

ENERGY BETTER REGULATION PROJECT

FINAL REPORT

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Executive Summary

The Energy Better Regulation Project was set up to engage with industry in examining energy regulation.

Project Objectives

- Review DTI's energy regulations
- Identify options for streamlining, simplification, consolidation and abolition of existing legislation
- Identify specific measures for the DTI Simplification plan
- Ensure the current regulatory framework is fit for purpose

The project team has worked in partnership with Ofgem to ensure that proposals complement Ofgem's better regulation work, which includes the major Supply Licence Review. The team has also worked with other government departments where appropriate, so that wider simplification agendas have been considered and proposals have been assessed by the most appropriate officials.

The key part of the team's role has also been to embed better regulation principles across Energy Group. A stronger adherence to these principles should create greater consistency in the Group's regulatory activities and ultimately more effective industry involvement in policy development and implementation.

Key findings

The project has been based on engaging with industry to get business' perceptions of regulatory problems and potential solutions in the energy sector. Therefore, the findings in this report represent a summary of industry feedback and its analysis.

There were a significant number of issues raised relating to OGDs (other government departments) and regulators, although we found relatively few specific areas for change within the DTI's remit of energy regulations.

A key theme raised during this exercise was the difficulty of achieving a joined-up approach to energy across government, given differing departmental policy objectives. Furthermore, rather than focusing primarily on changing existing legislation, the consensus was that scarce resource would be better utilised improving how future legislation is implemented and identifying opportunities to consolidate and amend out of date legislation as a specific consideration during that process.

Actions taken

- Improved awareness and use of better regulation best practice across DTI's Energy Group building on feedback from industry about need for better evidence base
- Established measures to make a contribution to better joined up working across government departments on energy regulation, including setting up a working group to look at regulation
- Actively worked with DTI's policy teams to ensure that specific proposals have been or will be taken forward
- Liaised with OGDs and regulators on specific issues raised which are part of their remit
- Improved internal and external Internet guidance
- Established ongoing point of contact in Energy Group on regulatory issues for industry
- Explored the value of repealing specific pieces of legislation

There were also a number of proposals that were not universally deemed to be sufficiently beneficial, following further analysis.

Future direction

The better regulation agenda is being embedded deeper in all government departments. A number of current reviews and consultations across Whitehall will provide ongoing opportunities to simplify regulation and reduce the burdens on business. To maximise the benefits of these and ensure the agenda is consistently applied, industry has a key role to play in using ongoing dialogue to inform and drive policy processes from inception through to implementation.

1. Introduction

This project is one piece of a much wider departmental better regulation agenda. It was initiated to explore the options and need for regulatory change within Energy Group's remit, with the aim of ensuring that Energy Group's contribution to the departmental Simplification Plan was as far reaching and robust as it could be. The objectives of the project were to look at options for simplification, including streamlining, consolidation and abolition of regulations where and if appropriate.

The DTI Simplification Plan

The DTI, along with all other government departments, is committed to producing and publishing a Simplification Plan during 2006. This will be a rolling programme setting out all the simplification measures that the department is undertaking in order to improve the regulatory framework and reduce overall burdens on business.

The DTI published a first draft on 29 November 2005, and formal publication of the final plan will be around the Pre-Budget Report 2006, when other departments will be publishing Simplification Plans in a similar timeframe. These final plans will include additional detail on how each department intends to meet targets on admin burden reduction.

The Simplification Plan will be revised and updated as appropriate to reflect the department's future measures with an expectation that there will be another iteration of the plan during 2007. Continued dialogue with industry will inform future entries for energy.

Within Energy, it was also considered a timely opportunity to review the current regulatory framework more broadly, with a view to streamlining and ensuring it is fit for purpose. The expectation was that the project team would then take forward interim actions over the summer and autumn, making final recommendations on further work by the end of 2006 as part of this report. The project has been run in partnership with Ofgem, as they are also working to apply better regulation principles within their remit in regulating the energy markets.

The main tenet of the project has been to understand and explore the issues and burdens as perceived by industry, in order to ensure that the recommendations generated address real concerns and propose actions that will make a tangible difference to the sector. Therefore, the focus of the project has been to seek direct input by talking to industry, both representative groups as well as individual businesses, bilaterally and through collective discussion forums. This opportunity for stakeholder input and consultation has continued throughout the lifetime of the project, even though in the interim report we ruled out holding a formal public consultation on the general findings and proposals as we felt it would not really add value to industry at that point.

Following feedback from industry, we have discussed specific issues in detail with the relevant policy officials in DTI and sought advice from other government departments about their policy areas.

The outcomes of the project were intended to dovetail with existing cross Whitehall work to map administrative burdens (the Admin Burdens Measurement Exercise carried out by consultants PricewaterhouseCoopers), and to incorporate the findings of that work so far as was relevant and practicable. However, we have not been able to do that as effectively as anticipated for a number of reasons. Firstly, that particular project has not yet formally reported, and secondly, the main admin burdens and associated costs identified as relating to the energy sector did not match the key regulatory concerns raised by industry. In addition, we have needed to allow for ongoing work arising from the Energy Review and not pre-empt outcomes of the Barker, Eddington and Davidson Reviews, which are yet to conclude.

The Administrative Burdens Measurement Exercise

The DTI's admin burdens were measured in a Whitehall-wide project carried out by PwC. Their report is complete and is due to be published alongside the Simplification Plan.

As part of this publication the DTI will announce its targets for reducing its admin burdens. These targets will be set for the department as a whole and Energy Group will have a role to play in helping to meet the targets.

We have discussed the high cost energy burdens identified with key industry stakeholders and the consensus so far has been that the individual burdens are not excessive for what the regulation is there to achieve. Nevertheless, future simplification measures and new regulation will have to include an assessment of the costs and benefits in terms of admin burdens in order that the DTI can accurately measure how it is performing against its reduction targets.

This report sets out the issues raised, the proposals to address those issues and our response in the short, medium and long term where appropriate. It is possible that formal consultation will be necessary before implementing some of the individual proposals in the future, but this would need to be considered on a case by case basis. Decisions for further prioritisation and action will be based on evidence of need, added value and more detailed cost benefit analysis. Industry will also be able to continue to input their views through a number channels including: simplify@dti, ongoing dialogue on a bilateral basis with specific policy leads, or through established stakeholder forums and via their Trade Associations.

2. Process and approach

The project has been run to maximise industry input. During the initial scoping phase the team met bilaterally with trade associations across the energy sector to explore high level issues and identify possible solutions. The team also met with a number of businesses and ran workshops with a cross section of stakeholders to address specific issues. The engagement strategy included the involvement of policy officials from within DTI and OGDs, regulators, academics and think tank representatives, as well as trade associations, lobby groups and

individuals from industry. Over the last few months we have also sought stakeholder views via informal consultation and have received feedback to the project interim report published in July.

Although the original project plan had allowed for the option of a formal public consultation to be held over the summer and autumn, on the basis of the range of issues raised, we decided that this was not the most useful route for engagement without having specific proposals for consideration. We propose that we continue to engage industry through ongoing informal dialogue beyond the conclusion of this project in order to maintain the momentum on simplifying energy regulation.

There may be a need in the future to consult formally on some of the proposals arising out of this project. However, this will only become apparent once those projects are under way and their scope becomes clear.

3. Project scope

The project was set up with the remit to look at those energy regulations which fall specifically within DTI's remit. However, recognising that the regulatory framework is much wider than merely DTI's responsibility, the project has been run in partnership with Ofgem to ensure that we minimise duplication, whilst allowing the project to have a broader scope.

Nevertheless, a significant proportion of the proposals and issues raised fall outside both DTI and Ofgem's combined remit; for instance planning regulations and environmental legislation which fall to DCLG and Defra respectively. There are also other regulators, notably HSE and EA, which impose regulatory requirements on industry. As the project team obviously could not commit to action on behalf of other bodies, we have focused instead on options for engaging jointly on the overarching cross government simplification agenda, and utilising existing avenues to ensure read across.

The better regulation agenda has gained momentum across government and is something that all departments will continue to focus on. As well as simplification of existing regulations, this will mean that new policies are implemented with a greater emphasis on better regulation principles, underpinned by consistent guidance. Therefore, it will be key for DTI and industry to continue liaising directly on the subject of regulation.

As part of the constant drive to improve regulation, industry will play a vital role in influencing government departments and regulators by utilising all available forums to raise issues and add input to policy making.

4. Project findings, issues raised and key themes

4.1 Summary of findings

The informal consultation process has highlighted that whilst the regulatory framework for energy is not perfect, it is far from being the overwhelmingly defective burden that is implied by the high level, widespread criticism of government that there is 'too much red tape'. Probing beneath this initial

reaction within the energy sector, we have found that in many cases, there are relatively few discrete problem areas from the better regulation perspective in DTI's remit of legislation.

As noted above, the majority of the specific issues raised come under the remit of HMT (taxation), Defra (environmental regulation), DCLG (planning issues) and Ofgem (licensing). Those that do fall to DTI Energy are either: related to the existing policy position (rather than the regulations implementing the policy); linked to process, engagement and implementation (again rather than to specific regulations); or are right down at the detail of specific wording and definitions, often in secondary legislation.

In some ways, for DTI's Energy Group, this is a positive message: there is significantly less than anticipated to consider in terms of change to primary legislation to remove or reduce burdens; but on the other hand, there are fewer obvious measures that will make an immediate or major difference to the energy industry overall. However, we recognise that this does not mean we can be complacent about the level of burden imposed by our regulation, and for this reason we are working to ensure we maintain effective dialogue with industry on this topic as an ongoing process of re-evaluation.

In summary, the issues raised broadly fall into a number of themes, themselves in two categories:

- a) those which are within DTI Energy Group's gift to address:
 - detailed sector specific concerns
 - implementation of better regulation approaches and principles
 - joined up government and access to information / policy development
 - more general legislative issues
- b) those falling outside the direct project remit:
 - Ofgem owned regulations
 - planning regulations
 - environmental issues
 - EU implementation and policy development

4.2 Key themes and proposals falling within DTI's remit

4.2.1 Sector specific concerns

a) Gas and Electricity

In the gas and electricity sectors, the licence exemption regime has been identified as an overly complex and burdensome area of regulation. In our interim report we proposed that both electricity and gas licence exemptions should be reviewed, with the purpose of clarification and simplification. In fact, electricity exemptions will be reviewed as part of the distributed generation workstream arising from the Energy Review. Although we recommend that gas exemptions should also be reviewed and simplified, rather than do so in isolation, we believe it will provide greater benefit if this is done once greater consistency between the two regimes can be achieved.

Therefore, we are intending to wait until the work on distributed generation, including electricity exemptions, has been completed, so that the specific gas/electricity exemption regime can be addressed as a whole within the new policy context. As a result, this is something that we hope to address in the medium to longer term. We foresee any proposed change being preceded by a formal public consultation, and that industry would be closely involved in the process of exploring options.

Another key area on which we have received specific feedback is the regime around electricity (section 37) planning consents and wayleaves, particularly relating to appeals and hearings and the need for stronger statutory rights for maintaining and developing infrastructure.

The Department committed to a number of actions in the Energy Review report that will improve the current energy planning system and which have simplification benefits. These include more efficient public inquiry procedures for power station applications, new rules allowing companies to do minor works to overhead lines without requiring fresh consents and improved guidance for developers on how to take CHP opportunities into account. On a broader scale, the Government is committed to fundamental reform to the planning regimes for major infrastructure. This provides significant scope for more simplification gains for the energy industry.

A further set of concerns relate to the policy around CHP generation, ranging from apparent conflicts in policy positions and incentives between different departments; the complexity of the regime acting as a barrier to small operators; right through to lack of clear guidance and support available. The general provision of guidance for electricity generators is something that the DTI will address, although the main specific concerns are largely about Defra-led regulations.

A problem for smaller CHP generators in particular is the amount of relatively complicated legislation they have to comply with. However, the environmental regulations, specifically the EU ETS, are complicated policy areas trying to establish a market for carbon. This is a vital part of the strategy for energy and the environment and it is in its infancy. Therefore, whilst simplification is desirable and what DTI and Defra are striving for in their review of the EU ETS and Phase II work, it may not be possible to get the ideal outcomes as quickly as we would want in the short term. Nevertheless, DTI and Defra will continue to work with the CHP sector to ensure their concerns are understood and considered as part of future solutions.

b) Upstream Oil and Gas

In the upstream oil sector, there are a number of areas of possible action suggested by industry, from establishing a register of licences and obligations; looking at funding mechanisms; simplifying the annual award process; through to streamlining the time-consuming regime for small well approvals and improving the DTI website. We have explored these concerns with the relevant DTI officials in order to establish the feasibility of beneficial intervention. Again, there are also a number of concerns relating to environmental legislation which is a Defra lead although, given the scale and cost of projects, taxation levels are the key concern for the sector.

The upstream sector is already moving towards increased self-regulation, particularly on the information gathering mechanisms. However, there are issues regarding the responsibility and payment for specific activities. The Deal Data Repository has running costs of £0.5m paid primarily by UKOOA, although non-members get the benefit of its use without contributing to the running costs. Nevertheless, the use of distributed data repositories with an associated index (Deal) was the model of choice adopted by the industry when the issue of how best to improve data availability was agreed several years ago. This cost effective solution ensures continued data availability without the need for DTI to collect large volumes of data from owning companies. Whilst the current system does not establish the perfect balance between data ownership and running costs, we believe it is better than an apportionment based on the number of licences held by a company. This will need to be reviewed in the future, particularly in the light of uptake in use of the National Hydrocarbons Data Archive.

The Environmental Monitoring Scheme is funded similarly to Deal, and it was suggested that it could be funded through the cost of permits. Although it would be possible to fund the monitoring requirement as a component part of the permit, this would result in the monitoring carried out by the permit holder, vastly increasing the total industry cost compared to the current arrangements.

In terms of Environmental Impact Assessments, we received feedback that the process could be speeded up if the assessment was submitted at the time of the licence application. Under EU Directives and resultant transposed UK regulations, the EIA can only be carried out based on a detailed plan or project. Therefore, at the time of the licence award, the company involved would not have sufficient information to submit an EIA. As such, we do not believe the EIA could be submitted at the time of application to speed up the process.

Well approvals were another area of concern for industry. There are not enough rigs available to drill wells as needed, so there is urgency to move forward as soon as rigs become available. The process of well application can be relatively lengthy, primarily due to the requirements of the EIA. However, in practice most well approvals are processed without a full Environmental Statement unless a well is in an environmentally sensitive area, in which case the DTI is required to ask for a full Environmental Statement with the necessary public consultation. Even in such a case, once a company has all the necessary information it can go out to public consultation, giving details of the environmental sensitivities of the area, while it is waiting for a rig to become available. In this context, under the current regime, the DTI is fulfilling its remit of optimising the field's potential while preventing unnecessary proliferation of infrastructure on the UKCS.

As a result of feedback, the DTI's oil and gas licensing team is reviewing its web content with a view to improving guidance. Any future updates will include a review of the Petroleum Operations Notices, which are considered in particular need of update by stakeholders. The team is continually assessing information provision with industry, attempting to streamline where applicable and will be working actively with UKOOA to simplify processes beyond the lifetime of the Better Regulation Project.

In addition to the DTI's close links with UKOOA, the sector is well served by the PILOT group which is a good vehicle for industry and government interaction. An example of this interaction is working with the oil and gas industry to minimise the burdens of security arrangements to cover the risk of defaults on decommissioning of oil and gas installations. The aim is to facilitate increased trading in UKCS assets. The number of companies benefiting will be small (i.e. probably < 75), but many are SMEs who will be better able to help sustain UK oil and gas production. The actions agreed include standardised agreements, guidance on cost estimating and clearer financial assessment processes. DTI is also considering proposals on the distribution of the risk between industry and government. Furthermore, the oil and gas portal, developed with industry, provides high quality web guidance for the upstream sector.

c) Downstream Oil

The UK's current system for holding emergency oil stocks is no longer optimal for delivering compliance with international obligations. The system is part of the global contingency arrangements for responding to disruption of international oil supplies and reinforcing market confidence during times of threatened disruption.

The DTI has held a public consultation to decide on a long-term basis for the system. The current proposal is to continue directing companies to hold stocks, although on a different basis, and to make this change with effect from July 2007. However, we are still discussing the results of the consultation with affected sectors and considering options.

A number of proposals fell within the remit of DTI's policy teams outside Energy Group. One issue was with the discrepancy between the Statutory Instrument and the British Standard on pump labelling. NWML has introduced a simpler pump labelling requirement in connection with its regulations implementing the Measuring Instruments Directive, which came into force on 30 October 2006. This requirement removes the obligation to mark the reference number of the relevant British Standard.

The DTI's Consumer and Competition Policy (CCP) Directorate lead on compensated metering of fuel supplies. The problem of resolving the fuel volume discrepancies at different temperatures has been debated for several years. The DTI's view is that a contractual solution can be agreed by retailers and refiners, in which case legislative change will not be necessary.

d) Coal

The issues raised with regard to the coal industry include environmental and planning regulations, thereby spanning Defra and DCLG responsibilities, as well as those of the DTI.

The coal industry's licensing body, the Coal Authority, is precluded under its establishing legislation (the Coal Industry Act 1994) from taking steps to assist an operator in obtaining planning permission for coal mining activity. Consultees have suggested that extending the Coal Authority's powers to enable them to do this would have the effect of a deregulatory measure, even though the current restrictions apply only to a single body set up by statute.

Following the Energy Review published earlier this year, the Department has established a Coal Forum, a key purpose of which is to examine ways in which to optimise the economical use of coal reserves in the UK. We envisage that the Forum will wish to consider a range of issues surrounding the planning regime for coal extraction and it would appear appropriate to address the Coal Authority's role in that context.

In addition to the issue of the Coal Authority's remit, there are specific policy issues about the use of methane for electricity generation, the ownership and licensing of gas in coal and issues about policy incentives for the extraction of methane from un-mined coal seams.

The use of methane for electricity generation falls under the umbrella of the EU ETS. The UK's implementation of the scheme does not allow for any recognition of the use of methane in generation, but all sectors apart from 'large electricity producers' (generally above 100MW) are allocated free allowances according to projected need.

For Phase II of the scheme (2008 - 2012) member states are able to include greenhouse gases other than carbon dioxide, such as methane, in the scheme. The UK and the majority of other member states have chosen to include only Carbon Dioxide at this relatively early stage of the scheme. Some preliminary research conducted by Defra last year identified very few sources where the environmental benefits of wider inclusion outweigh the costs and complexities.

However, the inclusion of other gases and the relationship between the EU ETS and action on other environmental matters, along with other issues, will be considered fully as part of the upcoming review of the EU ETS Directive, which is expected to begin in 2007.

A second issue relates to long term coal access leases. Coal mining operators drain methane from their mines and generate electricity under the terms of a Methane Drainage Licence (MDL). Petroleum Exploration and Development Licenses (PEDL) holders in the gas industry are unhappy at reluctance of coal mine operators to relinquish their rights to drain methane forcibly beyond the life of the mine. There remains the issue that the lease for coal is with the coal operator and without their consent the gas operator will never be allowed to commercially extract the methane from within the closed mine. However, these issues related to land-ownership and long-term coal access leases are commercial matters between the coal mine methane operators and mining companies, and so are beyond DTI's remit as regulator under the Petroleum Act 1998.

A further point raised is that there is uncertainty as to whether or not an operator carrying out Underground Coal Gasification (UCG) in coal needs to be the PEDL holder for the area, as well as having the necessary licence and lease from the Coal Authority. The question is whether the Coal Industry Act 1994 envisaged that UCG would be effected under the Coal Authority's regime, rather than requiring a PEDL, or indeed both. The DTI's oil & gas licensing team will be able to take a firm view on this in light of actual cases. Following evidence, the DTI will consider the government's requirements, taking into account its wider objectives for the sector as well as what is already being accomplished by other regulatory mechanisms. Following a decision on this basis, options for reducing

or even removing the regulatory burden, by reviewing the required licences, would be assessed.

We considered at length the proposal of repealing and/or consolidating parts of the coal legislation. Whilst we agree that there is scope for tidying up the statute book for coal, our initial scoping work made clear that it would be a substantial exercise merely to identify potential legislation, even before looking at options and routes for legislative change. Following discussions with the policy and legal officials concerned, it was felt that it would be a complex and expensive exercise which could not be justified at this point given the lack of quantifiable benefit expected to result from it. This issue is covered further in section 4.2.4 b).

e) Nuclear

Concerns raised by the nuclear sector focus largely on planning and consents, and the need to integrate licensing and planning processes to provide predictable timeframes. However, they have also raised a secondary issue relating to the fact that the UK does not accept international standards and approvals, but requires its own approval process, which is naturally time consuming and more costly for industry. These issues have already been considered as part of the Energy Review, with some of the planning aspects also being addressed by the Barker and Eddington Reviews. Ongoing workstreams will aim to simplify processes and provide clarity for the sector.

Following the Energy Review, the DTI developed a proposal for a policy framework under which developers will be able to make proposals for new nuclear build. The consultation on the nuclear policy framework closed on 31 October, with views sought on the following proposal: a policy framework (including a nuclear "statement of need") in which national strategic and regulatory issues are most appropriately discussed through processes other than the planning inquiry. The intention is that the Energy White Paper in 2007 will set out the Government's policy stance on new nuclear build.

4.2.2 Better regulation approaches and principles

A general theme from stakeholders is that whilst they welcome better regulation principles relating to consultation and guidance, they are concerned that the principles are not applied consistently across DTI or government more widely, and therefore do not provide the predictability and stability that business would like. For instance, there is a concern that timeframes are not adhered to at all times, and consultation fatigue can lead to the perception that government consults as part of due process rather than to add value. The number, length and frequency of consultations is a real issue, especially for smaller organisations, who often do not have the resource to contribute fully.

Therefore, we need to ensure that Energy Group as a whole is committed to following best practice on better regulation, particularly developing clear, robust RIAs in a timely manner to enable industry to challenge our evidence base as appropriate, and short, focused consultations to add value to the policy development process and ensure costs and benefits are fully tested. Engaging effectively with stakeholders is a key element of driving the better regulation

agenda, and this plays into the existing mechanisms and approaches across both Energy Group and the Department more widely.

One of the proposals that the project team has been able to target in the short term is the improvement of internal processes in Energy Group. Across the DTI there is an increasing emphasis on all future policy being strongly evidence based and utilising better regulation best practice. Within Energy Group, the project team has run sessions for staff to disseminate information, educate and encourage the use of best practice when formulating and implementing policy. Specifically, the aim is to achieve consistently high quality regulatory impact assessments and consultations. As a path to achieving this we have improved the guidance available to policy officials, and encourage industry to challenge us on delivering these key elements externally.

The publication of forward look information regarding commencement dates for legislation coming into force is seen as a positive move, although there is concern that it does not seem to be widely adopted by other departments. The DTI pioneered common commencement dates and, in fact, the majority of departments have now implemented them and the remainder have signed up to doing so. Therefore, this is a communication issue, linked to the fact that there is no obvious single source of information on better regulation for industry that joins together what they can expect from government as a whole, alongside specific sectoral or departmental measures, and the role or opportunities for industry to input and challenge. We are in communication with other departments and the Better Regulation Executive about how to encourage greater transparency in relation to forthcoming regulatory change.

However, this is a government-wide agenda, and as better regulation principles and common commencement dates are applied more consistently, industry should have a better oversight of upcoming changes to the regulatory framework and where their input is required.

4.2.3 Joined up government

A major criticism that has been voiced repeatedly by industry relates to the lack of coherent joining up across government and the way that one department's policies can be in direct conflict with another's. Even where policy is working towards a common objective, there can be overlaps and inconsistencies between different departments, and this can have an adverse impact on industry. Furthermore, devolution has, in certain cases, created further complexity in regulation.

One option we proposed in our interim report to improve this situation was to look at establishing a combined regulatory forum for energy, potentially along the lines of the existing VIPER (Vehicle Industry Policy and European Regulation) forum. However, having considered the number and content of existing forums on energy it was judged that an additional forum would be excessive given that the likely membership would overlap with the established forums. Nevertheless, given the need to have some way of addressing regulatory issues specifically, we are working on setting up a better regulation working group underneath and reporting to the Business Climate Change and Energy Group (BCCEG) which we believe will be fit for purpose, alongside maintaining ongoing individual dialogue. The BCCEG is attended by representatives from the DTI, Defra, HMT, Ofgem,

Energywatch and the Environment Agency as well as trade associations, energy companies and energy intensive users.

There are a number of other forums which provide the opportunity for a cross-government presence to engage with industry on energy and the environment, including the Business Energy Forum and the Sustainable Energy Policy Network Advisory Board. Furthermore, work on the Energy Review was undertaken by a cross-departmental team and the workstreams arising out of it, which will directly contribute to the Energy White Paper development, will have input from DTI, HMT, Defra, DCLG and DfT. This approach recognises the need for joined up working to develop a long term energy strategy.

To address some concerns in the shorter term, we will run a joint seminar with Defra in the new year on simplification options for industry to ensure the concerns of business on energy and environmental policies are heard directly by the relevant lead departments.

4.2.4 Legislative issues

a) Legislative stability

Of major concern to industry are the broad issues of regulatory stability and transparency which would contribute to an overall framework to ensure the certainty of long term investments and business planning.

Throughout the project we have received feedback about the need for stability in energy legislation. Industry is concerned that reviews of legislation are too frequent, particularly in the renewables and environmental areas. A lack of stability affects investment, leads to uncertainty in the market and can increase costs. Given the long term nature of business and investment plans, energy legislation would serve the industry better if it remained unchanged for similarly long periods wherever possible.

A lot of change arises out of the quest to apply the most relevant policy in the most suitable way. There is also the combined impact of the interaction between policies implemented through the EU and a number of domestic government departments, agencies and regulators.

The frequent changes that have occurred in recent years, particularly in environmental policy, reflect the relative infancy of this policy area. Reviewing legislation, particularly in new policy areas, is important to ensure that it is fit for purpose. Following several years of use and a clear policy goal we are hopeful that there will be a lesser need for regular change.

The Energy Review has outlined the UK's energy strategy for several decades in order to meet its key objectives. Although in the short term this is likely to require some legislative change, it should also lead to greater long term stability in UK energy. We anticipate that the necessity for Europe to work together to tackle climate change and security of supply may also result in an increasingly coherent and stable approach in EU legislation.

b) Tidying up the statute book

Whilst the main aims of simplification and streamlining have been welcomed by industry, there are polarised views on the value of consolidation and abolition: tidying up the statute book is seen as potentially a good thing, but outweighed by the significant opportunity costs involved. The main practical advantage to pursuing either repeal or consolidation would appear to be the potential for easing the access of smaller, newer players into the sector.

The general consensus is that where regulations are not in active use, they are not imposing a real burden on industry, and therefore there is limited benefit in removing them as part of a specific project. Therefore, having examined the potential costs and benefits of repealing regulations in a specific sector to use as an example (see section 4.2.1 d), we have not been able to identify discrete regulations for which the cost of repeal is justified by the small reduction in burden it would create.

Consolidation may offer more immediate value, although again there is a lack of evidence regarding the benefits considering the resource intensive process. We believe that a more efficient way of tackling the problems caused by a complex statute book would be to ensure that new legislation is introduced only following a critical appraisal of the potential to update, repeal or consolidate existing legislation in that area. In other words, the statute book should be tidied up over time as part of ongoing legislative renewal. The need to follow better regulation best practice and the one in, one-out approach to regulation will provide the impetus for this change to happen.

An alternative and additional option proposed that might mitigate the problems posed by the complexity of the statute book, is some form of guide to currently relevant legislation for industry - both primary and secondary. To address this in the most cost effective and practical way, we have embarked on a project to improve the external guidance on the DTI's web pages for energy by creating a page signposting current legislation to enable stakeholders to find DTI's energy regulations from one place.

c) Distance between policy intention and implementation consequences

We anticipate that the BCCEG working group already mentioned above (see 4.2.3) should help to address the issues around legislation not meeting the policy intention behind it when implemented in practice. This will operate at a working level, and provide industry with a forum for discussing the detail of energy policy and regulation with government officials, to ensure that they achieve the original policy intention with as few unintended consequences and grey areas as possible. Also important is industry's role in providing input as early in the process as possible right through to implementation, through formal and informal consultations as well as through representatives on the numerous energy forums.

d) Guidance and support

Stakeholders have also raised concern about the lack of clarity in guidance and legislation creating problems of interpretation. Whilst we would not want

guidance to take on quasi-legal status and prevent flexibility, this does indicate that we could improve the quality of guidance provided, and look at ways to make legislation easier to understand.

We have worked to address this by working with the Better Regulation Team on their culture change programme to explore ways of embedding best practice and improving the skills of our officials in this area. In addition, we have improved energy guidance on better regulation and briefed officials on the value of incorporating better regulation principles in policy making, from formulation to implementation.

Potentially, utilising the BCCEG working group mentioned above, industry participation in the development of new legislation, and through ongoing dialogue and feedback will also play a part in improving the quality of legislation and guidance.

e) Changing policy drivers and the need to update legislation

In addition, a general issue has been raised relating to the evolution of the markets and policy drivers over time, leading to legislation being based on objectives and assumptions that are no longer entirely valid. This means that some legislation is very out of date and does not necessarily meet the requirements of the current competitive environment. In particular, the new emphasis on environmental factors, a desire to stimulate innovation and investment, and the encouragement of smaller players is not wholly supported by existing legislation that was based on policies set ten or twenty years ago. The questions around the value of repealing historic legislation are discussed earlier, although this issue is more about reviewing and updating existing policy to ensure that implementation supports the policy intention rather than focusing on simply repealing chunks of legislation.

Given the potential changes in the energy framework following the Energy Review and subsequent White Paper, it will be increasingly important for industry to provide timely feedback on how policy is being developed and implemented to ensure that it best reflects and supports effective operation of the market.

4.3 Key themes and proposals outside the project scope

There are a number of areas where we do not have a remit for taking forward proposals and implementing change. We have engaged with those who do lead on these areas, and have raised these issues with the Better Regulation Executive to ensure that there is an awareness of them at the centre and that they are appropriately handled as part of the cross government simplification agenda.

4.3.1 Ofgem responsibilities

A significant number of the gas and electricity specific issues raised by industry relate to Ofgem responsibilities. For example, a potential area of regulation that

industry believes could be simplified or removed are the standards of performance regulations, which fall to Ofgem to administer and enforce, and they have already committed to reviewing these. The burdens created by requirements on business to notify changes of tariff, for instance, are already being addressed as part of the Supply Licence Review, as are industry concerns about the existing duplication within specific licence conditions of much broader national legislation.

Industry has expressed concern about Ofgem's handling of the single appeal since the change in the process of appealing Ofgem's decisions. In that instance Ofgem acted in a way to protect the public interest. However, the handling of that single case does not necessarily act as a precedent for future appeals and, therefore, at this stage, there does not appear to be a case for DTI prescribing how Ofgem should operate in such circumstances. Naturally, as and when further appeals or representations by industry are made, this may be an area for further review, if the evidence reveals an underlying problem.

As well as specific feedback about the various strands of Ofgem's simplification work and its policies, there have been several wider-ranging comments about its role. A belief stated by several stakeholders was that Ofgem's simplification agenda should 'focus on a withdrawal from active direction of and involvement with the energy markets, where this is feasible'.

Stakeholders specifically commented that 'there is considerable scope for a reduction in Ofgem's direct involvement in industry matters' and that, 'DTI should encourage a withdrawal strategy from Ofgem in those areas of the energy market where competition and consumer protection law combined with enhanced self-regulation are sufficient'.

Ofgem's primary role is to promote choice and value for all customers. It does this by promoting effective competition wherever appropriate and regulating effectively the monopoly companies which run the gas and electricity infrastructure. Whilst Ofgem has other priorities, including helping secure Britain's energy supplies and helping industry achieve environmental improvements as efficiently as possible, it has to relate these back to its customer-focused role.

Ofgem is committed to the principles of better regulation and to running its operations as efficiently and effectively as it can. There are a number of significant measures it is undertaking to achieve this.

In terms of cost efficiency, Ofgem has adopted an RPI -3 per cent control for the period 2005-06 to 2009-10. This will see sustained real reductions in the costs of regulation for the first time since the privatisation of the gas and electricity industries. Ofgem has to date beaten its RPI-X target and as a result has reduced the licence fees payable in 2006/7 by £2.9 million, or nearly 10 per cent of its allowed budget.

Ofgem, like DTI, has a simplification plan with forthcoming measures which will reduce costs and increase benefits to business. Ofgem's commitment in its Corporate Plan is to continue to review its policy and processes with a view to achieving best practice in relation to better regulation.

A significant new project is examining industry codes and their requirements, determining the appropriate role for licence regulation and self-regulation in securing compliance with these codes in the future. An example of this is

rationalising the Network Codes for Independent Gas Transporters and looking at the effectiveness of the Supply Point Administration Agreement.

A key piece of Ofgem's simplification work is the review of the electricity supply standard licence conditions (SLCs). The review aims to bring the regulatory rules for gas and electricity suppliers up to date given that competition is now firmly established and that developments in consumer and competition law make some rules redundant. The aim of the review is to ensure that SLCs are retained only where there is a clear need for protection for customers over and above that provided by the market itself and general consumer protection law and competition law. In July 2006 Ofgem published initial proposals. These were intended to remove unnecessary red tape and ensure that obligations on gas and electricity suppliers were targeted and proportionate for a highly competitive market and neither discouraged market entry nor stifled innovation in the range and types of contracts and services on offer. Ofgem proposed to remove and simplify licence obligations wherever possible, and identified where self-regulation could replace formal regulation, while recognising the need to maintain appropriate protection for vulnerable customers, given that energy is an essential service, but proposed clearer and simpler obligations on suppliers towards those customers.

Ofgem's initial proposals would cut the supply licence from 160 to 80 pages. Ofgem aims to issue a final decision document on the proposed modifications in March 2007. Depending on acceptance of the modifications, the plan is to introduce the new licence from June 2007.

4.3.2 Planning

The issues and concerns arising around planning regulations are largely connected to process and involve addressing timescales, levels of expertise and providing greater certainty and predictability for industry. Many of the issues are linked to the planning regime more generally, which lies within the remit of DCLG, and have been identified as part of the Energy and Barker Reviews as well as this project. The Barker Review, which is looking for ways in which the planning system can better deliver economic growth while maintaining sustainable development goals, is due to report by the end of 2006.

The remainder are more specific issues linked to the process and policy around electricity consents, of which overhead lines and wayleaves are a subset, falling within DTI's policy remit. These specific wayleaves issues are currently being addressed within Energy Group, as part of EDU's own broader review of consents, looking to simplify and streamline the process around hearings and disputes related to overhead lines. This is set out in section 4.2.1 a).

Furthermore, as part of the Energy White Paper work, which will have DCLG involvement on planning, there is a review of regulations governing existing buildings and an update of micro generation planning rules. In its simplification plan DCLG has outlined the measures it will undertake to simplify planning and building regulations. It is also anticipated that there will be a Planning White Paper in 2007, which will address key policy issues in this area.

4.3.3 Environmental legislation

There are a number of specific issues raised in relation to environmental legislation and the burdens imposed by regulations stemming from EU Directives. Some of these link to the requirements for Environmental Impact Assessments, whilst others are much wider issues to deal with EU ETS requirements or overly prescriptive definitions within regulations. A key recurring theme is the need to rationalise environmental legislation to ensure a better alignment with other cross government objectives on innovation, economic growth and investment, and to reduce the policy conflicts that currently exist. One further concern is that that devolved administrations' regulations also have to be taken into account, which can add to the overall complexity.

There are also a number of issues, particularly in the CHP field, where there appears to be some conflict between energy efficiency policy and the practicalities of the legislation. There is a concern that the complexity is acting as a barrier to smaller operators, of which the CHP sector has a significant proportion. These concerns fall largely within Defra's remit, and indeed are issues they are already aware of.

As these issues are not led by DTI, we have shared them with Defra and the EA who are also exploring opportunities for simplification. Stakeholders expressed a desire to be more closely involved with Defra on this, hence our approach of setting up a joint seminar as set out in section 4.2.3. The implementation of EU Directives in the UK, a large number of which pertain to environmental legislation, has been reviewed as part of the Davidson Review, discussed further in the next section.

4.3.4 EU and international

In terms of the EU more generally, there have been a number of concerns expressed about regulatory process, in particular the lack of consultation on some legislation or the general plethora of consultations, which can result in proposals being missed. Other concerns include the issue of gold-plating, and limited following of best practice on implementation by other Member States. The main specific issues relate to EU ETS, although other regulations such as the Habitats Directive, Integrated Pollution Prevention and Control (IPPC) Directive and the Waste Directives have also been raised as overly burdensome in the UK implementation.

Both DTI and DEFRA lead on a number of EU issues and are in a position to lobby for improved policy development processes. One potential avenue for raising issues of implementation early in the process would be through the BCCEG working group, although this would need to complement the effective industry forum on European Regulation already in existence. This is an AEP chaired forum representing major electricity producers, network operators, trade associations, DTI and Ofgem, which discusses latest EU developments, their impact and relevant UK implementation. Even more so than on domestic legislation, it is key that industry inputs into the process as early as possible and is involved in all stages of consultation with regards to EU Directives. More generally, industry can use the Confederation of European Business, the European Energy Forum and the European Energy and Transport Forum to input

views. Furthermore, the DTI's European Energy team is developing a stakeholder management plan to enable better discussion of EU energy policy issues.

Gold plating more generally is a cross Whitehall issue that is being addressed through the Cabinet Office's Davidson Review, which is aiming to ensure that EU legislation has been implemented in the UK in a way that does not create unnecessary burdens. We are aware that a significant number of industry stakeholders have provided input to the Davidson Review, and its interim report contained the majority of Defra related issues raised with us during the project. The Davidson Review will publish its final report with recommendations made to government by the end of 2006. The recommendations will comprise specific simplification proposals to remove regulatory burdens and best practice advice to regulators and departments on how to avoid unnecessary over-implementation of EU legislation in the future.

5. Conclusions

This is the final report for the Energy Better Regulation Project and it sets out the work which has been done during the project, work that will be undertaken in the future and the reasoning behind decisions for not addressing some of the issues raised during the informal consultation with stakeholders.

The project has been based on working with industry to get a stakeholder perspective on key problems and proposals to resolve them. Through this approach of active dialogue we were able to get a lot of valuable input from a cross section of industry. This complemented the concurrent work on admin burdens and allowed us to get a robust picture of the burdens on the energy industry.

There are a number of actions which have been undertaken by the project team as a result of feedback from industry, which were first outlined in the interim report. Firstly, we have improved the better regulation guidance material for energy policy officials, setting out the processes and support available and providing practical help; establishing protocols on consultation and engagement strategy, RIA development and monitoring. To complement this we have run a session for staff to provide face-to-face guidance on the better policy making process to help embed it into their work. The increasing emphasis on and uptake of this should enhance the quality and consistency of evidence based policy going forward.

We are also going to set up a working group underneath the existing Business Climate Change and Energy Group (BCCEG) to discuss regulatory issues, policy proposals, RIAs and guidance at an early stage. A wider one-off seminar will also take place to allow DTI and Defra to outline simplification options and for industry to ensure the concerns of business on energy and environmental policies are heard directly by the relevant lead departments.

To address the complexity of the statute book for energy in the most cost effective and practical way, we have embarked on a project to improve the external guidance on the DTI's web pages for energy by creating a page signposting current energy legislation to enable stakeholders to find all DTI's energy regulations in one place. We believe this will act as a good starting point for anyone looking for an overview of legislation affecting the sector, with links

to other relevant departments' and regulators' web sites. We will be engaged with stakeholders on how best to maintain and improve this guidance.

There were some views that there should be a single regulator for the onshore and offshore industry rather than the current split between DTI and Ofgem. Feedback on the interim report suggested that there was little appetite for change in this area, rather that regulatory stability is desirable to maximise the economic utilisation of the remaining reserves in the UKCS. Similarly, recent feedback has agreed with our interim report conclusion that rationalising licences into a single energy licence is of limited benefit.

There were a number of proposals which we undertook to analyse further in the interim report, and which are set out in more detail in the sector specific sections of this report. In summary, gas licence exemptions will be reviewed following the completion of work on electricity exemptions. The consultation responses on the oil stocking system are still being considered and a change is anticipated in July 2007.

The discrepancy between the British Standard and the Statutory Instrument on pump labeling has been addressed by the implementation of the Measuring Instruments Directive. With regard to compensated metering, the DTI believes a contractual solution between retailers and refiners is preferable to legislation.

There are a number of broad proposals arising during this project that fall within the remit of other current projects: the Davidson Review; the Barker Review; and the Energy White Paper. These reviews have had input from a wide selection of industries, including the energy sector, and will impact on a cross section of government departments. The Davidson, Barker and Eddington reviews will report by the end of 2006 and it is anticipated that they will contain recommendations for significant simplification in the areas of regulation they have reviewed. The Energy White Paper, although led by the DTI, will have significant input from and cross working with other departments in order to produce a cohesive energy strategy which encompasses relevant environmental, planning and transport policies.

Following the conclusion of this project, it will be important for the industry and DTI to continue engaging on the subject of energy regulation in order to identify and explore opportunities to simplify the regulatory framework for energy. The most effective way of bringing about positive change is for industry to provide us with evidence of where and how things are not working and ideas of how they can be improved, which we can then explore further. There are various mechanisms which industry can utilise to raise issues with DTI, Ofgem, other government departments, devolved administrations and at EU level. Full and early engagement in the consultation process should help to ensure that legislation is fit for purpose, effective and proportionate. Significant proposals taken forward as part of this project and stemming from future industry feedback will be included in the Simplification Plan in future years.

To conclude, the project's key achievement has been establishing constructive dialogue with industry on the important issue of how we best ensure the regulatory framework is fit for purpose, alongside improving the internal better regulation processes within DTI's Energy Group by raising awareness and improving guidance, which should lead to improvements in the quality of future policy development and implementation. Some of the proposals have fallen within the remits of other government departments, regulators and other

reviews, including the DTI's Energy Review, while some have been considered by DTI's policy teams and will be taken forward in the medium to long term.

Going forward it is vital that dialogue on this agenda continues between government and industry to help ensure that existing regulation is under ongoing review to ensure it remains current. Furthermore, future policy should undergo robust assessment of the evidence base and be implemented in a way such that it serves its purpose while minimising the burdens on business.