a period of scoping, Ofgem published a document⁴ which concluded that the move to half-hourly settlement (based on actual half-hourly consumption data) is likely to be beneficial to consumers. Settling consumers against their actual half-hourly data would fully expose suppliers to the difference in cost across the day of purchasing and transporting energy. This improvement in the accuracy of the allocation of energy and network costs would place stronger incentives on suppliers to help consumers move consumption to periods when electricity is cheapest. In addition this reform could also make the settlement process more efficient and reduce the risk of operating in the market. Hence moving to half-hourly settlement could increase customer engagement and also promote more effective competition between suppliers. The document also set out plans for how Ofgem would progress the settlement project.
9. The CMA has also concluded that settlement reforms are necessary, finding that:
'the absence of a firm plan for moving to half-hourly settlement for domestic electricity customers is a feature of the market for domestic and SME retail electricity supply in Great Britain that gives rise to an AEC [adverse effect on competition] through the distortion of suppliers' incentives to encourage their customers to change their consumption profile, which overall reduces the efficiency and, therefore, the competitiveness of domestic and microbusiness retail electricity supply.'⁵
10. On the 28th of January 2015, Ofgem published an update on the electricity settlement project⁶ which outlined the following:
 - a. Ofgem had approved a modification to the Balancing and Settlement Code (BSC) that requires larger non-domestic consumers to be settled using half-hourly consumption data.
 - b. A subsequent modification to the BSC confirmed that non-domestic consumers will start to migrate to the new arrangements from 1 November 2015, with migration complete by 1 April 2017.
 - c. Ofgem had launched a project to explore how this could be achieved for domestic and smaller non-domestic consumers.
 - d. Ofgem's intention to publish a strategy to promote energy system flexibility in 2015. The next steps for settlement reform will be considered in the context of this strategy.
11. The joint Government/Ofgem *Smart Systems and Flexibility Plan* (July 2017) confirmed the importance of half-hourly settlement as a key enabler of the move towards a smart energy system,⁷ and Ofgem launched an SCR on market-wide half-hourly settlement alongside the Plan.⁸

1.2 Background: Current SCR powers, code modification appeals process and licence modification 'standstill period'

SCR powers and code modification appeals process

12. The SCR mechanism enables Ofgem to direct licensee(s) to make changes to relevant industry codes to deliver outcomes specified in an SCR Direction made by Ofgem, or to raise and develop such changes itself.

⁴ Ofgem, 2014, Electricity settlement reform – moving to half-hourly settlement [web], available at: https://www.ofgem.gov.uk/sites/default/files/docs/2014/04/electricity_settlement_launch_statement_0.pdf

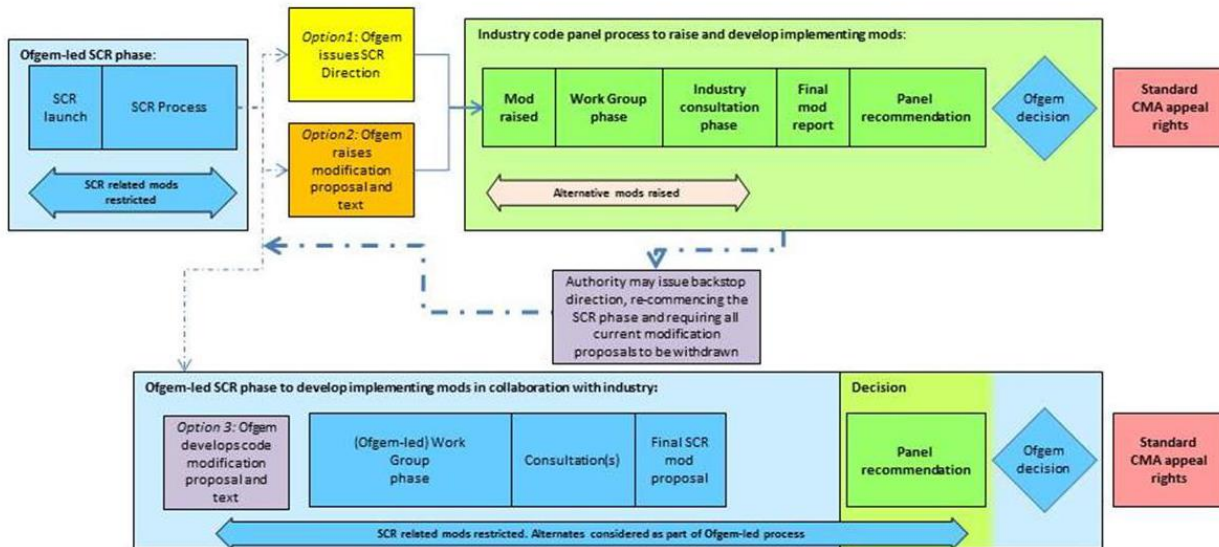
⁵ CMA (2016) *Energy market investigation – summary of final report*, paragraph 187. See: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/531157/Energy-final-report-summary.pdf

⁷ See: <https://www.gov.uk/government/publications/upgrading-our-energy-system-smart-systems-and-flexibility-plan>

⁸ See: <https://www.ofgem.gov.uk/publications-and-updates/electricity-settlement-reform-significant-code-review-launch-statement-revised-timetable-and-request-applications-membership-target-operating-model-design-working-group>

13. The SCR process generally starts with an Ofgem-led series of consultations which could lead to an SCR launch. In 2016, the process following a launch was revised in order to give Ofgem options to take a more directive role in the process by raising or developing modifications itself (rather than directing industry parties to do so), including by leading the workgroups that develop proposals. This followed concerns that the SCR approach was prone to delays and lacked co-ordination. The three options for the process are set out in Figure 1 below.

Figure 1: High-level SCR process and appeals process



14. Figure 1 illustrates the high level SCR process outlined in the preceding paragraphs as well as the SCR's current appeals process.

15. Currently, Ofgem's decision following the panel recommendation may be appealed by way of Judicial Review (JR) or by statutory right of appeal to the CMA (see figure 1). There is a right to appeal to the CMA where Ofgem's decision is not to consent to the recommendation of the industry panel. Judicial Review (JR) may be available where Ofgem consents to the panel's recommendation. Generally speaking, the CMA appeal route may raise substantive grounds of challenge to the decision, whilst the grounds for judicial review are broadly procedural.

Licence modification 'standstill period'

16. As well as modifying industry codes, part of the settlement reforms will involve modifying the licences of industry participants. The current, minimum, process for modifying licences is as follows.

- Statutory consultation, for 28 days, on proposed licence changes
- Decision notice published
- 56 days after the decision notice is published, the licence change comes into effect.

17. In practice, it is usual to have one or more policy consultations before the statutory consultation is eventually published.

18. The 56-day 'standstill' period before the licence changes are implemented reflects the time in which the CMA may grant permission for an appeal to be raised (up to 40 working days). There is not an equivalent statutory or licence-based standstill period in the code modification process.

1.3 Proposed Primary Powers

19. This Impact Assessment (IA) accompanies time and scope limited primary legislation which will enable Ofgem to implement settlement reforms in a timelier and more cost-effective manner relative to existing arrangements so as to ensure better outcomes for consumers. The proposed powers will

be time limited to five years from commencement and scope limited to the settlement reform programme only.

20. The proposed primary powers will enable industry codes to be modified directly by Ofgem rather than industry so as to facilitate expeditious and coordinated changes to industry codes. This is because it is considered that the current SCR process will not deliver the policy objectives (enhanced competition and increased consumer choice/engagement) of the settlement reforms in a timely and cost effective manner that ensures better outcomes to consumers.
21. The proposed powers will also introduce a new appeals process. Although the CMA appeals route is currently available under the SCR process in circumstances where Ofgem's decision is not to consent to the recommendation of the industry panel, the new process (enabled by the proposed powers) will utilise the JR appeals process only. It is considered that the CMA appeals route will not be needed to support the proposed powers because Industry will be able to provide sufficient scrutiny of Ofgem's policy-making and decision-making throughout the programme of reforms through stakeholder consultation and workgroups.
22. The proposed powers will also require Ofgem to conduct an impact assessment when enacting code modifications. This will provide affected parties another opportunity to provide scrutiny and oversight to Ofgem without adversely affecting the timely delivery of the reform programmes.
23. Finally, the proposed powers will introduce the ability for Ofgem to reduce the 56-day period between the notice of a licence modification being published and the modification coming into effect. This is intended to facilitate the timely implementation of changes to licences in the time-critical periods immediately before, and after, go live of the reforms. Further information on the rationale for the proposed powers is provided in Section 2.
24. In summary, although the proposed settlement reforms are at an early stage of development, Ofgem considers that the proposed settlement reforms are likely to be net beneficial as they will increase consumer engagement and consumer choice as well as enhance competition between suppliers. Whilst Ofgem have existing powers to deliver settlement reforms through the SCR process, past experience shows that using this process is prone to delays and lack of coordination across codes. While new processes were introduced in 2016 to deal with these issues, there is still a major concern in relying on those new processes: the new processes do not give Ofgem the ability to raise modifications at different times during the SCR process. This causes a problem in managing a complex and large change programme, as there will be a need for Ofgem to put in place transitional requirements on the path to introducing new systems and processes, as well as requirements to enable the enduring solution. It is also possible that issues at late stages of the process would require further code modifications that were not predicted earlier on.
25. These concerns mean that Ofgem would be likely to have to rely on industry led modifications outside of the SCR process to address any further issues, instead of having the ability to make further modifications later on to address these issues, which would create significant risks of time delays, lack of co-ordination between various codes and sub-optimal definition of requirements. As such, whilst there is a longer term objective to reform the industry code governance processes more fundamentally, it is considered that the proposed time and scope limited powers are needed to ensure that the benefits from the proposed reforms are successfully delivered sooner rather than later.

2. Rationale for Intervention

26. The primary focus of this IA is to assess the potential direct impact of the proposed primary powers which are intended to enable Ofgem to deliver the settlement reforms in a more timely, coordinated and cost-effective manner. Hence the IA will not focus on assessing the actual direct impact of the settlement reforms as these are still at an early stage of development and will be separately assessed in subsequent IA(s) produced by Ofgem.
27. The UK Government supports the intention to promote a more dynamic and efficient energy market. It is considered that competition, consumer choice and consumer engagement are currently constrained by the existing electricity settlement processes. Ofgem's intended reforms will help overcome these barriers, opening up opportunities for time-of-use tariffs and demand-side response by reforming the existing settlement processes.
28. Whilst Ofgem have existing powers to deliver the settlement reforms through the SCR process, past experience shows that this process has been prone to delays and lack of coordination across codes. Even though the SCR powers were updated in 2016 to allow Ofgem to play a more active role in driving forward the process, it is unlikely that Ofgem could rely entirely on the SCR process to make the required changes for settlement reform and would therefore face risks of time delays and insufficient co-ordination between codes.
29. Hence, the rationale for the time and scope limited proposed powers is driven by Ofgem's ambition to address the overarching barriers to competition and consumer engagement/choice associated with the current settlement processes. The new powers will enable the expedited delivery of the reforms in a more coordinated and cost-effective manner by addressing the regulatory failure associated with the existing SCR process.
30. The subsequent sections will provide further detail on why the new process (enabled by the primary powers) is needed to ensure the outcomes outlined above are achieved.

2.1 Rationale for the proposed powers to amend the SCR process

31. As outlined in the preceding section, the overarching policy objective is to reform settlement processes to ensure that the barriers identified (consumer choice, consumer engagement and competition are currently constrained) are overcome.
32. The primary policy objective of the new powers is to establish a new (time and scope limited) regulatory regime which enables Ofgem to facilitate the implementation of settlement reforms in a timelier, more coordinated and more cost-effective manner which ensures better outcomes for consumers and industry relative to the existing arrangements.
33. The primary objective outlined above supports the UK Government's plan of action to guarantee clean, affordable and secure energy as the new powers will:
 - a. Ensure that the key policy objective of settlement reforms is achieved (promoting a more dynamic and efficient energy market); and
 - b. Minimise the resource costs and risk of delay in the pre-implementation phase.
34. Hence, the proposed powers are intended to ensure better outcomes for both consumers and industry as the powers are expected to promote a more efficient reform programme for half-hourly settlement.
35. The actual implementation of settlement reforms will require changes to multiple industry codes with consequent, significant changes expected to parties' IT systems and processes. Ofgem have indicated that in the absence of new powers they would use existing SCR powers to deliver settlement reforms, as the most appropriate way of delivering the reforms using the current regulatory regime.
36. However, the use of existing SCR powers raises risks that the policy objectives identified in the preceding paragraphs will not be achieved. Under the existing powers, the industry is responsible for

delivering policy conclusions through the code modification process. However in the CMA's final report, the CMA states its concerns around the length of time that code modifications have generally taken in the past and concern around the fact that the process has not begun for the settlement reforms in particular⁹.

37. It is considered that there are two reasons why industry is unlikely to lead this process effectively for the settlement programme:

- a. Parties that oppose reform can derail or delay the modification process; and
- b. There is a need for leadership and coordination across industry codes, but there is no industry party able to play this role for complex changes, for example changes that cut across multiple codes.

a. Parties that oppose reform can derail or delay the modification process

38. Whilst Ofgem has launched an SCR for the settlement reforms, Ofgem has also noted that in the meantime industry may not currently have the appropriate incentives to raise the modifications that will deliver the necessary settlement reforms under the existing SCR powers, which in turn raises the following risks:

- That the policy objectives for settlement reforms will not be achieved; and
- That implementation is delayed.

39. Some industry parties may not be incentivised to deliver the necessary reforms in a timely, coordinated and cost-effective way that maximises the benefits to consumers because the reforms may impose additional costs on industry players and could also threaten the benefits that some suppliers are currently able to accrue. This reasoning is outlined below:

- I. Currently, the evidence suggests that weak customer response gives suppliers a position of unilateral market power concerning their inactive customer base in which they are able to exploit these customers through their pricing policies. Hence, some suppliers may oppose the reforms because one of the key objectives of the reforms is to promote competition (by decreasing barriers to entry and/or by decreasing constraints on the way suppliers compete and/or by increasing customer engagement), which could in turn exert downwards pressure on prices. This would benefit consumers through lower bills, though this would also represent a transfer from suppliers to consumers.
- II. In a competitive market, half-hourly settlement is likely to create an incentive for suppliers to offer tariffs to consumers which incentivise them to reduce their demand for energy at more expensive times, e.g. in winter at times of peak demand. This could reduce consumer bills directly, and also reduce the pressure on the system at times of peak demand. However these are not necessarily benefits which will accrue to current suppliers so they may not have an incentive to take them into account as part of an SCR process.
- III. Suppliers may also oppose the reforms because of the additional up-front implementation costs. Implementation of the reforms will require changes to multiple industry codes with consequent, significant changes to parties' IT systems and processes. Crucially, while suppliers will need to incur the additional implementation costs, they may not however realise all of the benefits from the reforms as outlined in the previous section (for example, because some of the benefits will accrue to new entrants in the market).

40. Suppliers' opposition can be manifested by parties raising alternative modifications which seek to reopen issues that may have already been considered in making any SCR conclusions/direction which would require additional resources to assess. The industry-led process is also reliant on

⁹ CMA, 2016, Energy Market Investigation: summary of final report, page 44 [web], available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/531157/Energy-final-report-summary.pdf

suppliers providing information that would allow a robust impact assessment to be carried out and previous experience suggests that suppliers' opposition to a proposal could be reflected in the quality or timeliness of the information they provide to support impact assessments.

b. The need for leadership and coordination

41. A significant risk of time delays and lack of coordination across various codes exists even under the updated SCR process as Ofgem would still have to rely on industry parties to put in place the required code modifications to address any further issues (given the restriction under the updated SCR process, meaning Ofgem cannot make further modifications at different times throughout the process). However, currently there is no incentive for an industry party to take on the necessary leadership role to co-ordinate changes across multiple industry codes. While the benefits of a cross-industry reform may accrue to consumers, or to industry as a whole, it is unlikely that any one party would be able to capture enough private benefits to incentivise it to lead the reform process. The proposed new powers will enable Ofgem to make multiple, coordinated changes to industry codes for the purpose of the reforms. This will enable Ofgem to lead the delivery of the programme whilst simultaneously ensuring that the programme's objectives are met through effective coordination.
42. While Ofgem takes decisions on whether to approve a modification at the end of the process, outside of the enhanced SCR process it is very limited in the role it can play in coordinating modifications during their development. While Ofgem has some scope under some of the codes to influence timings, it does not control the modification process or timetable and neither can it make or propose changes to modifications during their development (outside of the enhanced SCR process).
43. There is a currently a need to coordinate changes:
 - Across codes;
 - Across codes and licences;
 - Between the changes being agreed and go-live as new issues are discovered; and
 - After go-live to resolve issues in live operation.
44. Ofgem anticipate that once the initial tranche of modifications for new settlement arrangements have been made, there will be the need to consider further changes at short notice through the implementation phase and after go-live. Ofgem would not be able to use its SCR powers here given the notice periods and published process. It would be reliant on the industry-led code modification process. As above, while changes can be raised by industry parties with an urgent status, Ofgem is not able to raise and coordinate any required changes which could have impacts for consumer and industry experience in operating the new arrangements.

2.2 Rationale for the proposed code modification appeals process

45. Under the Energy Act 2004, market participants who wish to challenge Ofgem's decisions on proposed industry code changes may appeal to the CMA.¹⁰ There are exclusions from this right of appeal where Ofgem are either:
 - In agreement with the majority recommendation of the code's governing panel
 - Consider that the delay caused by holding an appeal is likely to have a material adverse effect on the availability of electricity or gas for meeting the reasonable demands of consumers in Great Britain.
46. Under the proposed new powers, this CMA appeal route for code changes would not be available. However parties would be able to challenge decisions made under the legislation through Judicial Review (JR).
47. It is considered that JR will be appropriate as Ofgem intends to work closely with industry parties in developing the code modifications to ensure a sufficient level of input from industry experts in developing the new arrangements for electricity settlement. By working closely with industry, with appropriate consultation and impact assessment procedures as required by the proposed

¹⁰Ofgem, 2015, Industry Codes work, [web], available at:
<https://www.ofgem.gov.uk/licences-codes-and-standards/codes/industry-codes-work>

legislation, Ofgem intend to ensure adequate scrutiny and expert input in its development of the new arrangements. This will help secure industry support, at the end of this phase, for the code and licence modifications that will be made. The new powers are therefore expected to incentivise industry to work closely with Ofgem during the pre-implementation phase to ensure effective policy development, which will reduce the scope for industry to appeal the policy at a later stage. The risk of sub-optimal policy development as a result of inadequate scrutiny and/or expert input, due to the loss of the CMA appeal route, is therefore considered to be limited.

48. While the risk of an appeal is low, for the reasons described above, the power for Ofgem to make code changes directly removes the 'safeguard' of the code panel vote. This safeguard prevents parties from appealing code modification decisions to the CMA when the decision represents the consensus of industry, as reflected in the decision of the relevant code panel. Without the code panel recommendation, it is possible that one party who opposes the reforms could launch a spurious appeal to the CMA and delay the programme. In addition, the CMA appeal enables parties to challenge one element of a proposal, rather than the proposal in its entirety. This could mean that there is more scope for a party opposed to the reforms to find an aspect of the policy in relation to which the CMA would accept an appeal, regardless of the robustness of the overall package of reforms.

49. In the circumstance of an appeal being raised, Ofgem estimates that the impact on the programme could be as follows:

- Within 15 working days of the code modification decision, a party can launch an application for permission to bring an appeal to the CMA.
- At this point, the programme would have to pause to consider the impact of the appeal on other areas of work. It is possible that related policy or design work would have to be halted while the appeal is underway. At a minimum, a risk assessment would need to be conducted of the options for continuing to develop aspects of the programme while the appeal is being considered. There is a chance that the entire programme could be halted
- The CMA can suspend the particular decision being appealed, prior to the outcome of the decision
- The CMA is expected to reach a final decision in approximately three months from the date of the code modification decision. While some work may be able to progress while the appeal is underway, key milestones such as the agreement of design baselines, consultation and decisions will not be able to progress until the appeal is concluded
- This could mean that if the appeal is raised close to a milestone or phase end being reached, this milestone or phase end could be delayed by at least the length of time for the appeal to be considered, and likely to be longer.
- This would delay the progression of the programme and, ultimately, the delivery of the reforms. It would also increase the costs of the programme.

50. The impact outlined above would be similar in the case of a JR¹¹. However, an appeal route is required to meet requirements under European legislation, in addition to the general principles of good regulation, and we consider that the JR would be sufficient for these purposes.

2.3 Rationale for the amended licence modification 'standstill period'

51. It is likely that, to deliver the reforms, a number of licence and code modifications would need to be made in parallel. Given the scale of complex changes required, it is expected that, once the main suite of code and licence changes have been made, additional, smaller changes will be needed during the 'design, build and test' (pre-implementation) phase, and after go-live (see section 5.1 for more detail on these phases).

¹¹ The timescales for JR appeal are likely to be longer, with a claim form required to be lodged by the applicant as soon as possible, but in any event within three months of the decision that is being appealed.

52. In some circumstances, Ofgem will need to make urgent modifications to codes and licences, for example, to address an issue that has arisen in testing or after the new arrangements have gone live. The need for a revised time period which is shorter than 56 days could arise from:
- The need to align new code and licence modifications with planned IT systems releases as part of the testing and implementation of the reforms. For example, if a systems release is scheduled for before the 56 day period expiry period, the programme would not be able to take advantage of the scheduled release to implement the urgent changes. This means it would be necessary to wait longer for the next planned release, or plan a new, bespoke systems change, which would add time and cost to the programme.
 - The risk of not being able to make urgent changes to licences, or combined changes to licences and codes, in the event of an issue being identified that could place the customer, or the integrity of the new arrangements, at risk.
53. In this situation, it is proposed that Ofgem have the power to reduce, in consultation with industry, the length of time of the standstill period after which a licence change may come into effect. However, it is assumed that unless the circumstances of the programme require it, the 56-day period will be the default period after which licence modifications are effective.
54. The benefits of this change would be to enable rapid action to be taken in response to an issue that presents risks to consumers, or the integrity of the new arrangements. Reducing the 56-day period would allow these risks to be addressed more quickly, and enable better coordination of code and licence changes that are made in tandem.
55. There is currently no alternative means for urgent licence changes to be made. When Ofgem makes a licence change, it can include powers of direction – that is, powers to subsequently direct licensees to do specific things to meet the policy objective of the licence change that has been made. This is a mechanism to deal with uncertainty. However this power of direction is limited and may not be able to cover all the circumstances under which an urgent licence modification might be required. Having a shorter standstill period will enable Ofgem to make changes more quickly to address issues that cannot be tackled through Ofgem’s powers of direction.
56. The requirement for Ofgem to consult with industry on an appropriate alternative standstill period provides a safeguard against licence changes being imposed more quickly than 56 days without justification. It is also a means for parties to make representations to Ofgem on the issue, which Ofgem must take into account.

2.4 Rationale for the time and scope limit of the proposed powers

57. The proposed primary powers will only be used for the settlement reform programme. However it should be noted that in May 2015, Ofgem issued an open letter seeking views on the case for a further review of the SCR process in general¹² and stated that:
- *‘In the context of the anticipated scale of change required in the coming years, we continue to have concerns that the arrangements may not be operating in the best interests of consumers. We consider it is timely to review the reforms we have implemented and potentially introduce further reform to the arrangements.’*
58. In the letter, Ofgem noted that each of the previous SCR processes’ timescales had been delayed and hence requested views on the factors that may have driven the delays as well as views on how both Ofgem and Industry stages of the process could be streamlined.
59. The CMA also considers that the current arrangements need to be improved and has recommended reforms to the process.¹³ Hence, though the proposed powers will only be used for settlement

¹² Ofgem, 2015, Open letter on Further Review of Industry Code Governance [web], available at: <https://www.ofgem.gov.uk/sites/default/files/docs/2015/05/cgr-open-letter.pdf>

¹³ CMA, 2016, Energy Market Investigation: summary of final report, page 77-78 [web], available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/531157/Energy-final-report-summary.pdf

reforms, work is currently underway to consider longer-term reforms to the current code governance arrangements.

60. The proposed powers will be time limited to five years from commencement to reduce the regulatory risk for the market and ensure that the powers are not in place for longer than is necessary to deliver the objectives being sought.

2.5 Summary

61. In summary, the rationale for the use of the proposed time and scope limited powers is to overcome the existing issues with incentives and coordination by:

- a. Streamlining the pre-implementation phase;
- b. Minimising the potential risk of delay associated with the SCR process; and
- c. Enabling Ofgem to take on the leadership role to ensure that the whole process is coordinated effectively.

62. The proposed powers may also enable the expedited implementation of the reforms which will help deliver the consumer and competition benefits outlined in the preceding sections, meaning that any net benefits from the proposed reforms are delivered sooner.

63. The potential impacts of the proposed powers are discussed in more detail in Section 4.

3. Policy Objectives

64. The overarching objective is to reform the electricity settlement processes to enhance competition and increase consumer choice/engagement. The primary policy objective associated with the new powers is to establish a new (time and scope limited) regulatory regime which enables Ofgem to facilitate the implementation of the settlement reforms in a timelier, more coordinated and more cost-effective manner which ensures better outcomes for both consumers and industry, relative to the existing arrangements.

65. The primary objective outlined above, supports the UK Government's plan of action to guarantee clean, affordable and secure energy, as the new time-limited powers will:

- Ensure that the key policy objective of electricity settlement reforms is achieved (promoting a more dynamic and efficient energy market); and
- Minimise the resource costs and risk of delay in the pre-implementation phase.

66. Hence, the proposed powers are intended to ensure a better outcome for both consumers and industry as the powers are expected to promote a more efficient reform programme for half-hourly electricity settlement.

4. Description of options considered

67. Two options were considered:

- a. Option 1: A '**Do Nothing**' option was ruled out on the basis that it is unlikely to achieve the policy objectives. Under this approach Ofgem would not have the powers to ensure that settlement reforms are delivered in a timely, coordinated and cost-effective manner that ensures better outcomes for consumers (due to risk of derailment or delay).
- b. Option 2 : The '**Preferred Option**' is the introduction of time-limited primary powers that will allow Ofgem to use a more streamlined process than an SCR to make changes in a timely way to require suppliers to settle electricity balances with consumers on the basis of actual half-hourly consumption data

68. Option 2 is the preferred option as it ensures that settlement reforms are delivered in a timelier and more cost-effective manner that ensures better outcomes for both consumers and industry relative to the existing arrangements.

i. *Details of the proposed time-limited primary powers*

69. The proposed powers will enable industry codes to be modified directly by Ofgem so as to facilitate expeditious and coordinated changes to industry codes. The new powers will also amend the existing appeals processes (for code modifications available to industry) from two appeals processes (CMA and Judicial Review) to one (Judicial Review only) as this is the default appeals process for new legislation. The new powers will also require Ofgem to produce an impact assessment when making code changes. The new powers will allow Ofgem to reduce the licence modification standstill period from 56 days where it is deemed necessary.

70. The powers will be time-limited: the powers will only be exercisable for 5 years starting from commencement of the powers.

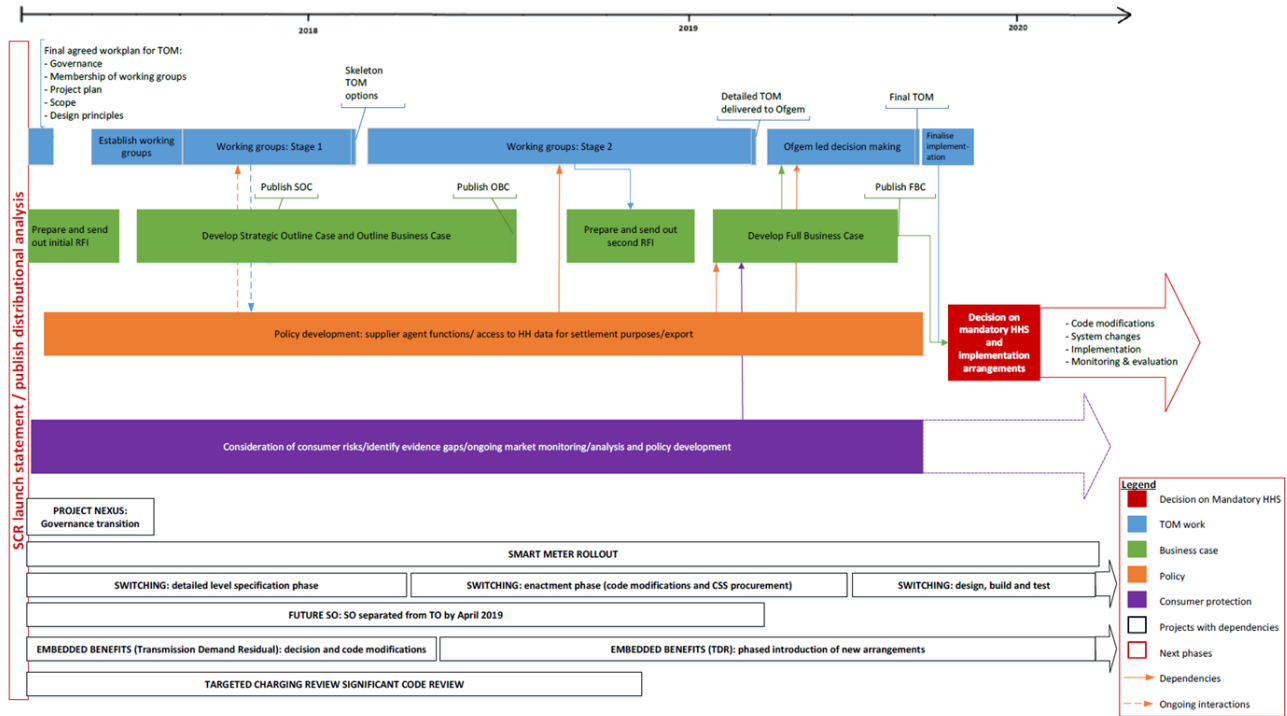
5. Monetised and non-monetised costs and benefits of each option

71. The proposed powers will enable Ofgem to facilitate the settlement reforms as outlined in Section 4. There are no immediate costs or benefits associated with the proposed primary powers as the powers are broad enabling powers and hence will not affect the nature of regulation in the sector until the scope of its use has been defined by Ofgem for settlement reforms.
72. However, given that Ofgem is likely to use these powers to directly modify industry codes instead of using the current SCR process, consideration has been given to the potential impacts on both industry and Ofgem of the new code modification process, in the form of an indicative quantitative and qualitative assessment. In addition, given the degree of uncertainty related to the overall quantitative impact of the actual settlement reforms at this early stage of policy development, consideration has been given to the potential subsequent impacts of the reforms in the form of a qualitative assessment.
73. The indicative quantitative assessment in this IA considers the potential costs/benefits to business and Ofgem of exercising the new powers. This does not reflect the immediate impact of the primary powers. The proposed powers will require Ofgem to conduct an impact assessment when enacting code modifications for the purposes of settlement. While the assumptions underpinning the indicative analysis are subject to a range of uncertainty, they have drawn on Ofgem's current views of how the new powers are likely to operate in practice and Ofgem's current view of the resource requirement for the pre-implementation phase that will be directly affected by the proposed powers.
74. The potential impacts of the proposed powers on industry and Ofgem in the pre-implementation phase and the potential subsequent impact during the implementation phase of the reforms are considered in turn. The range of indicative quantitative assessments is summarised in Table 4.
75. Overall, under the central case the current assessment suggests that the potential additional costs to industry and/or Ofgem are likely to be negligible as a result of exercising the new powers. The assessment suggests that the overall potential impact of the new powers on both industry and Ofgem is likely to be net beneficial.
76. It should be noted that there is some uncertainty around the quantified impacts of the new powers relating to the risk of delay in the 'do nothing' (counterfactual) option. Where appropriate, the ranges or sensitivity analysis aims to reflect the current level of uncertainty around the potential direct impacts of the powers. It should also be recognised that there is considerable uncertainty at this stage around the potential impacts on the actual implementation of the reforms as they will largely be determined by subsequent policy development by Ofgem. This assessment should be viewed as indicative at this stage; the quantified assessment of the actual implementation of the reforms will be further clarified in a subsequent IA from Ofgem.
77. By definition, there are no additional impacts associated with the 'do nothing' (counterfactual) option.
78. This section outlines the monetised and non-monetised benefits/costs associated with Option 2 (the preferred option).

5.1 The do Nothing Option

79. Table 1 below illustrates the high-level timeline for the electricity settlement reform programme.

Table 1: Indicative Ofgem Electricity Settlement Reform Programme phases¹⁴



80. The steps in this timetable show the products that will need to be developed to enable Ofgem to reach a final decision on market-wide half hourly settlement by the second half of 2019. In autumn 2017 Ofgem and industry began detailed work on a Target Operating Model (TOM). The timetable will be kept under review depending on the development of the TOM and the policy decisions that are taken. Ofgem intends to reach a decision on if, when and how market-wide half-hourly settlement moves forward into the delivery phase by the second half of 2019. This phase would begin with code modifications and rule changes to implement the conclusions of the design work, requiring cross-code co-ordination to deliver the necessary code changes. Changes would then be made to ELEXON's central systems, suppliers' own systems and systems of any other relevant parties, as well as the processes for transfer of data to manage the changes brought about by market-wide half-hourly settlement. Moving consumers over to half-hourly settlement would follow this, with the arrangements for this transition to be developed over time as the design work progresses and to be set out fully in the final TOM and Business Case.

5.2 Option: Additional powers to Ofgem – The 'Do Something' (Preferred) Option

81. As outlined in Section 3, the primary powers are expected to:

- **Ensure that the policy objectives of the reforms are achieved**, as the new powers will enable Ofgem to take on the necessary leadership and coordination role; and
- **Minimise the resource requirement/reduce the risk of delay associated with the SCR process** in the pre-implementation phase relative to the counterfactual for both Ofgem and industry. Under the SCR process, delays would be more likely to occur in the pre-implementation phase, which in turn would have meant an increase in resource costs for both

¹⁴ See:

https://www.ofgem.gov.uk/system/files/docs/2018/01/appendix_1_significant_code_review_timeline_consultation_feedback_summary_and_scope.pdf

Ofgem and industry. In addition, as Ofgem will be leading and coordinating the process, it is expected this will result in a more streamlined approach.

82. The subsequent sections will set out the potential impacts of the proposed powers in the following way:

- a. Ofgem's leadership role (qualitative assessment);
- b. Streamlined pre-implementation phase (quantitative assessment);
- c. Expedited delivery of the actual settlement reforms (qualitative assessment); and
- d. Amended appeals process (qualitative assessment).

a. Ofgem's leadership role

83. The new powers are expected to address the restrictions under the SCR process, in relation to developing and making modifications throughout the process. The new powers will enable Ofgem to take on the necessary leadership and coordination role across industry codes for the entirety of the implementation phase and will enable Ofgem to lead the delivery of the programme whilst simultaneously ensuring that the programme's objectives are met through effective coordination.

84. It has not been possible to quantify the benefit of potentially addressing the existing lack of coordination across codes, nor to provide a robust qualitative order of magnitude. However it is expected that this change could result in a reduction in the resource requirements (for both Ofgem and industry) associated with the delivery of the settlement reform programme as a result of the enhanced coordination. This is because better coordination of the whole process could potentially reduce any existing inefficiencies associated with the SCR process. This change is expected to be net beneficial relative to the existing arrangements.

b. Streamlined pre-implementation phase

85. The new powers are expected to reduce the length of time that the pre-implementation phase would take under the SCR process and hence reduce the resource requirement associated with this phase of the settlement reform programme. We judge the risk of further delays by industry limited given control over timings by Ofgem with the new powers.

86. The new time-limited powers would allow Ofgem to develop the code modifications with industry, to consult on them and then issue a decision without the need for the formal industry change process outlined above at any time during the implementation of settlement reforms. Consequently, it is expected that the new powers will reduce the length of the pre-implementation phase.

87. For the settlement reform programme, avoiding the formal industry change process for modifying industry codes is expected to reduce the pre-implementation phase (for both Industry and Ofgem) by around 7.5 months relative to the counterfactual.

88. Table 2 outlines the length of the previous SCR processes. While the timings may vary depending on the complexity of the issues, Ofgem's expectation, when the SCR process was developed, was that the process would take up to 18 months. However the actual duration of previous SCR processes has been around 32-44 months.

Table 2 Previous SCR processes.¹⁵

	SCR Launch Date	Ofgem Direction	Panel Recommendation	Code Modification decision	Total Duration
Gas Security of Supply	Jan-2011	Sep-2014	n/a*	n/a*	44 Months
Electricity Transmission Charging (Transmit)	Jul-2011	May-2012	Jun-2013	Jul-2014	36 Months
Electricity Balancing	Aug-2012	May-2014	Mar-2015	Apr-2015	32 Months

* no industry led process/panel as Ofgem directed changes to the UNC using powers under s.36C of the Gas Act

89. The new powers may also reduce the risk of delay associated with the current SCR process. We have quantified the potential reduction of this risk as set below.

90. For the settlement reforms programme, it is considered appropriate to assume an expected delay to the pre-implementation phase under the SCR process of around 6 months

91. Consequently in addition to the expected resource savings identified in Paragraph 87, given that it is highly likely that the pre-implementation phase would have been delayed in the counterfactual the new powers are expected to reduce the pre-implementation phase relative to the counterfactual by a total of 13.5 months for the settlement reforms programme (6 months for the expected delay savings and 7.5 months for the expected resource savings from avoiding the industry change control process).

92. Table 3 outlines the assumptions underpinning the scenarios used in this IA.

Table 3: Summary of scenarios for settlement reforms programme*

Settlement reforms programme			
Assumption	Low scenario	Central	High Scenario
Resource saving: Industry change control process	7.5 months	7.5 months	7.5 months
Resource saving: Potential SCR delay	0 months	6 months	12 months
Total Resource saving:	7.5 months	13.5 months	19.5 months

* Resource savings assumed to accrue in the pre-implementation phase only

93. It should be noted that there is a considerable level of uncertainty associated with the assumed central case resource savings associated with minimising the risk of delay associated with the SCR process, given the small number of previous SCR processes that the assumption is based on and given Ofgem’s enhanced SCR powers are as yet untested. As such it is considered appropriate to include both low and high scenarios to reflect the level of uncertainty. The 7.5 month assumption related to the savings from the industry change control process is based on Ofgem’s plans and hence no scenarios have been used for this assumption.

94. Table 4 outlines the expected total savings for the settlement reforms over an appraisal period of five years. Given the early stage of policy development for the programme of reforms there is some uncertainty surrounding the period over which the potential savings outlined below will likely be accrued. For the purpose of this IA, to demonstrate that the savings will be accrued in the future, we have assumed that the savings will be accrued evenly over 2 years (2020 & 2021) for the programme of reforms (the last two years of the appraisal period).

¹⁵ Ofgem, 2015, Open letter on Further Review of Industry Code Governance [web], available at: <https://www.ofgem.gov.uk/sites/default/files/docs/2015/05/cgr-open-letter.pdf>

95. The monthly resource cost estimates are based on Ofgem's best view (given previous SCR experiences) of the resource requirements in the pre-implementation phase under the SCR process. Further information on the assumptions underpinning the resource estimates can be found in Paragraph 74 (the assumptions section).

Table 4: Summary of the expected total savings*

Settlement Reforms			
<i>Assumptions</i>	Low	Central	High
Resource savings (months): Ofgem	-7.5	-13.5	-19.5
Resource savings (months): Industry	-7.5	-13.5	-19.5
Monthly resource cost (2015 prices, undiscounted): Ofgem	£57,000		
Monthly resource cost (2015 prices, undiscounted): Industry	£108,000		
Total Saving (2015 prices, undiscounted): Ofgem	£420,000	£760,000	£1,100,000
Total Saving (2015 prices, undiscounted): Industry	£810,000	£1,460,000	£2,110,000
Total Saving (2015 prices, discounted 2015 PV): Ofgem	£380,000	£680,000	£980,000
Total Saving (2015 prices, discounted 2015 PV): Industry	£720,000	£1,300,000	£1,870,000

* Totals may not sum due to rounding.

96. In the central scenario, for industry, the new powers could result in discounted benefits of around £1.3 million (2015 prices) for the settlement reforms programme as a result of the reduction in the resource requirement under the pre-implementation phase. The potential estimated discounted benefits for Ofgem is around £0.7 million (2015 prices).

97. Given the level of uncertainty around the expected resource savings associated with minimising the risk of delay associated with using the current SCR process,¹⁶ a range based on high/low scenarios has also been provided. Under the high/low scenarios the potential estimated discounted industry savings are between £0.7 – 1.9 million (2015 prices) for the settlement reforms programme as a result of the reduction in the resource requirement under the pre-implementation phase. The potential estimated discounted Ofgem savings are between £0.4 – 1.0 million.

c. Expedited delivery of the actual settlement reforms

98. As outlined in Section 3, the new powers would enable Ofgem to facilitate the implementation of the settlement reforms in a timelier, more coordinated and more cost-effective manner which ensures better outcomes for both consumers and industry relative to the existing arrangements. The previous sections outlined the potential impacts of the enabling powers.

99. It is expected that the settlement reform programmes will have a positive Net Present Value (NPV), hence the impact of bringing forward the delivery date by 13.5 months is expected to be net beneficial (all else being equal). The NPV is expected to be positive as the overarching objective of the reforms is to address the existing barriers to consumer engagement, consumer choice and competition in the most cost-effective manner. The benefits of the reform programme will be further clarified in a subsequent IA(s) produced by Ofgem.

d. Amended appeals process

100. The proposed powers will provide for appeal only by Judicial Review (JR) and not to the CMA, as is currently the case when Ofgem reject a panel recommendation. However, it is considered that JR will be sufficient as Ofgem will be working closely with industry to develop the new arrangements and intend to ensure adequate scrutiny and expert input through extensive consultation with industry parties. Ofgem will also be required to produce an impact assessment when making code changes. This should help secure industry support, at the end of this phase, for the code and licence

¹⁶ The SCR process Ofgem is using for settlement reform is an Ofgem-led end-to-end process where Ofgem will raise and make code changes. However, even with this updated SCR process, there is a risk of delay to making further code changes should further issues arise later during implementation.

modifications that will be made. The new powers are expected to reduce the scope for industry to appeal the policy at the end of the pre-implementation phase, but the powers will also incentivise industry to work closely with Ofgem during the pre-implementation phase to ensure effective policy development. The risk of sub-optimal policy development due to the loss of the CMA appeal route is therefore limited. It has not been possible to quantify this change nor to give a robust qualitative order of magnitude of the impact. However, it is considered that the overall potential impact of this change will be negligible, as the JR will remain and industry will still be able to challenge the policy throughout the pre-implementation phase.

e. Reducing licence modification standstill period

101. The proposed powers will allow Ofgem, in consultation with industry to reduce the length of time of the standstill period after which a licence change may come into effect. It is assumed that unless the circumstances of the programme require it, the 56-day period will be the default period after which licence modifications are effective. Therefore, while it has not been possible to quantify the impact of this change, in the circumstances where it allows licence modifications to take place in a more time efficient manner, we expect that the impact of this powers will be net beneficial.

5.3 Summary of monetised/non-monetised Estimates

102. It should be noted that this is a current assessment of the potential costs and benefits to business but the direct impacts will depend on subsequent operational directions to be provided by Ofgem. It is considered that these primary legislative enabling powers will not, by themselves, alter the regulatory burden on business.

103. We have monetised as far as possible the possible impacts and included a qualitative assessment of the potential indirect impacts of the new provisions. The potential impacts are however uncertain at this stage of policy development and therefore the ranges (where presented) should be viewed purely as indicative of the potential magnitude of benefits which may accrue.

- Quantitative assessment

104. In summary, the proposed powers are expected to shorten the pre-implementation phase by around 7.5 months and to reduce the risk of delay in the counterfactual by around 6 months in the central case. Under the central case over a five year appraisal period, the discounted potential savings (2015 prices) for Ofgem are expected to be around £0.7 million. The discounted potential savings (2015 prices) for Industry are expected to be around £1.3 million.

- Qualitative assessment

105. In addition to the potential benefits from the streamlined pre-implementation phase which have been outlined in the preceding section, the proposed powers are expected to address the lack of coordination that would result from the need to rely on an industry-led change process during the lifetime of the programme. It has not been possible to quantify this benefit however it is expected that this change could result in a reduction in the resource requirements (for both Ofgem and Industry) associated with delivering the reforms programme as it could potentially reduce any existing inefficiencies associated the existing SCR process. This change is expected to be net beneficial relative to existing arrangements.

106. It has not been possible to quantify the earlier implementation date for the actual settlement reforms however it is expected that the programme will have a positive NPV. Hence the impact of bringing forward the delivery date of the reforms by 13.5 months is expected to be net beneficial (all else equal).

107. It has not been possible to quantify the change to the existing appeals process, however it is considered that the overall potential impact of this change will be negligible, as the JR will remain and industry will still be able to challenge the policy throughout the pre-implementation phase.

108. Finally it has not been possible to quantify the impact of the reduction in the licence modification standstill period. The impact is likely to be relatively small, however where this allows the process to

take place in a more time efficient manner, we would expect this change to have a net beneficial impact.

5.4 Assumptions

109. The following assumptions were used in the analysis:

- The NPV base year is 2017, a 3.5% real discount rate is used and all values are expressed in 2015 prices.
- Subject to Parliamentary approval, the powers are assumed to come into force by mid-2019, and the resource savings have been assumed to accrue evenly over 2020 & 2021 (though the policy is still at an early stage of development, this period is uncertain).
- Appraisal period: 5 years

110. Tables 5 and 6 outline the assumptions underpinning the monthly resource costs used in Table 4 for both Ofgem and Industry¹⁷.

FTEs	Aggregate Monthly resource cost (including ENIC) ¹⁹	Aggregate daily resource cost ²⁰
11	£57,000	£3,000

Detail	Number per annum	Number of attendees	Working days	Annual Salary (including ENIC) ²²	Daily resource cost ²³	Monthly Resource cost ²⁴
Working groups	63	15	2	£78,000	£600	£95,000
Meetings	13	20	1	£78,000	£600	£13,000
				Total	£6,000	£108,000

- Risks and uncertainty

111. It should be recognised that there is considerable uncertainty surrounding the estimated impacts presented in this IA. They are indicative in nature and will be considered in the subsequent Impact Assessment(s) that will accompany Ofgem's policy development.

¹⁷ Totals may not sum due to rounding.

¹⁸ Assumptions provided by Ofgem. These are unchanged from the previous IA published in 2016.

¹⁹ Monthly rates were calculated assuming 220 working days or 18 working days per month.

²⁰ Daily rates were calculated assuming 220 working days per annum.

²¹ Assumptions provided by Ofgem.

²² Salaries are based on the Annual Survey of Hours and Earnings (ASHE) Office for National Statistics (corporate managers), an uplift factor was applied to the salary assumptions to account for the additional employment costs that employers incur (ENIC, superannuation and accommodation costs).

²³ Daily rates were calculated assuming 220 working days per annum. This includes around £250 per day per person as a conservative estimate for non-staff costs: travel, travel, hotels etc.

²⁴ Monthly rates were calculated assuming 220 working days or 18 working days per month.

6. Direct costs and benefits to business (OITO methodology)

112. The One-in, Two-out (OITO) rule ensures that any new regulatory measure that is expected to result in a direct net cost to business and civil society organisations must be offset by compensatory deregulatory measures providing savings to business of at least double that amount.
113. While the policy is in scope of the OITO rule, the introduction of powers in primary legislation will not result in immediate impacts on business and therefore should be considered as zero net cost. Where possible this Impact Assessment provides estimates of the potential impacts associated with implementing the proposed powers. As outlined in the preceding section, in the central case over a five year appraisal period, the potential savings (discounted, 2015 prices) for Industry are expected to be around £1.3 million.
114. The estimates are however subject to significant uncertainty. Ofgem will prepare final Impact Assessments for the settlement reforms programme which will present a holistic assessment of the impacts associated with the delivery of the reform programmes. However given that Ofgem is the regulator, it will not be required to assess the overall impact on business as a result of the new powers for the purposes of OITO.

7. Wider impacts

115. The proposed primary powers are enabling powers; hence the proposed legislation will not result in any immediate wider impacts.
116. However, the key potential wider impact of the proposed powers is enhanced competition in the energy market sooner than would be delivered under the do nothing option. The proposed powers will enable Ofgem to deliver the reform programme more efficiently relative to the counterfactual.
117. The actual implementation of the reform programmes is expected to open up opportunities for time-of-use tariffs and demand-side response. These reforms are expected to:
- a. Increase customer engagement/consumer choice; and to
 - b. Promote a more even playing field for suppliers to compete more effectively.
118. The increase in customer engagement/consumer choice and the increase in the ability of suppliers to effectively compete together are expected to promote a more dynamic and efficient energy market which would benefit consumers and market participants.
119. Moreover the increase in customer engagement could result in overall reductions in energy consumption which could deliver further environmental benefits.
120. The potential wider impacts outlined above will be further clarified in the subsequent IAs to accompany the proposed settlement reforms which will be produced by Ofgem.

8. Rationale and evidence that justifies the level of analysis

121. The analysis contained in this Impact Assessment is considered proportionate at this stage of policy development. The analysis sets out preliminary estimates of the potential impacts associated with the implementation of the proposal as a whole. The appraisal period of 5 years is considered an appropriate time horizon for providing an initial assessment for the potential costs and benefits associated with the proposed primary legislation. The key analytical risks and uncertainties have been identified. The monetised impacts presented in this impact assessment are indicative in nature and will be revisited in due course as necessary to reflect further policy development by Ofgem.

9. Small and Microbusiness Assessment (SMBA)

122. The exact number of small or microbusinesses (defined as having up to 49 FTE and 10 FTE employees respectively, as per BIS Better Regulation Framework Manual) that the proposed provisions will affect is uncertain. However, both types of companies operate in this sector.
123. The Government believes that including businesses of all sizes in the policy will promote a higher level and more effective co-ordination by the new Regulator and will allow extracting the maximum benefit from the implementation of the provisions. Given that the proposed powers are enabling powers, there are no immediate impacts expected for small and microbusinesses. We do not expect small and micro businesses to be disproportionately impacted in exercising these enabling powers.
124. It is expected that small and microbusinesses could also benefit from the resource savings identified in Section 5 as a result of the timelier and more cost effective programme. The intention is not to impose any disproportionate burden on companies of any size.

10. Summary and preferred option with description of implementation plan

125. In summary, Option 2 is the preferred option rather than the 'Do nothing' option. Option 2 would involve new primary powers for Ofgem as this would enable Ofgem to facilitate the delivery of the reforms in a timelier, more coordinated and more efficient manner. As enabling powers, there are no immediate monetised costs or benefits to business associated with this stage of the implementation. Indicative potential costs and benefits of implementing the provisions have been assessed so far as possible at this stage. Further IAs will be produced as the policies are developed further.
126. As with any other use of public resources, it is important to monitor performance and review the service routinely. The policies outlined in this Impact Assessment have a review date of 2022.

Appendix A: Summary of the key documents referred to in this Impact assessment

Title	Scope	Status
Ofgem, 2014, Electricity settlement reform – moving to half-hourly settlement	After a period of scoping Ofgem considers that is in consumers' interests to be settled against their half-hourly consumption data. In this document, Ofgem explains its' reasoning and sets out its' plans for examining how this can be achieved through the settlement project.	Published, can be found at: https://www.ofgem.gov.uk/sites/default/files/docs/2014/04/electricity_settlement_launch_statement_0.pdf
Ofgem, 2015, Update on electricity settlement project	This document provides an update on Ofgem's electricity settlement reforms project.	Published, can be found at: https://www.ofgem.gov.uk/sites/default/files/docs/2015/01/settlement_final_doc.pdf
Ofgem, 2015, Open letter on Further Review of Industry Code Governance	This letter outlines Ofgem's concerns with the existing industry code governance arrangements. The letter also seeks views from stakeholders on the issues with the existing arrangements and how best to overcome them.	Published, can be found at: https://www.ofgem.gov.uk/sites/default/files/docs/2015/05/cgr-open-letter.pdf
HM Government, 2016, Draft Measures: Fast and reliable switching and Half-hourly electricity settlement power(s) Impact Assessment	This Impact Assessment was published alongside draft powers on faster switching and half-hourly settlement that were considered for pre-legislative scrutiny in 2016.	Published, can be found at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/493713/Impact_Assessment_-_Draft_Measures_-_Fast_and_Reliable_Switching_and_Half-hourly_Electricity_Settlement_Power.pdf
CMA, 2016, Energy market investigation – summary of final report	This document is a summary of the CMA's final recommendations.	Published, can be found at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/531157/Energy-final-report-summary.pdf
HM Government/Ofgem, 2017, Upgrading Our Energy System: Smart Systems and Flexibility Plan	This document outlines 29 actions the government, Ofgem and industry will take to remove barriers to smart technologies (such as storage and demand-side response); enable smart homes and businesses; and improve access to energy markets for new technologies and business models.	Published, can be found at: https://www.gov.uk/government/publications/upgrading-our-energy-system-smart-systems-and-flexibility-plan
Ofgem, 2017, Electricity Settlement Reform Significant Code Review: Launch Statement	This statement launches the Electricity Settlement Reform Significant Code Review and sets out Ofgem's revised timetable following the consultation on the plan for market-wide half-hourly settlement (HHS) in November 2016.	Published, can be found at: https://www.ofgem.gov.uk/publications-and-updates/electricity-settlement-reform-significant-code-review-launch-statement-revised-timetable-and-request-applications-membership-target-operating-model-design-working-group

Appendix B: Glossary

BSC	Balancing and Settlement Code
CMA	Competition and Markets Authority
ENIC	Employer's National Insurance Contributions
EANCB	Equivalent Annual Net cost to Business
IA	Impact Assessment
Ofgem	Office of Gas and Electricity Markets
OITO	One In Two Out
SCR	Significant Code Review
SEC	Smart Energy Code

Appendix C: SCR process: background

The Significant Code Review (SCR) mechanism enables Ofgem to:

- i. direct licensee(s) to make changes to relevant industry codes to deliver outcomes specified in an SCR Direction made by Ofgem.
- ii. raise modifications itself at the end of an SCR, to be developed through the normal industry processes
- iii. lead an end to end SCR process to deliver detailed proposed code change at the end of the SCR

The SCR process was introduced by Ofgem following their Code Governance Review (CGR) which concluded in 2010 and was then extended to cover all of the industry codes in 2013, following the conclusion of the second phase of CGR (CGR2). Under the third phase of the Code Governance Review (CGR3), Ofgem introduced changes to the SCR powers to give it the three delivery options set out above (previously, only option i. above was available).

The SCR process was introduced by CGR to enable Ofgem to lead holistic reviews, to deliver complex and/or cross code changes. Ofgem set out in their March 2010 final proposals document that they would give as much notice as possible and consult with stakeholders before undertaking an SCR, where possible flagging it in their Corporate Plan. Ofgem also noted that they did not expect to undertake more than one or two SCRs per financial year.

Ofgem set out that the process may vary on a case by case basis according to the complexity or contentiousness of the issues at stake, and that they would keep this under review in light of experience of the SCR process. In addition, they set out that the precise duration of an SCR would also vary according to the complexity of the issue.

Following CGR3, Ofgem published updated guidance on the SCR process, which is available on Ofgem's website: https://www.ofgem.gov.uk/system/files/docs/2016/06/scr_guidance.pdf