

UTILITY REGULATION AND SUSTAINABLE DEVELOPMENT

JEFF MOCHAN, RESEARCH OFFICER

INTRODUCTION

This paper provides information on:

- The role of the NI Authority for Utility Regulation (known informally as the Utility Regulator¹).
- Guidance to regulators by the UK Government and Organisation for Economic Cooperation and Development (OECD).
- The perspective of the Utility Regulator on Sustainable Development.
- The perspective of the Sustainable Development Commission on utility regulation.

1.0 THE ROLE OF THE REGULATOR

1.1 STATUTORY AUTHORITY FOR THE UTILITY REGULATOR

The NI Authority for Utility Regulation (known informally as the Utility Regulator) is an independent public body set up to ensure the effective regulation of the electricity, gas and water and sewerage industries in NI; it has wide ranging powers to enable it to carry out its duties².

The Utility Regulator was established under Article 3 Part II of the Energy (NI) Order 2003³, as amended by Article 3 of the Water and Sewerage Services (Northern Ireland) Order 2006⁴. Most of the functions of the Directors General of Electricity Supply and Gas for NI were transferred to the Utility Regulator on 1 April 2003, and water and sewerage functions were transferred on 1 April 2007⁵.

The water, gas and electricity industries are at different stages of evolution, so the Utility Regulator has different duties for each industry. The duties are set out in detail in Article 6 of the Water and Sewerage Services (NI) Order 2006 (for water), Article 14 of the Energy (NI) Order 2003 (for gas), and Article 12 of the Energy (NI) Order 2003 (for electricity), and in outline below.

¹ <http://ofreg.nics.gov.uk/what%20is%20the%20Utility%20Regulator.htm>

² <http://ofreg.nics.gov.uk/what%20is%20the%20Utility%20Regulator.htm>

³ <http://www.opsi.gov.uk/si/si2003/03em0419.htm>

⁴ <http://www.opsi.gov.uk/si/si2006/06em3336.htm>

⁵ <http://ofreg.nics.gov.uk/index.html>

1.2 PRINCIPAL OBJECTIVE AND KEY DUTIES OF THE UTILITY REGULATOR

The principal objective of the Utility Regulator in all industries is protection of the customer, both present and future. In the electricity and water industries this is to be achieved by promotion of competition, while in gas it is to be achieved by promotion of the industry.

The key duties of the Utility Regulator include:

Water:

- Protect the interests of consumers of water and sewerage services, where appropriate by the promotion of effective competition.
- Ensure that water and sewerage undertakers properly carry out their functions in all areas of NI.
- Ensure that water and sewerage companies can properly finance their activities.
- Have regard to (among other things) the interests of individuals who are disabled, chronically sick, of pensionable age, on low income or residing in rural areas.
- Contribute to the achievement of sustainable development.

Gas:

- Promote the development and maintenance of an efficient, economic and coordinated gas industry in NI.
- Have regard to (among other things) the interests of consumers of gas.
- Ensure that gas licence holders can properly finance their activities.
- Have regard to the interests of individuals who are disabled, chronically sick, of pensionable age, or on low income.
- Have regard to the need to secure a diverse and long-term energy supply.
- Have regard to the effect on the environment of activities connected with the conveyance, storage and supply of gas.

Electricity:

- Protect the interests of consumers of electricity, wherever appropriate by promoting effective competition.
- Have regard to the interests of individuals who are disabled, chronically sick, of pensionable age, on low income or residing in rural areas.
- Promote efficiency and economy on the part of the licence holders.

- Secure a diverse and viable long-term energy supply.
- Have regard to the effect on the environment.
- Participate in the Single Electricity Market in NI and RoI, which went live on 1 November 2007 and is governed in NI by the Electricity (Single Wholesale Market) (NI) Order 2007⁶, and is intended to secure a diverse, viable and environmentally sustainable long-term energy supply in NI and RoI, and promote the use of energy from renewable sources.

2.0 GUIDANCE ON REGULATION

2.1 ORGANISATION FOR ECONOMIC COOPERATION AND DEVELOPMENT (OECD)

The 2008 OECD policy brief 'Measuring Regulatory Quality'⁷ outlines, in the context of regulatory reform in its widest sense, the components of effective regulatory policy, the essential tools for improved regulatory decision making, and the factors which inform good regulation.

An effective regulatory policy has 3 basic, mutually supporting components:

- Adoption at the highest political levels.
- Explicit and measurable regulatory quality standards.
- A continuing regulatory management capacity.

Improved regulatory decision making is achieved with 4 essential tools:

- Regulatory impact analysis.
- Public consultation.
- Consideration of regulatory alternatives.
- Measures to reduce the burden of compliance.

Good regulation requires consideration of several factors, including:

- Regulatory reform and management, which require political support if they are to succeed.
- Institutional capacity, which is key to improving the quality of new and existing rules.
- The suitability of alternatives to traditional regulation, such as more flexible and less prescriptive regulation, co-regulation and self-regulation, incentives and market-based instruments, and information approaches, all considered within a context of 'joined-up government' and a 'comprehensive approach'.

⁶ http://www.opsi.gov.uk/si/si2007/em/ukxiem_20070913_en.pdf

⁷ <http://www.oecd.org/dataoecd/38/13/40395187.pdf>

- Regulatory Impact Assessment, which underpins the capacity of governments to ensure that regulations are efficient and effective in a changing and complex world.

The 2005 OECD Guiding Principles for Regulatory Quality and Performance⁸ provide guidance to member countries to improve regulatory policies and tools, strengthen regulatory policies and tools, strengthen market openness and competition, and reduce regulatory burdens, as follows:

- Adopt at the political level broad programmes of regulatory reform that establish clear objectives and frameworks for implementation.
- Assess impacts and review regulations systematically to ensure that they meet their intended objectives efficiently and effectively in a changing and complex economic and social environment.
- Ensure that regulations, regulatory institutions charged with implementation, and regulatory processes are transparent and non-discriminatory.
- Review and strengthen where necessary the scope, effectiveness and enforcement of competition policy.
- Design economic regulations in all sectors to stimulate competition and efficiency, and eliminate them except where clear evidence demonstrates that they are the best way to serve broad public interests.
- Eliminate unnecessary regulatory barriers to trade and investment through continued liberalisation and enhance the consideration and better integration of market openness throughout the regulatory process, thus strengthening economic efficiency and competitiveness.
- Identify important linkages with other policy objectives and develop policies to achieve those objectives in ways that support reform.

2.2 UK GOVERNMENT

The Better Regulation Task Force was an independent advisory group established by the Cabinet Office in 1997 to advise government on action to ensure that regulation and its enforcement are transparent, accountable, proportionate, consistent and targeted. In its 2005 report to the Prime Minister 'Regulation – Less is More: Reducing Burdens, Improving Outcomes'⁹, it states the following 5 Principles of Good Regulation:

- Proportionality. Regulators should only intervene when necessary. Remedies should be appropriate to the risk posed and costs identified and minimised.
- Accountability. Regulators must be able to justify decisions and be subject to public scrutiny.

⁸ <http://www.oecd.org/dataoecd/38/13/40395187.pdf>

⁹ <http://archive.cabinetoffice.gov.uk/brc/upload/assets/www.brc.gov.uk/lessismore.pdf>

- Consistency. Government rules and standards must be joined up and implemented fairly.
- Transparency. Regulators should be open and keep regulations simple and user-friendly.
- Targeting. Regulation should be focused on the problem and minimise side-effects.

The Better Regulation Commission succeeded the Better Regulation Task Force, with a vision of 'a policy making environment in which a sustained commitment to evidence-based, high quality, flexible process leads to public risk being tackled in a systemic, targeted, an proportionate manner with good intentions leading routinely to good outcomes'. In its 2008 report to the Prime Minister 'Public Risk – the Next Frontier for Better Regulation'¹⁰ it notes that:

- The public expects the government to get the balance right, even in a crisis, between protecting citizens and maintaining freedom, resisting the clamour of scaremongers and stiffening the resolve of the timid.
- Public trust in government to do this is on the wane.
- Temptation to move prematurely from problem to solution to intervention results in, all too often, ineffective policies, unnecessary regulatory burden and unwelcome curtailment of civil liberties.
- Excessive focus on treating symptoms rather than causes leads to misdirected efforts.
- It is fiction that it is possible to get interventions right first time; trial, adaptation and learning are key to successful intervention.

3.0 KEY ISSUES OF REGULATION AND SUSTAINABLE DEVELOPMENT

3.1 THE VIEW OF THE UTILITY REGULATOR

The Utility Regulator's 2008 consultation paper 'Sustainable Development, The Regulator's Role'¹¹ notes that:

- Sustainable utility service is at the heart of the Utility Regulator's work, and decisions regarding water, electricity and gas services must be taken in the context of factors including: overall economic competitiveness; vulnerable customers; security and quality of supply; sustainable finance and long-term maintenance; and the cost of carbon and the potential future price and availability of carbon fuels.
- Utility services in NI could do more in relation to sustainability. NI's ecological footprint is highest in the UK; NI is highly reliant on fossil fuels; NI cannot rely

¹⁰

http://archive.cabinetoffice.gov.uk/brc/upload/assets/www.brc.gov.uk/public_risk_report_070108.pdf

¹¹ <http://ofreg.nics.gov.uk/31%20March%202008S.htm>

in the future on efficient technology which has previously held down its greenhouse gas emissions levels; vulnerable customers who suffer from energy poverty, and might suffer from water poverty, may face extra risk of the effects of climate change, such as flooding.

- NI's current and future customers will face unavoidable costs relating to both mitigation of climate change and adaptation to climate change, many of the costs of which are already evident.
- Early action towards sustainability, as it relates to utility services, could be in the form of energy efficiency, water conservation, or moves to lower carbon energy or renewable energy.
- Energy efficiency and renewable energy, as means of reducing carbon emissions, can bring the bonus of increased security of supply.
- Water conservation can contribute to sustainability.
- Fuel and water poverty must be addressed in the context of sustainability.
- The Utility Regulator's response to the challenge of sustainability must be framed within its statutory duties, and it is currently responsible for implementing a number of policy strands aimed at promoting energy efficiency and lower carbon, water conservation and biodiversity, but could do more.
- The Utility Regulator could contribute more to the sustainable development of utilities in NI by: gathering and publishing more evidence; contributing expertise and experience to wider government policy; and regulating differently.

3.2 THE VIEW OF THE SUSTAINABLE DEVELOPMENT COMMISSION

The Sustainable Development Commission¹² has not commented formally on the sustainability performance of the Utility Regulator in NI. It did, however, publish a report on the Office of Gas and Electricity Markets (OFGEM)¹³, the Utility Regulator for gas and electricity in GB, the lessons of which the Utility Regulator in NI admits might be transferable to the NI context. The 2007 Sustainable Development Commission report 'Lost in Transmission: The Role of OFGEM in a Changing Climate'¹⁴, comments that:

- The policy landscape for energy is complex, with a responsibility for energy and environment policy split between 2 Secretaries of State. There is also a lack of alignment between OFGEM's goals and government's goals, and there is no regulatory framework for the provision of heat. OFGEM's institutional culture and approach do not reflect the imperative of sustainable development, particularly climate change.

¹² The Sustainable Development Commission is the UK government's independent advisor on sustainable development, reporting to the Prime Minister and the First Ministers of Scotland, Wales and NI

¹³ <http://www.ofgem.gov.uk/Pages/OfgemHome.aspx>

¹⁴ [http://www.sd-commission.org.uk/publications/downloads/SDC_ofgem_report%20\(2\).pdf](http://www.sd-commission.org.uk/publications/downloads/SDC_ofgem_report%20(2).pdf)

- Combined heat and power and renewable generators face a number of barriers to participating in the energy markets and connecting to the transmission and distribution grids. The UK's ageing distribution networks need strengthening to cope with increase levels of distributed generation.
- Consumers need to receive accurate and informative bills in order to engage with their energy use, but the existing approach to metering and billing prevents this. Reductions in energy prices have helped to alleviate fuel poverty, but this has been partially reversed by recent price rises. These needs to be greater focus on managing energy use through better information and energy efficiency measures.

MAY 2008