

Minutes of the Meeting of the Gas and Electricity Markets Authority

Thursday, 26 April 2007 at 8.15 am

Ofgem, 9 Millbank, London SW1P 3GE

Introductory remarks by the Chairman

1. The Chairman noted that there were no apologies for absence. A potential conflict of interest had been registered in relation to part of the content of one agenda item and the Member (who had not received the relevant paper) agreed not to take part in discussion of these aspects but would provide comments separately, and as necessary, to the Chairman. The Chairman noted that one additional paper had been circulated, this dealing with proposals from the Electricity Retailers' Association on smart metering. The Chairman suggested and it was agreed that he would brief the non-Executive members on the results of the recent discussions of the Remunerations Committee on senior staff salaries. The Chairman recalled that the Authority would be joined at lunch by Lord Whitty (Chair) and Ed Mayo (Chief Executive) of the National Consumers' Council. Finally, the Chairman said that Professor Len Waverman would be stepping down from the Authority soon after the meeting. He had made a very significant contribution to the Authority's work over the preceding five years on both economics and competition policy matters. The Authority added their thanks and wished Professor Waverman well for his new post in Canada.

Reports from the Chief Executive and Managing Directors

2. The Chief Executive drew out the following main issues from his report:
 - On the full-year financial analysis for 2006/007, the achievement of RPI-3% for Ofgem's expenditure, for the second year in succession, during a year of high activity particularly on price reviews, and with substantial reorganisation.
 - The consequent and cumulative return of some £5.6m to licence payers over two years which exceeded the figure which the cost control regime had been estimated to achieve over its full five year period.
 - Aspects of operational performance for the year including sound delivery against targets for modifications, FOI requests and the ECM project.
 - Key indicators showing a good HR performance, including the introduction of a new graduate entry scheme.
 - The promotion of Charles Gallacher to the post of Director, David Halldearn's new role as a senior adviser on European matters and the imminent retirement of Nick Simpson after his work on the ECM project.
 - An analysis of performance, and of current mergers and acquisitions activity in the energy market businesses, nationally and internationally, and the role of Ofgem in providing advice, as requested, to OFT.

- A review of the key European energy developments, the central role being played by CEER and ERGEG, and the timetable for taking forward the Commission's plans for regulation of the EU market.

The Authority welcomed this briefing, offering its congratulations to the Chief Executive and all Ofgem teams for the favourable financial outcomes for 2006/7 and the sound results against target across the business.

3. On corporate affairs, the Authority was briefed on developments relating to the Energy White Paper and the audit of Ofgem by the Sustainable Development Commission. The Authority noted recent amendments tabled by Government to the Consumers' Bill before Parliament proposing new duties for Ofgem to set complaints standards. The Authority noted continuing concerns about the recalibration of pre-payment meters and steps taken to write to the new management of Scottish Power to press for further action. The Authority was updated on plans for publication of a Supplementary Statement of Objections in respect of a potential case under the Competition Act 1998. The Authority welcomed the launch of the new Ofgem website and looked forward to an update on the new Consumer First project and consumer issues at its next meeting.
4. On networks, the Authority discussed the current issues on the construction of the gas pipeline from Milford Haven and the implications of the recent decision by the High Court to overturn the planning permission granted by Neath and Port Talbot Council in respect of a pressure reduction installation on part of the pipeline's route. The Authority was informed of the complaint to the European Commission by one company in respect of aspects of National Grid's charging methodology for electricity. On modifications, the Authority was briefed on the industry reactions to UNC 90 in respect of reformed GDN interruption arrangements; and on the decision taken on UNC 116.
5. On markets, a presentation was given to the Authority on the recent announcements on cuts in domestic retail energy prices to consumers and an analysis showing that competition remained vigorous in the domestic retail market based on an examination of prices, innovation, service, movements in market shares and switching.

Minutes of the meeting of the Authority on 22 March, 2007

6. These were approved as circulated

Smart metering

7. The Authority reviewed a paper which examined a set of proposals recently been put forward to Ministers by the Energy Retail Association (ERA) on the rolling out of smart gas and electricity meters, and the installation of visual display units; and the terms and conditions under which the six major companies involved believed should apply. The Authority noted that it was suggested by industry that this might work through a franchise model under which a set of regions would hold a competitive tender for a monopoly in that area to provide smart gas and electricity meters to all customers, with HMG or Ofgem overseeing tender rules and advising on the mechanisms for recovering stranded costs for the early retirement of existing meters. Ofgem had met the ERA to seek information about its proposals.

8. The Authority discussed, on a preliminary basis, some of the issues from these proposals. It recalled the research which Ofgem had led in 2006 on the benefits of smart metering, its consultations, and the Authority's view that the competitive market would be the best route for delivery of smart metering. The Authority also noted the continuing work on reducing barriers to the introduction of smart metering methods such as minimum standards and interoperability. Ofgem was also managing, for Government, the Energy Demand Reduction Trial designed to assess a range of different solutions, including new forms of metering and consumption display devices. The Authority examined some of the policy issues and choices which might arise from the industry's proposals, and agreed to consider these further.

Winter 2006/7 and Outlook for 2007/8

9. The Authority received a presentation on aspects of the Winter 2006/7 experiences and the initial energy outlook for Winter 2007/8, following the publication of National Grid's initial Winter Consultation report and the Ofgem "Winter to Date" seminar held with industry interests in late March. A number of new infrastructure projects were expected to come on line potentially increasing the supply of gas to the GB market over Winter 2007/08. These included the new link with the Orman Lange field in Norway; capacity enhancements at the German/Belgian border; LNG import prospects and the possibility of LNG delivery through Milford Haven (but with remaining uncertainties due to planning delays to delivery of the necessary transportation capacity). The outlook for gas supply was therefore more positive than last year. Non-storage supply could be higher than during last winter. It was noted that GB forward gas prices for winter 2007/8 were currently higher than outturn for winter 2006/7. This might reflect a number of factors such as the risks of higher demand, oil-indexed continental gas prices, LNG prices in the US and the potential diversion of cargoes, and possibly market views on network constraints.
10. On electricity, the position appeared comfortable, even for a 1 in 50 cold winter, with sufficient plant to meet demand given projected gas supplies as a feedstock for generation, assuming that plant breakdowns or CCGT unavailability were not significant. On prices, forward electricity prices were also higher than last year. This was driven by three main factors. Gas prices were trading at a premium compared to winter 2006/7 outturn prices. Increased carbon prices would feed through under Phase II of the EU Emissions Trading Scheme from 1 January 2008. Finally, there was the impact of the EU's Large Combustion Plant Directive and its restrictions on coal and oil generation from January 2008. The Authority welcomed these analyses, reviewed the timetable for future work on the Winter Outlook report and consultations, and commended the teams on their proactive work with consumer interests.

Supply Licence Review

11. The Authority considered a paper on the development and presentation of proposals for the final stages of the supply licence review, a two year project to review all Ofgem supply licences, and a 'flagship' Better Regulation project which had involved significant commitments from the industry and other stakeholders. The new approach would shorten all licences and would halve the number of licence conditions, with the standard conditions now reduced from around 160 pages to 60 pages. All stakeholders had welcomed the clarity and style of the new conditions.

The new licences would provide a more proportionate and appropriate level of regulation for the competitive retail market whilst maintaining important safeguards for vulnerable customers.

12. On policy issues arising during the review, the Authority considered an analysis of the consultation results on the proposal to remove the present obligation to inspect meters every two years, allowing suppliers to have greater control over management aspects. The Authority concluded that the present proposals should stand as licence conditions for the time being but with provision for an Authority derogation if suppliers could satisfy Ofgem that this would not compromise safety. The Authority also considered advice on the matter of free gas safety checks for certain qualifying customers, already an obligation on suppliers, agreeing that some extensions to the eligible groups would be desirable as condition of supply licence, and on which further consultation was in progress. On pre-payment meter recalibration, the Authority agreed the proposals adopted for consultation in December 2006 to address consumer concerns arising from delayed recalibration of token meters. Finally, the Authority considered the means of presentation of the statutory modification notice, including the procedural and legal aspects, concluding that it should be presented as a package of separate licence modifications rather than as a single proposal.

Financial penalties

13. The Authority reviewed a paper on financial penalties and concluded that its current policies and powers were adequate at present but asked Ofgem to continue to keep these under review in the light of changing needs and wider developments, such as implementation of the Macrory review November 2006.

DPCR5

14. The Authority considered a paper setting out the overall approach and strategic issues arising for the next electricity distribution price control (DPCR5). The review would be starting in early 2008 and should reach final conclusions in late 2009. The proposal was to consult soon, through an open letter, on the major topics which Ofgem considered might be addressed, in order to gather and assess stakeholders' views prior to the formal start of the review. Issues on which views would be welcome – in addition to the financial and efficiency aspects which would also form part of the review – could include roles and responsibilities in respect of distributed generation; output delivery with less emphasis on opex and capex allowances; incentives packages; and some procedural issues for the conduct of the review, such as improved consumer inputs. The Authority noted the wider context of energy policy developments and agreed the approaches suggested in the paper, together with the overall timetable of the review.

NTS exit capacity and interruption incentives for GDNs, 2010/11

15. The Authority discussed a paper seeking approval for an extension of the GDNs' transitional exit capacity and interruption incentive to cover the 2010/11 gas year in the light of the decision taken by the Authority to delay implementation of Mod 116 (NTS offtake) and Mod 90 (interruption reform) by one year. The Authority noted that the proposed scope and form of the incentives would be as in the current incentives, though

incentive target values would be appropriately updated in line with exit capacity volume forecasts for the 2010/11 period. The Authority confirmed its agreement to these proposals, and agreed that it need not be consulted further in advance of any statutory consultation on associated modifications to the GDN licence conditions.

Investigation case

16. The Authority reviewed an update paper concerning an apparent breach by a DNO of a licence obligation. The Authority confirmed, in the circumstances of this specific case and in accordance with its rules of procedure, that the MD Networks, in consultation with the MD Corporate Affairs, should be delegated to determine the question of breach and penalty as appropriate.

Communications Strategy

17. The Authority considered a paper and presentations on aspects of its communications strategy for 2007/8. This addressed the major media and policy issues facing Ofgem in the year ahead, and the associated opportunities and risks. This analysis was welcomed by the Authority, its key elements endorsed, and the planned activities agreed.

Other business

18. There was none.

Date of next meeting

19. This was agreed as 24 May at 8.15 am.

Those present

Sir John Mogg (Chairman)
Alistair Buchanan (Chief Executive)

Dr Robin Bidwell
David Gray
Miriam Greenwood
Judith Hanratty
Sarah Harrison
Jayne Scott
Steve Smith
Prof Len Waverman
John Wybrew
Prof George Yarrow

Those attending

Charles Gallacher	(all items)
Roy Field	(CE's report)
Philip Davies	(Metering, winter outlook, Supply Licence Review)
Rachel Fletcher	(Metering)
Maxine Frerk	(Supply licence Review, Penalties, Licence breach)
Martin Crouch	(DPCR5, licence breach)
Joanna Whittington	(GDN incentives)
Lewis Hodgart	(")
James Hope	(Investigation case)
Pamela Taylor	(")
Gordon McDowall	(")
Stuart Hudson	(Communications review)
Trevor Loveday	(" ")
Michael Brocklehurst	(Legal Adviser to the Authority)
Dr Tony Burne	(Secretary to the Authority)