

The Balancing and Settlement Code and Human Rights issues

1 Background

- 1.1 The Balancing and Settlement Code (BSC) is a component of the British Electricity Trading and Transmission Arrangements which specify the systems and methods of sale, purchase and transmission of wholesale electricity in England, Wales and Scotland.
- 1.2 The BSC also defines the obligations on ELEXON, the Balancing and Settlement Code Company defined and created by the Code, in providing or procuring the services necessary to operate the BSC arrangements efficiently. ELEXON is a wholly owned subsidiary of the National Grid company (NGC) and procures, manages and operates services and systems, which enable the balancing and imbalance settlement of the wholesale electricity market and retail competition in electricity supply.
- 1.3 The requirement to have the BSC in force is placed on the NGC through its Licence. All licensed electricity companies are obliged to sign the BSC. It is a condition of a Generation and Supply Licence that licensees are bound by the BSC and they must sign the BSC Framework Agreement which gives contractual force to the BSC (as well as the Grid Code and CUSC and CUSC Framework Agreement which give contractual force to the Grid Code).
- 1.4 The BSC contains obligations for the development and implementation of proposals to amend the Trading Arrangements by means of "Modifications". Proposed Modifications are subject to approval by the Office of Gas and Electricity Markets (OFGEM).
- 1.5 One such Modification under discussion is P173: Revised Settlement Arrangements for Emergency Instructions.

2 The Human Rights Act and the Convention

- 2.1 The Human Rights Act 1998 ("the Act") allows people to claim certain rights under the European Convention on Human Rights in UK courts, instead of having to go to the European Court in Strasbourg (although it does not exclude that option). The Act underpins this by requiring all public authorities in the UK to act compatibly with the Convention rights.
- 2.2 One of the Convention rights which is protected is that under Article 1 of the First Protocol to the Convention:

Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.

The preceding provisions shall not, however, in any way impair the right of the state to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure payment of taxes or other contributions or penalties.

- 2.3 Note that this is a heavily-qualified right in that it allows for deprivation or control of a person's property in the circumstances described.
- 2.4 The question has been raised as to whether the Modification Proposal P173 is compatible with this Convention Right.

3 Electricity regulation generally

- 3.1 There is little doubt that the statutory licensing regime under which the BSC is established and the statutory powers under which OFGEM operates mean that the system of electricity

regulation generally will be covered by the Human Rights Act¹. Specifically, it seems clear that a decision by OFGEM on a Modification Proposal will be the act of a public authority for the purposes of the Human Rights Act. This is assumed to be the case for the purposes of this note.

- 3.2 It is less clear whether the electricity generators themselves will benefit from the protections under the Act. The Government made it clear when the Act was a Bill passing through Parliament that privatised utilities, to the extent that they are performing public functions, are expected to be public authorities for the purposes of the Act. The significance of this is that it is commonly considered that a public authority cannot itself be a "victim" of a human rights infringement and so it is conceivable that utility companies could not invoke Convention rights on their own behalf². The law on this issue is unclear and so, for the purposes of what follows, it is assumed that an electricity generating company could be able to claim protection of its human rights.

4 Licensing and the code

- 4.1 The issue of whether the right to peaceful enjoyment of possessions might include a company having an unfettered right to construct and operate an electricity generating station has not been raised and it would be unlikely to succeed. It is taken for granted for our purposes that licensing of utilities' operations by the State is not in itself an infringement of the right under Article 1 of the First Protocol.
- 4.2 As a condition of licensing, a company is required to sign up to the BSC and Grid Code. Again, this requirement itself has not been raised as a possible infringement of the Article 1 right. However, a modification to the BSC can be treated as tantamount to a licence modification and might well engage the Article 1 right, although it is likely to be seen as happening within the context of State control over electricity generation in the public interest.
- 4.3 This has been put as follows when applied to an individual operator's licence:

"Such licence modifications are, more likely than not, controls of use within the [*right of the state to enforce such laws as it deems necessary to control the use of property in accordance with the general interest*] and energy regulators will need to show why such interference was justified, particularly where modification causes loss to the relevant operator, not least in circumstances where [The Utilities Act 2000] makes no provision for compensation."³

5 The general interest

- 5.1 In fact case law shows that States have a wide scope in terms of controlling the use of property in the general interest⁴. A court is likely to look first at the existence of any public interest justification. There are some pertinent factors which support the Proposed Modification to P173 to the BSC:

- it is understood that the Modification has been developed in the context of an Emergency Instruction which involves a generator ceasing to supply electricity to the national grid for reasons of safety and/or integrity of the network;

¹ This issue is considered generally in "The Human Rights Act and the Regulation of Utilities" by S Hamilton, *Util. Law Rev.* 10(3) May-June 1999.

² See for instance the discussion in "Business and the Human Rights Act 1998" by Michael Smyth, paras 3.140 *et seq*

³ *Ibid* paragraph 9.84.

⁴ see the judgment of the European Court of Human Rights in *Jokela v Finland (2002)*: "the Court reiterates that the national authorities -- with their direct knowledge of their society and its needs -- are in principle better placed than an international judge to appreciate what is "in the public interest". In performing their assessment in matters arising in the field of Article 1 of Protocol 1 the national authorities therefore enjoy a wide margin of appreciation".

- such cessation would be of temporary effect; and
- although an individual instruction will apply to a specific operator, the modification to the BSC will apply to all generators.

6 Compensation and loss

- 6.1 A number of decisions of the European Court of Human Rights give guidance on the requirement for and amount of compensation in the case of an interference with the Article 1 right.
- 6.2 As a starting point, and notwithstanding the general rule of thumb expressed in paragraph 4.3 above, case law has indicated that compensation for loss is not necessarily always payable in cases where there is a control of use of possessions by the State; "a right to compensation is not inherent"⁵.
- 6.3 However the Court has said: "An interference with the peaceful enjoyment of possessions must also strike a "fair balance" between the demands of the general interest of the community and the requirements of the protection of the individual's fundamental rights. Compensation terms under the relevant legislation are material to the assessment whether the contested measure respects the requisite fair balance and, notably, whether it does not impose a disproportionate burden on the applicant."⁶
- 6.4 In addition: "Compensation must normally be reasonably related to the value of the property taken, but Protocol 1, Article 1, does not guarantee full compensation in all cases. Legitimate objectives of public interest may justify reimbursement at less than the full market value; the nature of the property taken and the circumstances of the taking may be taken into account in holding the balance between public and private interests... a court will respect the national legislature's judgment in this respect unless manifestly without reasonable foundation."⁷
- 6.5 Clearly an arbitrary assessment of compensation is not likely to be acceptable. However, if one considers that the "circumstances of the taking" in the case presently under consideration carry the strong imperative of public safety and the integrity of the electricity supply and distribution system, there is a strong argument that "reimbursement" at less than full market value may be acceptable.
- 6.6 Putting all this together, a mechanism devised to deal with emergency situations, where there is a genuine attempt to recompense the generator in a transparent non-arbitrary way is unlikely to be outside the latitude allowed to States in controlling the use of possessions in the public interest – even if a "shortfall" in compensation leaves the generator "out of pocket".
- 6.7 The question of whether a generator will actually suffer a loss if the proposed P173 is implemented is a matter of fact. We understand that the aim of the proposed rules put the generator in a neutral position as respect his costs, in that the generator is still able to sell the electricity volumes it would have otherwise generated and sold⁸, even though the generation costs are not actually incurred, but that there may be a payment by the generator corresponding to the savings on those generation costs (fuel costs) subject to other avoidable costs which the generator may be entitled to recover.
- 6.8 In our view it is legitimate to look at the whole transaction within the context of the BSC in the round and at net effects; to focus on the payment made by the generator in isolation can be misleading when looking at the human rights implications.

⁵ Baner v Sweden (1989)

⁶ Jokela v Finland (2002)

⁷ Lithgow v UK (1986)

⁸ The effect of treating the emergency instruction as an acceptance is that the volume which would have been generated, but for the emergency instruction, remains credited to the generator for the purposes of calculating its imbalance.

7 Summary and Conclusion

- 7.1 The survey and analysis presented above have concentrated on a possible infringement of the human rights of an electricity generator under Article 1 of the First Protocol by a proposed Modification by P173 to the BSC.
- 7.2 For the purposes of this analysis we have assumed that decision on the proposed modification will be the action of a public authority for the purposes of the Human Rights Act and that affected generators may establish the status of "victims" of a human rights infringement.
- 7.3 It appears to be commonly appreciated that a system of regulation and licensing of an electricity generator or other utility's operations does not constitute an interference with human rights, but that individual modifications to a licence can fall within the scope of Article 1 of the First Protocol.
- 7.4 The Article 1 right is a highly-qualified right. The State is allowed a wide scope of control of the use of possessions in the public interest and the Courts are not likely to interfere.
- 7.5 An interference which arises by reasons of public emergency, is temporary and applies to all equally can be argued to be within the State's scope.
- 7.6 A right to compensation does not always arise in circumstances of state control in the public interest. However, it is likely to indicate whether the proper balancing of public interest and individual rights has been carried out.
- 7.7 "Full" compensation is not always required but compensation should not be assessed arbitrarily. A mechanism which results in a person being "out of pocket" does not necessarily infringe the Article 1 right; it depends on the circumstances and the scope allowed by the State to control possessions in the public interest.
- 7.8 The Proposed Modification is intended to place a generator in a "cost neutral" position in the event of an Emergency Instruction (when looking at net results) and in doing so is compatible with the scope allowed to the States and is unlikely to amount to an infringement of the Article 1 right. Even if the effect were to leave a generator out of pocket the fact that it is a genuine attempt to recompense the generator in a transparent non-arbitrary way is unlikely to be outside the latitude allowed to States in controlling the use of possessions in the public interest in an emergency situation.