

Sizewell C - A Concatenation of Conflicts and How to Deal With Them

Governance and Stewardship review of NNB SZC

Detailed submission to Planning inspectors' Inquiry for Sizewell C - Finance and Funding by Mark Goyder¹

EXECUTIVE SUMMARY

This paper draws on 30 years of experience in the fields of governance and stewardship. It deals with two issues. The first is the undefined identity and character of those who might eventually have ownership of NNB SZC. The second is the implications for governance of financing arrangements which transfer risk away from investors and the applicant company, and on to the electricity bills and tax burden of ordinary people.

- 1) The application made in the name of NNB SZC is effectively a **Ghost Application**. The applicant is making promises on behalf of unknown owners and investors. These are promises with which current and future stakeholders will have to live for more than a century. The Planning Inspectorate is being asked to consider an application without knowing the true ownership or indeed identity of the applicant, let alone its values, its priorities or its ultimate intentions. In the light of these extraordinary circumstances, the best course of action in the event of any positive decision would be for **approval to be provisional**. When and only when there is a tangible and credible company with identifiable investors committed to responsible stewardship could the inspectors evaluate the robustness of the promises being made. In particular they should, at that point, ask the applicant to prepare a [board mandate](#) after discussion with the owners and key stakeholders.
- 2) **The proposed financing arrangements place an unprecedented stewardship responsibility in the hands of the Planning Inspectors.** Changes from the model used for Hinkley have profound governance consequences. **They shift the balance of risk. They protect the investors while financially exposing the ordinary citizen** in the event of overruns and overspends. Ideally the Planning Inspectors would **recommend that the UK Government revisits the current plans with their built-in rewards for failure**. In the absence of any change, and if planning permission were to be granted, there would have to be an independent chair, and representation on the board of current and future risk-bearing stakeholders - the electricity consumers, the taxpayers and the affected communities. These, more than investors are the ones most at risk in the event of delay and overspend. **In reaching their decision on the application, the inspectors are asked to recognise the heavy responsibility that they would bear if, as a result of**

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permission being granted on the present terms, undue burdens were placed on future generations of local and national stakeholders in order to benefit absentee investors.

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The Corporate Governance background

Corporate governance is about leadership and accountability. It is the system that keeps organisations and their owners and leaders honest through holding them accountable to those who risk their money and their effort, and who are affected by the organisations actions. It includes accountability for the longer term consequences of the organisation's actions.

In this instance we are dealing with governance in the widest sense - the governance not only of a company, but a company contributing to a national infrastructure project in line with the nation's policies and priorities. Good governance is essential to the system working as intended to achieve the national policy objectives.

In his book 'Stop the Rot' the leading corporate governance expert Professor Bob Garratt describes two elements of governance.

The word has had dual and linked meanings throughout - giving direction into the future and simultaneously ensuring the prudent current control of an organisation. ²

He goes on to describe four major groups as crucial to our, currently imperfect, system of governance.³

-Boards of directors

- Owners-

-Regulators

-Legislators.

Legislators set the rules for the other players. They create the laws within which boards and owners may operate in a market. They also set up regulation which is especially necessary where - as is the case with energy - monopolies or oligopolies may be involved.

In the case of major infrastructure projects the legislators have established the unique process of inspection on which the Sizewell C Planning Inspectors are currently embarked. The Planning Inquiry itself is therefore by definition an essential moving part in the total machinery of governance. Their focus is not only on Sizewell C but also on the operation of the whole system by which the nation's energy needs will be met. (Admittedly it is not the only moving part. For example the Office of Nuclear Regulation has to decide on the suitability of the proposed operator before it can grant a licence.)

It is logically impossible to separate the merits of the application from the proposed governance of the project and from the merits of the particular applicant. Obtaining planning approval is dependent on a series of important assurances and commitments. This becomes quickly evident from reading the national policy statement which identified Sizewell C as a possible site. Biodiversity, habitats, employment, listed buildings, traffic

² Stop The Rot – Reframing Governance for Directors and Politicians Bob Garratt Greenleaf Publishing 2017 p4

³ Ibid p22

congestion, tourism and many other concerns are acknowledged as potentially tricky issues which have to be handled if the site is in fact to prove suitable. The decision to include Sizewell as a possible site is dependent on confidence that the organisation described as the ‘nominator’ of the site (i.e. EDF) can overcome the difficulties and deliver on its assurances. If a planning inspector were to conclude that the promises and commitments and safeguards from the applicant were acceptable on paper, but unlikely to be delivered by that applicant under the proposed governance arrangements, in practice, then it would make no sense to grant the application.

The Stewardship Background

The second part of effective governance, as defined by Professor Garratt, is perhaps the most difficult because it involves giving direction into the future.

The concept of stewardship has been growing in importance in the last 20 years and is now having an increasing influence on economics and finance. It is the subject of a Stewardship Code for investors in the UK and many other countries.

Stewardship means a commitment to pass on the assets one has inherited or created onto one’s successors in better condition. It is second nature to the farmer who has inherited land on which her or his ancestors previously farmed. It is, or should be, the concern of every legislator and every regulator. It is becoming legally central to the concerns of pension funds that are charged to look after more than merely the financial interests of their beneficiaries.⁴ The growing influence of these champions of stewardship can be seen in two recent cases. In the first of these [Royal Dutch Shell has lost a court case brought against it](#). The court used the phrase ‘unlawful endangerment’ and affirmed that there was a climate-related duty of care. Meanwhile Exxon has seen the election, against the wishes of the company, of two climate activists to its board. Stewardship is on the march.

The principles of stewardship may not mean much when one is dealing with an application to build a small piece of infrastructure which can be dismantled within ten years. They become paramount when one is dealing with infrastructure that will take a decade to build, 60 years to operate, and an unknown time - and an , as yet, unproven method - to dispose of all the hazardous waste safely. The obligations of stewardship make it impossible for any application to be granted without a clear understanding of the safeguards offered to those affected, especially those who bear the greatest risk.

Discounted cash flow models tend to prioritise the here-and-now. Stewardship principles prioritise the claims of future generations. In economics and finance theory, the first gets more attention because it is easier to measure. Yet the real-world costs of neglecting stewardship are all around us - in decades of unnecessary deaths caused by the tobacco industry, or the waste and misery caused by housing developments built in areas with high flooding risk.

For these reasons, stewardship is increasingly demanding the attention of regulators. As the ancient Native American saying puts it, *we do not inherit the land from our ancestors; we borrow it from our children.*

⁴ See especially Chapter 4 of *Entrusted: stewardship for responsible Wealth Creation* – Ong Boon Hwee and Mark Goyder World Scientific 2020

The Financing and Ownership Background - Hinkley

For the Hinkley Planning inquiry EDF was the applicant. It said that it would establish a new company - NNB Generation Company (HPC) but the inquiry was conducted on the basis that EDF would be majority owner of the new company. Indeed the planning permission [is generally described as having been granted to EDF Energy](#), as if the creation of NNB HPC were a mere technicality. When Hinkley Point was approved EDF remained the majority owner with 65% of the shares. The minority shareholder was and is China General Nuclear.

As majority owner and operator, putting up 65% of the capital itself, EDF was granted a special privilege through a new system called Contracts for Difference (CFD). This is a government guarantee of the price NNB will be assured of when selling the electricity it generates. Crucially EDF and CGN were liable for most of the costs in the event of the project exceeding budget. The assured revenue gave EDF comfort but the buck largely stopped with it (together with CGN) as constructor, owner and operator.

The Financing and Ownership Background - Sizewell

Because of the financial weakness of EDF, the UK Government has changed the proposed financing mechanism for Sizewell C from that which is in operation at Hinkley. This has significant impact on key stakeholders and therefore has implications for governance and stewardship.

The UK government proposal for financing Sizewell C is known as the Regulated Asset Base. (RAB)

There are two major differences between RAB and CFD. First, under RAB, consumers would pay a surcharge on their bills up to the point the plant entered commercial service, while under CFD consumers do not start to pay until the plant is in service. The surcharge would pay the finance costs up to the point of operation so the owners would essentially receive interest free loans during the construction period. These costs would be paid from the point the deal was agreed and money began to be spent, allowing the developer to recoup the cost of getting the deal to Final Investment Decision.

The effect of the change is to load on to the ordinary person in England and Wales the risk of cost overruns. In the case of Hinkley these will be borne by the company up to a threshold - which is as yet to be defined - beyond which the UK government, and therefore the UK taxpayer, would bear the costs. There will be something called a Government Support Package agreed, which is the "cap" above which HMG would have to step in and pay for things which cannot have been foreseen.

Whether the extra costs will be borne by the electricity consumer or the UK taxpayer, the one certainty is that, for Sizewell C, they will not be borne by NNB SZC or its shareholders. The worse the underperformance of NNB SZC, the more the electricity consumer and/or taxpayer will have to pay. **The public would be subsidising the investors to ensure that they achieved their guaranteed profit level.**

Should this arrangement not be changed, corresponding changes will need to be made to corporate governance. As many controversies over chief executive 'Rewards for Failure' have illustrated, it is a basic principle of governance and indeed fairness that both influence and rewards should be proportional to risk. The UK public and the UK investment industry have already rebelled against huge 'golden parachute' payments that guarantee CEOs a large lump sum if they are dismissed. **The current plan for Sizewell C builds in 'Rewards for Failure' by the operator and its owners. If the Planning Inspectors approve this without amendment, they will be bequeathing an unmanaged risk to the UK government, to the electricity consumers, and to the general public.** The risk is obviously largest for those living near Sizewell and impacted by it. These are the people who will already have to endure the destruction and disruption during the ten year construction phase. The current arrangements would add insult to injury. With every month that construction was delayed and budgets were exceeded, the price to these long-suffering people would rise too! If they do nothing else it is vital that the inspectors draw attention to the 'Rewards for Failure' built into this plan.

The second, crucial, difference is in the proposed ownership of NNB SZC. As already mentioned, the position on Sizewell is quite different to that for Hinkley. At Hinkley it could truthfully be said that EDF was applying for a permission to allow it to operate the plant that it would be building. **At Sizewell it could truthfully be said that EDF is applying for permission for unknown people or organisations to build and operate the plant.**

Nobody knows who is going to own the company building and operating Sizewell C. It is not going to be the people now required to take the ultimate financial risk - the UK electricity consumer. All we know is that EDF will be, at best, a minority owner. Here is what EDF has said in its current submission to the Planning Inquiry (p37).

"The ownership of SZC Co. for the construction period is expected to be made up of third-party investors (predominantly pension investment funds which may include foreign investment) but has not yet been fixed"

Keenly aware of the scepticism about the ownership of UK strategic and defence-sensitive assets by overseas third parties, EDF hastens to add the following justification.

Foreign investment has been used to enable infrastructure development throughout the UK and external finance (equity and debt) is expected to be required to fund the construction of the Sizewell C Project. Although EDF Energy and China General Nuclear (CGN) have funded the development phase of Sizewell C to date, this will change for construction and operation of Sizewell C. In order to operate Sizewell C, SZC Co. must obtain a Nuclear Site Licence from the Office for Nuclear Regulation who will consider the Project to a great level of detail including considering an assessment of national security."

Issues of Concern

To summarise the issues of concern around governance and stewardship.

- 1) Unlike Hinkley this is a **Ghost Application**. The Planning Inspectorate is being asked to consider an application without knowing the true ownership or indeed identity of the applicant, let alone its values, its priorities or its ultimate intentions.
- 2) Unlike Hinkley, the ultimate financial risk bearers are not the 'investors', but the electricity bill-payers and the UK taxpayer. This plan builds in **rewards for failure** for the applicant and creates a **moral hazard**. It is the electricity consumers, the UK taxpayer, and those who live in the area who are putting their financial, human and natural capital at risk.

It is of course technically possible for the planning inspectors to say that this is not their problem: if the required promises and assurances exist on paper, it is not for them to worry about changes of ownership or lack of finance.

Consider other examples. [It is emerging from the inquiry into the Grenfell Tower tragedy](#) that, had the relevant Kensington and Chelsea committee probed rather harder, it might have discovered that questions had been raised about the safety of the cladding that was to be used. The failure to ask these questions will haunt the councillor responsible for the rest of his life. Probing into these questions may, strictly, have meant moving outside the defined remit of that committee. Yet that councillor had - and missed - the opportunity to ask the right questions about these matters and insist on action by others if the answers proved to be unsatisfactory. Stewardship demands of us all the widest sense of responsibility for the impact of our decisions on future generations. My recommendation is that the Planning Inspectors take their opportunity, and proceed in line with the following recommendations.

Recommendations

- 1) If the Planning Inspectors are minded to approve the application, do so conditionally. Ask that the application be resubmitted by NNB SZC when the ownership of the company is known and the board and senior management has been identified, and a full [board mandate](#) developed which clearly sets out the company's priorities, values and intentions.
- 2) If they are minded to grant the application without the conditions mentioned in 1) they should make approval dependent on governance arrangements appropriate to the unique circumstances resulting from the 'ghost applicant' and the RAB/ moral hazard problems. These arrangements would offer due protection to the **risk-bearing stakeholders** - i.e. the UK taxpayer, the affected electricity consumers, and the communities and businesses immediately at risk as a result of the huge construction impact. These arrangements could include the creation of a Supervisory Board including the following:
 - The chair of NNB SZC should be independent of EDF or its financial backers. Her/his appointment to be open to nomination by and subject to approval of the risk-bearing stakeholders.
 - NNB/SZC board composition should be as follows

- One third of seats on the board of NNB appointed by the financial investors (EDF, CGN etc)
 - One third of seats on the board to represent risk-bearing stakeholders ranging from local authority representatives, RSPB and electricity consumer organisations, and heavily impacted business in the region, and other stakeholder interests.
 - One third of seats on the board to represent stewardship considerations including the long-term interests of UK - such as an expert in the disposal of nuclear waste, an expert in coastal erosion and protection, a representative of the tourism and hospitality sector, and an expert capable of drawing together the threads of the Scottish Power and many other incursions along the coast which form part of the total impact.
 - A suitable high level forum would meet four times a year to receive reports from NNB SZC. It should be co-chaired by a government minister and a co-chair selected from all the affected local groups. Reports from the forum would be published and monitored by the relevant planning authorities who would be fully empowered to require remedial action funded by the NNB SZC.
- 3) The above arrangements could be reinforced by the UK Government retaining a Golden Share, with the ability to veto any inappropriate proposal from the owners
 - 4) In announcing their decision, and explaining why these governance arrangements are required, the inspectors are invited to draw attention to the 'Rewards for Failure' which are built in to this plan and to recommend to the UK government that it finds a more equitable basis for risk-sharing. Clearly if the investors were to take on more of the risks then the governance arrangements could be adjusted to offer them a stronger controlling influence.

1 June 2021

Appendix - Summary of Mark Goyder's remarks to the Open Floor Hearing

- 1) I asked the inspectors to favour a twenty-first century view of the economy - one which is in harmony with nature and which builds on the strength of all the capitals- natural, social, human as well as financial. Not a twentieth century view in which harm to natural, social and human capital is somehow justified by volume of output.
- 2) The inspectors should look carefully at the literature of mega-projects, and the evidence from research that these are uniquely fragile. Those proposing them rarely succeed in delivering what they promise. The assumption from experience must be that Sizewell C, like most mega-projects, will overspend its budget, overrun its timetable and fail to deliver on the safeguards and promises that have been made to the affected public.
- 3) As has been effectively argued by others, the technology being deployed to produce these outputs is already outdated and underperforming and, by the time construction is completed here, can justifiably be described as a 'white elephant'. If nuclear is required there are more modern technologies with which offer better return on investment without the mega-destruction involved.
- 4) Given the known fragility of megaprojects, the reliability of the proposed operator becomes crucial. So much depends on their ability to keep promises in the decade of construction and the century and more of operation and half life; to deliver promised safety, noise, pollution and traffic mitigation, to understand the geology and the dynamics of a delicate coastal location; to manage the project prudently and with sensitivity to local concerns. Other speakers have identified EDF's shortcomings in this regard. My focus is on the unknown quantity called NNB SZC - a new company formed to take the project forward which has, as yet, no leadership, no management and no-one committed to owning and controlling it except a promise of a 20% stake from Chinese state-owned energy corporation China General Nuclear. In other words the Planning Inquiry must have regard to the stewardship and governance vacuum at the heart of this application. The Inquiry should ask itself whether there is a single example of a permission being granted for such a fragile long-term project when its ownership and direction is at best remote and at worst entirely unknown. The unwillingness to invest shown by L&G and other leaders in responsible investment tells its own story.