OFG-206209

To: William Elliott[William.Elliott@ofgem.gov.uk]; Marcus Porter[Marcus.Porter@ofgem.gov.uk]
From: Keith Avis
Sent: 2012-10-04T13:56:54Z
Importance: Normal
Subject: RE: Administrative Arrangemnts: Comments Received from DETI
Received: 2012-10-04T13:56:55Z

Will
I am pretty much going to cut and paste your comments below in a submission to Bob, with some text around the process from here, so if you would prefer to do the submission to fit with Ruth's need that would be OK with me.
Rgds
Keith

From: William Elliott
Sent: 04 October 2012 14:46
To: Marcus Porter; Keith Avis
Subject: RE: Administrative Arrangemnts: Comments Received from DETI

Ruth mentioned yesterday that she would like to see whatever went to Bob.

From: Marcus Porter
Sent: 04 October 2012 13:59
To: Keith Avis; William Elliott
Subject: RE: Administrative Arrangemnts: Comments Received from DETI

Keith, Will
Following the meeting yesterday between the three of us, what I believe were our joint conclusions on the various points made by DETI are shown below in Joanne's email. I haven't copied to others for the moment, in case either of you disagree in any respect with my recollection of our discussion. Should that be the case, please amend appropriately before the conclusions are shared with others and let me know.
I am out for the remainder of this afternoon.
I should mention that I have elaborated somewhat on some of our answers where that seemed appropriate.
Marcus

From: Keith Avis
Sent: 03 October 2012 10:51
To: William Elliott
Cc: Marcus Porter; Mary Smith; Matthew Harnack; Paul Heigl; Michelle Murdoch; Rita Chohan
Subject: Administrative Arrangemnts: Comments Received from DETI

Will cc: Marcus, Mary, Matthew, Paul, Michelle, Rita
You will see (below) that we have finally received a response from DETI on the Administrative Arrangements. I appreciate that this will take some time to work through, but grateful if we could work up an initial view on the points raised by DETI, so that we can be clear on those points where we have major differences and decide on our strategy for tackling these. We have the usual teleconference with DETI tomorrow morning, if we could discuss this before then so that we have a broad overall message in mind that would be very helpful.
Regards
Keith

From: Keith Avis
Sent: 03 October 2012 10:35
To: 'McCutcheon, Joanne'
Cc: Hepper, Fiona; Hutchinson, Peter
Subject: RE: Administrative Arrangemnts

Joanne
Thank you for feeding back comments to us. I will discuss internally, particularly with our legal team, and will come back to you quickly with some initial headline views on the points that you have made. As you say, we can consider the appropriateness of a meeting once I have done this.
Regards
Keith

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OFG-206210

From: McCutcheon, Joanne [mailto:Joanne.McCutcheon@detini.gov.uk]
Sent: 03 October 2012 10:20
To: Keith Avis
Cc: Hepper, Fiona; Hutchinson, Peter
Subject: Administrative Arrangemnts

Keith

Thank you for the initial draft of the Administrative Arrangements. Having received feedback from our legal consultants and reviewed the Agreement within the Department, I have a number of points to make.

Issues with current content

1. We note that it is an informal agreement without the status of a legally binding document. That being the case, if GEMA was to breach any provision or were to terminate the Agreement, DETI would have no legal recourse. We are not entirely comfortable with this position. Grateful if you could outline your reasoning for adopting this informal approach and also advise us of the position for the GB RHI and for the NIRO (as you are aware we have not been able to have sight of either of these Agreements). **Not sure why they haven't been able to consider the GB Regs, given that they can readily be accessed via the internet. It's correct that they haven't had access to NIRO. This is because NIAUR declined to agree to them having access! It is true that the arrangements are specifically expressed not to be legally binding. This was done because –**

(a) the relevant primary legislation (section 114 of the Energy Act 2011) uses the term "arrangements" rather than "contract" and, whilst it might be argued that the term "arrangements" is wide enough to embrace "contract", the latter word or similar would probably have been used had that been envisaged. Thus the assumption is that it was *not* envisaged and that "arrangements" implies something less formal. (There is certainly no *requirement* for a contract) That must mean something short of a contract and on that basis the provision specifying that the arrangements are not legally binding appears entirely appropriate;

(b) the parties to the agreement are two government departments who are seeking to reach agreement, pursuant to statute, as to the terms on which one will carry out on behalf of the other functions arising under that legislation and which that other Department would otherwise have to carry out itself, there being no lawful third possibility. Thus the relationship is not commercial in nature (it is grounded rather in legislation) and the parties are essentially not operating "at arm's length" in the sense that one would expect in a commercial context. The relationship is far more collaborative in nature and, in such cases, it is common practice for government departments to enter into memoranda of understanding or similar relatively informal arrangements to reflect the nature of the relationship between them.[Indeed efforts are being made to agree a MoU with DECC which would govern the GB RHI and, in the meantime, the relationship arising from the administration by the Authority on behalf of DECC of the GB RHI is governed not by contract, but by correspondence]. Square bracketed text needs checking for accuracy.

(c) On a related note, therefore, it would seem somewhat anomalous if the Authority's relationship with DECC was dealt with in the above informal manner but that was not the case for the NI RHI scheme;

(d) The NIRO arrangements were more formal in nature but the primary powers in the Energy Act 2004 were cast in virtually the same terms as section 114 EA 2011 so there was no more a legal requirement then that the relationship be based on contract than under the 2011 Act. It was nevertheless one possibility wand it was decided to deal with matters in that way. Why is not known but there may have been factors in play that do not arise in relation to NI RHI or, alternatively, it may simply have been assumed (incorrectly) that a contract was required.

(e) Given the nature of the relationship described in (c) above, it is not envisaged that either party would ever be minded to take legal action against the other and that any dispute would be resolved instead in a different fashion and in a non-confrontational spirit. [it is thus the Ofgem senior management view that the arrangements be informal] CHECK SQUARE BRACKETED TEXT FOR ACCURACY.

Whilst it is true that DETI would not have no "legal recourse" in the sense meant by DETI, in the event of a "breach" by us of the arrangements they would nevertheless be able to terminate the arrangements in the event that the matter could not be resolved amicably. The Authority would have the same right in the event that DETI were in breach, which leads on to DETI's point that they would have no remedy if the Authority terminated. That is true but presumably the Authority could not agree to enter into arrangements for the administration of the scheme were it not able to extricate itself from the obligation to do so with relative ease – [presumably senior management would confirm this] NEED TO CHECK SQUARE BRACKETS. NB also that it is proposed that the statutory review role will be allocated to DETI. There could therefore be situations where DETI effectively overturns decisions made by the Authority – i.e. where the review procedure is invoked by a participant

2. Clause 1.1 – Definitions of "Administration Costs" and "Ancillary Activities"

This appears to give GEMA the right to pass through all costs associated with the scheme without exclusion. We are not content with this position. **The concern is understandable. Presumably though they're not saying that they reject the principle outright but rather that, if they are to accept it, there will need to be clear agreement as to the basis on which the costs are calculated and the elements included in the calculation. Doubtless the answer to this will become clear once the proposed method of**

calculation etc. is shared with DETI. So we need to share ASAP and the matter is in hand. Firstly we need clarity in exactly how NI costs are going to be calculated going forward. For example, we would like a list of the various costs you anticipate and precise information on how DETI costs will be calculated - will it be actuals relating to the NI installations, or will it be a percentage of overall costs? **See above** We consider this to be an important area given recent conversations between Fiona and Matthew which have highlighted the unreliability of the estimates contained in the feasibility study and the current difficulty in providing robust projections. **Agreed** Just to be clear, we are going to need some degree of certainty going forward. I am sure you can appreciate we would be unable to agree to a 'carte blanche' on charging which this currently appears to be **understood and we are proposing to provide that via the proposed calculation methodology**.

3. Under 'ancillary activities' GEMA appears to have an unfettered right to perform any duties it deems appropriate. This would not be acceptable and we would need to see a list of anticipated ancillary activities and would have thought that any additions to this list in the future would need agreement of both parties (and would need to be costed in advance).

On the basis that there will indeed be at least some ancillary activities that are "necessary" to the performance of the functions that the Authority will be carrying out on behalf of DETI and some that are "desirable", it seems necessary to provide in the agreement for the Authority to undertake the ancillary activities. Otherwise there would be no power for it to do that which was merely desirable and, arguably at least, none to do what was necessary.

As to the principle otherwise of the Authority being given power to do what is necessary - given that, as the relevant clause makes clear, this means necessary *for the proper performance of the conferred functions* and that it seems beyond dispute that the Authority should be able to do what is necessary to "properly" (i.e. lawfully in the main) undertake the DETI functions, the provision should stay as it is - to the extent that it relates to "necessary" activities. It is not, though, sensible to try to list these necessary activities in the agreement as we could not be sure that the list was comprehensive. We might, however, be able to provide some examples and the Ops team should be asked to input to this process.

As regards "desirable", again it should be kept in mind that this is for "proper performance" of the DETI functions so the principle should ultimately be acceptable to DETI. Again, not sensible to include a list in the agreement (for the reason already mentioned) but could provide an indicative list with assistance of Ops Team.

We could commit to discussing with DETI the need for any additional ancillary activities arising in the future but the decision as to these should remain with the Authority. Wrong in principle to agree to anything less for "necessary" and unwise, probably, from the Authority's point of view, for "desirable"

One example of a "necessary" ancillary activity would seem to be making the necessary procurement arrangements with third parties and a desirable on would be running an enquiry line for potential applicants.

4.

Clause 2.2 GEMA's responsibilities

Under (a) (i) – 'in such a manner as it thinks best' – this should presumably be with the agreement of DETI. **But then it wouldn't be our "thought" and it needs to be - since the obligation is again linked to "proper" performance by the Authority of the DETI functions and a significant element in propriety is lawfulness. After all the Authority, notwithstanding that it will not be named in the NI regulations, will effectively stand in DETIs shoes and will be answerable to the courts for the lawfulness of the decisions it takes in administering the scheme, no less than in relation to the GB Regs.**

5. **Clause 3 (e)** – grateful for clarity on what is meant by 'matters of common interest and common concern' – we are content to consult GEMA on matters relating to the administration of the NI RHI. Are you thinking wider than this?

The reference should be to 3(f) not 3(e).

An almost identical provision was included in NIRO.

Reassuring to hear that DETI are happy to consult the Authority in relation to the administration of the RHI. We are not thinking wider than that - as the inclusion in the clause of the words "relating.....activities" makes clear. However the consultation referred to in this provision is *public* consultation and any public consultation re amendment of the NI Regulations or guidance would be undertaken by DETI. We are thus undertaking here to consult DETI on "matters of common interest and common concern" prior to any such public consultation and this should be welcome to DETI as our input may inform their subsequent public consultation.

We can't identify in advance what issues might be "of common interest and common concern". This will vary from case to case. The term is an umbrella one designed to cover any eventuality that might arise.

6. Clause 5 – Payment of the Administration Costs

We note that you propose that any billing disputes in relation to Administration Costs (i.e. the costs to GEMA of performing the Conferred Functions and the Ancillary Activities) are not adjudicated by an independent party and are decided by GEMA's Chief Operating Officer. This causes us concern particularly when read in conjunction with Clause 1.1. We would require some form of dispute resolution process iro Administration costs and would wish third party involvement where agreement cannot be reached.

An identical provision is included in NIRO.

The matter is ultimately one of policy NEED SENIOR MANAGEMENT INPUT IN THIS REGARD. Whilst we could in theory agree to what DETI propose, it is assumed that we will not want to be in any less secure position than under NIRO and we would be if we agreed to this as the scope for a dispute arising with DETI as to costs levels would be enhanced and there would be the prospect of our position being overturned by a third party.

7. Clause 7 & 8

We will obviously need to agree review dates, breakpoints/notice for termination. Meanwhile, grateful if you could advise exactly

what you are suggesting we would have a right of access to in terms of - data, metadata, systems, documentation etc, in the event of termination. Given our investment we would want to be clear on what we can expect. **They would presumably need to have access to everything, given that termination would entail that they themselves would have to assume responsibility for administering the scheme thereafter. Agreed however that an Ops Team view in relation to this should be sought.**

8. Clause 9.3

Have you some specific examples in mind? DETI would probably want to be informed before such disclosure.
The inclusion of this was prompted by the fact that it is in NIRO and that, should the need to apply the corresponding NIRO provision ever occur there it might occur in relation to NIRO too. We do not have any specific examples in mind and it is assumed that the provision is unlikely to be invoked. It should be retained therefore in case needed and does no harm if it is *not* needed. It is belt and braces in other words.

9. Clause 12.1 e

DETI would wish the appointment of Counsel to be agreed between GEMA and DETI. Is there any reason why GEMA would be unhappy with this ? **Yes. It might not prove possible to reach agreement. Agreed that, in view of that, it would seem sensible to stipulate instead that we should endeavour to reach agreement but that deadlock should be resolved by GEMA deciding.**

Issues not covered by current Agreement

10. We would need the Agreement to include some detail on performance targets, remedies and safeguards in place for underperformance. I cannot see anything on these issues in the current draft.

The "remedy" for underperformance would ultimately be termination of the agreement by DETI.
Moreover a "safeguard" can be found in the fact that the statutory review role will reside with DETI, meaning that there could potentially be cases where a decision of the Authority is overturned by DETI.
As to KPIs, these exist in relation to GB RHI but *are not being provided to DECC* as the view is taken that this would be incompatible with Ofgem's role as independent regulator. Although Ofgem is not the regulator in NI, our position is analogous in relation to NI RHI given that, by virtue of statute, we will be exercising functions that would otherwise have to be carried out by DETI and should exercise them independently of DETI as the effect is in essence that we *replace* DETI for as long as the arrangements are in place in relation to those functions that we agree with them we will carry out. Accountability should not, therefore, arise.

11. We will also require a right of audit entry to be included – this was discussed some months ago. **In principle the same analysis applies as in relation to KPIs. However it may be acceptable for DETI to *request* our agreement to an audit, so long as we were free to decline if we considered it inappropriate.**

I think this summarises the main issues. We obviously need to populate some of the gaps but I would have thought that this would be relatively straightforward.

There is probably no point in scheduling a meeting until you have had a chance to respond to the points raised and provided some of the detail requested. We will then need to revert to our own Accountability and Audit branches as well as our legal consultants. I think that would probably be the best point in time to have a meeting.

Fiona Hepper will be out of the office from the end of this week until Monday 29th October. We will off course be able to continue work on the Agreement in her absence and hopefully make substantial progress but you will wish to note that it will ultimately require her approval and signature. **Clearance will be required here too and the agreement still needs work apart from these issues. Moreover we don't know how long it will take to agree the entire content of the arrangements with DETI, all of which raises the prospect of DETI's 1 November date being in jeopardy.**

Regards

Joanne

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