

## Office of Gas and Electricity Markets

Report of the Gas and Electricity Markets Authority for the period 1 April 2001 to 31 March 2002, to the Secretary of State for Trade and Industry.

The document comprises a report made under section 5(6) of the Utilities Act 2000.

## Office of Gas and Electricity Markets

Ofgem is the Office of Gas and Electricity Markets, regulating the gas and electricity industries in Great Britain.

Ofgem operates under the direction and governance of the Gas and Electricity Markets Authority which determines strategy and policy priorities.

Ofgem's powers and duties are provided for under the Gas Act 1986, the Electricity Act 1989, the Competition Act 1998, the Utilities Act 2000 and other statutes.

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# 1. Foreword by the Chairman and Chief Executive

This report covers Ofgem's work in the year 2001-2002. As in previous years, there are common themes which unite all that Ofgem does. Our overriding aim is to help promote choice and value for all gas and electricity customers, present and future. Everything we do is designed to protect and advance the interests of consumers, wherever appropriate through promoting effective competition. We rely on regulation only where competition is not possible or insufficiently developed. All our work is measured against these common themes.

This report allows you to judge how Ofgem has performed. As before, we are reporting against the priority headings used in our Plan and Budget for 2001-2002 and providing full details of how Ofgem performed against each major target identified.

Ofgem's work in 2001-2002 was again far-ranging and intense. Amid all this activity, it is sometimes difficult to see the most important developments. The following were of particular significance.

1. A continuing preoccupation of Ofgem is to make competition work for all, especially for those most in need. Our **Social Action Plan** is vital in helping achieve this. It is, therefore, very satisfying to see that customers on lower incomes are taking as much, if not more, advantage of competition by switching suppliers as those who are better-off. Importantly, energy companies are coming forward with a range of offerings especially tailored for customers in need as part of the competitive market rather than through an imposed social obligation. Because of these developments it is now possible to rely increasingly on Ofgem's powers under the Competition Act, rather than direct regulation of end prices, to protect the interests of all consumers.

Ofgem will continue to act to penalise companies whose sales practices fall short of what is properly expected. Although instances of misselling are experienced by a very small proportion of all energy customers approached by salespeople, they remain at unacceptable levels. Ofgem is determined that the companies address this seriously, effectively and rapidly.

2. Although Ofgem has succeeded in withdrawing from directly regulating around 70 per cent of all activities regulated at the time of privatisation, the need for **price regulation of the pipes and wires natural monopolies** remains. They account for between 30 and 40 per cent of domestic gas and electricity bills.

The Transco price control in 2001-2002 completed the round of controls begun in 1999. They are difficult to do well, requiring a carefully balanced judgement of what efficiency gains can reasonably

be made without choking off investment. All the signs are that we have struck this balance: consumers are benefiting in total by more than £1.25 billion each year, none of the companies is finding it difficult to raise finance, new equity is entering the sector and physical investment is growing. As important, Ofgem has significantly developed the concept of RPI-X regulation to place more emphasis on outputs, including quality of service, maintenance of assets, and investment in response to demand. I am glad to say that the companies are responding by engaging more constructively in the process, which will serve all interests well.

3. 2001-2002 was the first full year of the **New Electricity Trading Arrangements (NETA)**. NETA has performed far better against the objectives originally set than anyone could have reasonably expected. Wholesale electricity prices are now 40 per cent lower than they were when reform started and most electricity is now traded like any other commodity. The demand-side is playing an increasing part in setting prices, the trading exchanges are functioning well and liquidity is increasing.

Crucially, the systems, both IT and financial, passed the severe and major test of Enron's failure without interruption or dislocation. As it was designed to do, the corporate governance of NETA – quite unlike that of its predecessor, the Electricity Pool – has allowed changes to be made promptly and effectively.

It is notable that, in the balancing arrangements, these changes have led to a significant reduction in price volatility. The difference between the prices at which participants have to sell and buy electricity from the National Grid Company (NGC) to balance their positions, which has been a major source of contention, has reduced from £70 per MWh at Go-Live, to £17 per MWh today. By increasing competition, NETA has affected all, including smaller, generators which has been a matter of much public debate. It is important to distinguish between the general effects of greater competition on wholesale electricity prices, which impose pressure on all generators, and specific issues associated with the detailed NETA operations. Ofgem continues to monitor the position and make changes to improve the operation of the balancing arrangements.

Both Ofgem and the Department of Trade and Industry (DTI), as the organisations jointly responsible for NETA, as well as industry participants, can take great satisfaction from its performance, which has brought about a much more competitive wholesale electricity market to the benefit of customers.

The past year has been marked by an intense debate on **energy policy**. The Performance and Innovation Unit's (PIU) energy policy review illustrated how difficult the trade-offs are between the contribution that energy policy can make to economic competitiveness, helping tackle fuel poverty, meeting environmental goals and ensuring security of supply.

This is the circle of **sustainable development**, in its widest sense, that has to be squared. Ofgem's role in this is defined by the statutes that give us our duties and powers and provide the basis for all that Ofgem does. Within the scope of these duties and powers, Ofgem will continue to work to make its full contribution to resolving these trade-offs.

We can best do this in two ways. Firstly, by establishing a clear basis of facts for the analysis of difficult issues, as we did in the major piece of work on security of supply submitted by Ofgem to the PIU. Secondly, by developing practical and effective solutions to policy challenges, as we are doing in Ofgem's work on distribution and transmission. This work is designed to enable the electricity system in the future to continue to operate at the standards of performance and service that consumers properly expect, while at the same time accommodating substantial amounts of distributed generation that will be required to meet important environmental targets.

I hope that this report makes clear the impact Ofgem is making on the development of the energy industry. Making a difference on behalf of consumers drives Ofgem. It is making this difference that makes Ofgem worthwhile for those who work here. I am, as always, grateful to my colleagues, both those on the Authority, which directs Ofgem's activities and policies, and those responsible within Ofgem for developing and executing them, for all that they have done over the last year to deliver such far-reaching results against difficult and demanding objectives.



**Callum McCarthy**

Chairman of the Gas and Electricity Markets Authority  
Chief Executive of Ofgem

## 2. Ofgem corporate structure



John Belcher



Lord Currie



Richard Farrant



Margaret Ford



Dr Eileen Marshall



Callum McCarthy

### The Gas and Electricity Markets Authority

The Gas and Electricity Markets Authority has the ultimate responsibility for all that Ofgem does. It determines strategy and decides on major policy issues. Its members are:

<b>John Belcher</b>	Non-executive
<b>Lord Currie*</b>	Non-executive
<b>Richard Farrant</b>	Non-executive
<b>Margaret Ford</b>	Non-executive
<b>Dr Eileen Marshall</b>	Managing Director, Competition and Trading Arrangements
<b>Callum McCarthy</b>	Chairman
<b>John Neilson</b>	Managing Director, Customers and Supply
<b>Richard Ramsay</b>	Managing Director, Regulation and Financial Affairs
<b>James Strachan</b>	Non-executive
<b>Sir Keith Stuart</b>	Non-executive
<b>Gill Whittington</b>	Chief Operating Officer





**John Neilson**



**Richard Ramsay**



**James Strachan**



**Sir Keith Stuart**



**Gill Whittington**

### The Ofgem Management Committee

The Ofgem Management Committee manages all policy, resource and operational issues day-to-day. Its members are:

<b>Dr Eileen Marshall</b>	Managing Director, Competition and Trading Arrangements
<b>Callum McCarthy</b>	Chief Executive
<b>John Neilson</b>	Managing Director, Customers and Supply
<b>Richard Ramsay</b>	Managing Director, Regulation and Financial Affairs
<b>Gill Whittington</b>	Chief Operating Officer

### 3. Social and environmental action

#### Key achievements for 2001-2002 – Social Action

- Progress made in all areas identified in Social Action Plan (SAP)
- Industry introduced range of new services and tariffs to help vulnerable customers
- Range of initiatives introduced to help prepayment meter customers
- All research projects into the causes of fuel poverty completed

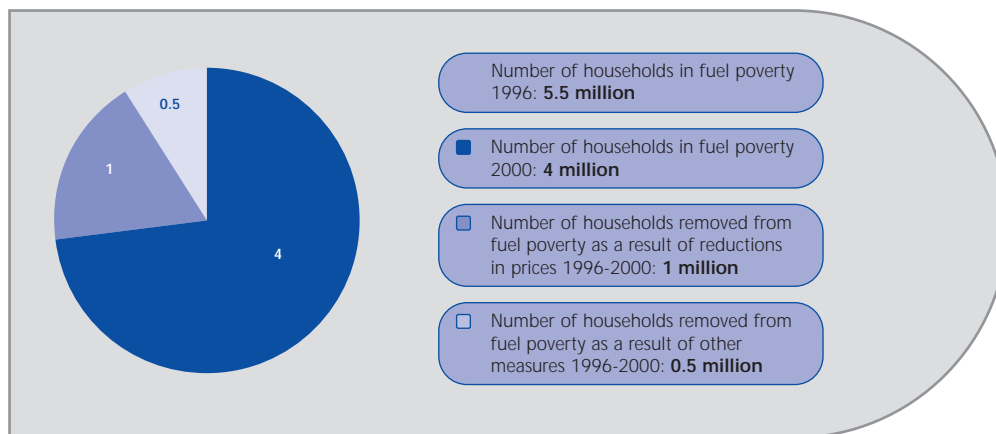
#### Key achievements for 2001-2002 – Environmental Action

- Procedures put in place to administer Government Renewables Obligations and Energy Efficiency Commitment
- Significant progress made to remove regulatory barriers to the development of distributed generation
- 200 schemes introduced under Energy Efficiency Standards of Performance (EESoP) between 2000 and 2002, all aimed at meeting energy savings targets
- Guidelines introduced to give domestic customers confidence when buying energy marketed as 'green'

## Introduction

Reconciling Britain's social, environmental and competitiveness goals is a major challenge for Government. For its part, Ofgem has important social and environmental duties in relation to energy policy, subject to its principal objective to protect the interests of consumers, present and future, wherever appropriate by promoting effective competition.

**Figure 1** Reduction in households in fuel poverty since 1996 (millions)



Lower energy prices resulting from competition and effective regulation have lifted one million households out of fuel poverty since 1996 – by far the single biggest contribution to tackling this scourge. This year, Ofgem made a significant contribution to the Government's Fuel Poverty Strategy, which aims to remove all vulnerable households from fuel poverty by 2010.

Ofgem worked to ensure that energy prices remain as competitive as possible and implemented its second year of programmes targeted at helping vulnerable customers suffering from fuel poverty through its Social Action Plan (SAP).

Ofgem contributes to meeting important environmental challenges by doing all it can within its duties, and by engaging with others who have environmental responsibilities. It works to promote measures across the gas and electricity supply chains that have the best chance of success in meeting environmental targets, at the least cost to gas and electricity customers.

Ofgem does this by:

- identifying and advancing the changes needed to the transmission and distribution systems, if the Government's objectives of a substantial increase in renewables and Combined Heat and Power (CHP) generation are to be met. This has involved work on distributed generation and transmission access
- regulating networks to ensure efficient use of resources and sufficient investment to meet future demand
- tackling those issues affecting the environment that are within its sphere of influence, seriously and effectively, and
- administering large Government schemes to promote renewables and energy efficiency.

Considerable resources were devoted to administering the Climate Change Levy exemption for renewable generators, which took effect on 1 April 2001, and to setting up procedures for administering the Renewables Obligation and Energy Efficiency Commitment (EEC), which took effect in April 2002. Ofgem is administering all three schemes for the Government to help it meet its Climate Change Programme target of reducing greenhouse gases by 12 per cent by 2010.

In the year, Ofgem produced its first Environmental Action Plan (EAP). This plan sets out Ofgem's work programme in relation to the environment, across the gas and electricity supply chains.

In February, Ofgem welcomed the Performance and Innovation Unit's (PIU) energy review, which flagged up the need for wider debate on Britain's environmental objectives and how to achieve them. There is a need to improve understanding of the implications of environmental targets and how best to meet these. Ofgem is committed to working constructively with Government and others to achieve this.

## SOCIAL ACTION

Some 3.5 million households in the United Kingdom are in fuel poverty, ie having to spend more than 10 per cent of household income to keep satisfactorily warm. The Government has set a target to end the blight of fuel poverty for vulnerable households by 2010 and a Fuel Poverty Strategy is in place to meet this target.

Low incomes, poor housing conditions and energy costs cause fuel poverty. Ofgem has a clear role to play in respect of energy costs and has a further role to play, particularly through its work on energy efficiency, in helping to improve housing conditions. Its work to promote lower prices – through continuing regulation of the monopoly pipes and wires businesses, and through the spread of competition elsewhere – clearly benefits Britain's economic growth and, hence, incomes.

### *Social Action Plan (SAP)*

In March 2000, Ofgem published its SAP, identifying four keys areas of action to help the fuel poor. They were:

- enhanced licence obligations
- improvements in monitoring and reporting
- a programme of research, and
- a number of broader structural changes.

In March 2001, Ofgem published its first SAP annual review, followed by the second in March 2002. They showed that progress had been made in all four areas.

### *Industry initiatives*

Ofgem has encouraged the industry to respond to the challenge of fuel poverty and this has led to an increase in the number and range of services and tariffs for the fuel poor developed by the energy companies. Ofgem will work to encourage more new services and tariffs through its SAP and the EEC.

### *Monitoring suppliers' social obligations*

Domestic suppliers have to publish codes of practice on key areas of their service. The codes of practice cover payment of bills, dealing with customers in difficulty, provision of energy efficiency advice, services for PPM customers and special help for older people and customers who are disabled or chronically sick. Examples of work carried out under social obligations include free meter safety checks, work to reduce the level of disconnections and promoting the Priority Services Register.

Ofgem approves the codes and monitors performance against them to ensure they are operated effectively. During the year, Ofgem started to publish quarterly reports on its website on how well companies are performing with regard to social obligations.

Also during the year, Ofgem introduced measures to monitor electricity distribution companies' compliance with their social obligations, which include providing special help to vulnerable customers during power cuts and maintaining a register of people with special needs.

### *Helping prepayment meter customers*

#### *Customers in debt*

Ofgem began work in 1999 to reduce the problem of debt blocking, which affects about one million gas and electricity customers who are repaying a debt via a PPM. The only way Ofgem can address this issue is through a collective licence amendment. This requires both the Government to implement the relevant provision under the Utilities Act and the necessary consent of licensees. In a move towards achieving this, Ofgem worked with licensees on a three-month trial which was started in December 2001.

This trial was seen as a step in the right direction to allow PPM customers in debt to switch their supplier and gain the full benefits of the competitive market. The results of this trial will be taken forward during the forthcoming year with a view to industry agreeing a licence modification. Ofgem will also produce, with energywatch, best practice guidelines for companies on debt management and prevention.

### *Other initiatives*

Although the majority of fuel poor households do not use a PPM, a significant number of low income customers do. As PPMs remain the most expensive way to buy energy, Ofgem has been working on a number of initiatives in the year to help these customers. They include:

- **more choice** – competition is delivering savings of up to eight per cent for electricity and seven per cent for gas PPM customers. PPM customers are also switching at similar rates to customers using standard credit tariffs.
- **metering** – Ofgem is encouraging the industry to come forward with more cost-effective meters to replace the current PPMs.
- **industry schemes** – Ofgem has been working with industry to get a better deal for PPM customers. This has seen some companies reduce prices for PPM customers. Industry has also adopted a code of practice aimed at ensuring PPM customers receive better advice and information.
- **tackling self-disconnection** – research commissioned for Ofgem suggests that there is a small minority of PPM customers for whom self-disconnection is a problem. Acting on these findings, Ofgem has proposed that suppliers should target those PPM customers most likely to self-disconnect by providing them with information on subjects such as how their meter works and how to obtain emergency credit. It is as a result of Ofgem's work that some companies now set their meters so that customers retain their energy supply overnight, even if the meter runs out of credit.
- **Fuel Direct** – guidelines for helping companies ensure that all customers using the Government's Fuel Direct scheme are treated consistently were issued by Ofgem. Fuel Direct allows people to have fuel bills deducted directly from their benefit payments. The impact of these is being monitored.

### *Research into the causes of fuel poverty*

A key aspect of the SAP has been the promotion of a series of research projects designed to establish the direct experience and needs of customers to help inform future policy making. Seven research projects were identified in the Plan. Three were completed in 2000-2001 and the last four were completed during 2001-2002. The projects and their objectives were as follows:

- **energy efficiency advice** – to establish how low-income customers prefer to access energy efficiency advice, the extent to which advice that is given is appropriate, and how it is acted upon
- **self-disconnection and rationing** – to identify and analyse the pattern of electricity and gas consumption in households vulnerable to fuel poverty, in particular the extent of self-disconnection amongst PPM users and patterns of rationing amongst credit customers
- **switching from PPM to other payment methods** – to examine why customers have PPMs and how they can be encouraged to change to cheaper payment methods
- **debt prevention and management** – to increase understanding about customers who are in debt and to explore ways of managing debt problems more effectively
- **identification of, and help for, vulnerable customers** – to examine the scope for working in partnership with local authorities, agencies and local and national charities to identify efficient and cost effective opportunities to help vulnerable customers
- **different forms of debt recovery using PPMs** – to examine the effectiveness of spreading the cost of payments through a PPM to avoid large winter bills, and
- **financial services to disadvantaged customers** – to identify the feasibility of developing community investment partnerships based upon credit unions, as a means of overcoming fuel poverty and financial exclusion at a local level.

The reports of all these projects have been published and are available on request. The results of the research are informing Ofgem's future work programme.



## ENVIRONMENTAL ACTION

The Utilities Act 2000 gave Ofgem a significant role in helping the UK meet its target to reduce greenhouse gases set out in the Government's Climate Change Programme. This programme outlines how the UK plans to reduce greenhouse gases by 12 per cent, and CO<sub>2</sub> emissions by 20 per cent, by 2010 so as to ensure that the UK meets and, for CO<sub>2</sub> gases, exceeds its commitment under the Kyoto protocol on Climate Change.

In August 2001, Ofgem published its Environmental Action Plan (EAP) setting out how it will meet its statutory duties and have regard to the environmental impact of its work across the gas and electricity industry. It defined the work Ofgem would carry out to promote a cleaner environment and the work that is more appropriately carried out by other agencies.

The Government has repeatedly made clear that it believes legislation, not regulation, should determine environmental and social policies that have significant economic costs. Accordingly, Ofgem will look to Ministers and other government bodies with direct environmental responsibilities to take the lead on policies where action would have significant financial implications. When called on to do so, and where it is compatible with its statutory duties, Ofgem plays an important role in executing these policies. In all cases, it promotes policies designed to deliver environmental benefits at the least cost to consumers.

Work on the EAP covers the whole of the energy supply chain with action being taken in:

- generation
- transmission and distribution, and
- supply.

### *Generation*

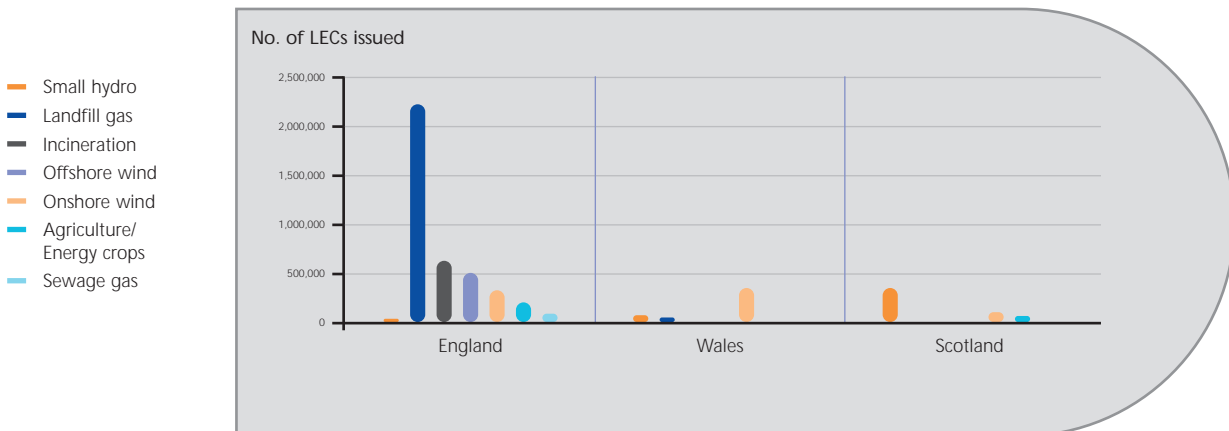
Ofgem has worked to ensure that smaller generators can participate effectively in the New Electricity Trading Arrangements (NETA) (see Chapter 4). Ofgem has also contributed to the work the Environment Agency has carried out in setting up an emissions trading scheme for Nitrous Oxide (NO<sub>x</sub>) emissions. In general, Ofgem sees market-based solutions as the best way to achieve environmental targets at the least cost to consumers.

### *Climate Change Levy (CCL) exemption for renewable generators*

Ofgem has administered the exemption scheme since the CCL came into force in April 2001. Renewable generators apply to Ofgem for accreditation to have their output exempted from the CCL. Ofgem checks whether they meet the criteria. To date, over 600 generators have been accredited. Thereafter, Levy Exemption Certificates (LECs) are issued based on metered output, with each Certificate representing 1 MWh of electricity. Between April 2001 and March 2002, five million LECs were issued (see below).

In October 2001, Ofgem's computer system for issuing LECs and Renewables Obligation Certificates (ROCs) became fully operational. In January 2002, Ofgem issued a set of guidance notes on the CCL exemption, which covered topics such as information for generators and suppliers, LEC over- or under-issue and provision of meter readings.

**Figure 2** LECs issued by country and technology 2001-2002



### *Renewables Obligation*

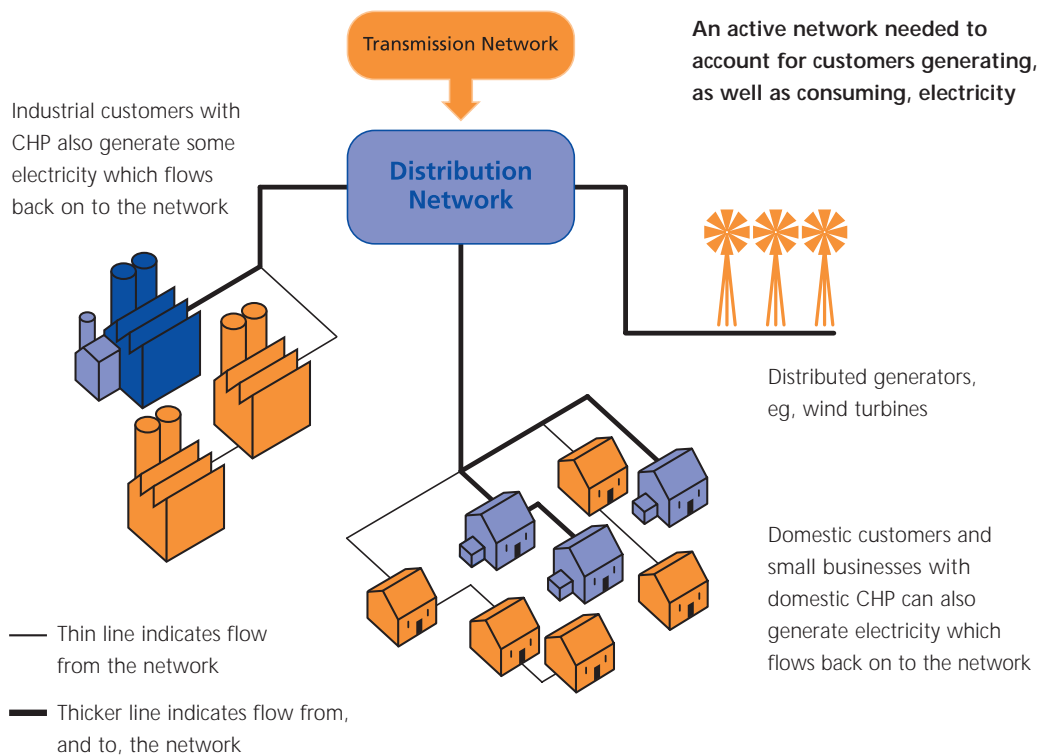
During the year, Ofgem began to put in place the procedures for administering the Government's Renewables Obligation (RO), which came into force in April 2002. The Obligation sets a target for how much electricity suppliers should get from renewable generators. This starts at three per cent for 2002-2004 and reaches 10.4 per cent in 2010-2011. Extensive consultation on these procedures was carried out and Ofgem also contributed to the Department of Trade and Industry's (DTI) work on the introduction of the Obligation.

## Transmission and distribution

### Distributed generation

One of the main ways that Ofgem can contribute to the development of renewables is by facilitating a fair and transparent regulatory regime for the development of distributed generation. This is electricity generation connected to the distribution network rather than to the high voltage national grid. It is typically small scale, such as Domestic Combined Heat and Power (DCHP), solar schemes and small wind projects.

**Figure 3** Distribution network – with distributed generation



Distributed generation can also help the Government meet its long-term environmental targets and reduce the losses caused by transmitting electricity over long distances.

A joint DTI/Ofgem Distributed Generation Co-ordinating Group (DGCG) was set up during the year to address the problems of renewable generators linking on to local distribution networks. This group was established following recommendations made in 2001 by the former Embedded Generation Working Group (EGWG), originally set up to look at these issues.

Following extensive consultation in March 2002, Ofgem put forward the following proposals on distributed generation:

- allowing generators the option of spreading the cost of connecting to the distribution network
- making it easier for DCHP customers, who have a heating system that can generate its own electricity, to connect to the networks by establishing a standard set of procedures, and
- providing full and easy-to-understand information for prospective distributed generators.

Ofgem will also ensure that the next distribution price control, which comes into effect in April 2005, will consider the need for changes to incentives on distribution companies.

#### *Transmission and distribution losses*

On average, about nine per cent of electricity is lost as heat as it is transported on the transmission and distribution networks – although losses are much higher in some areas than others. This is wasteful in environmental terms.

Ofgem has suggested that reform is necessary to the current transmission losses arrangements. Whatever reforms are eventually agreed, they must enable accurate signals to be given about the costs of entry to the system at different locations and bring environmental benefits through reduced transmission losses.

Ofgem has also committed resources to a review of the incentive framework in respect of losses of electricity on the distribution systems in Great Britain. This will look at interim changes that can be made as well as identify changes in the regulatory framework for the next distribution price control to take effect from 2005 (see also Chapter 6).

## Supply

### *Energy Efficiency Standards of Performance (EESoP)*

The EESoP programme was originally set up in 1994 and obliged each of the 14 former Public Electricity Suppliers (PESs) to achieve specified energy savings among their customers. This year saw the final year of the EESoPs 3 programme, which had been extended in 2000 to include second tier electricity suppliers and gas suppliers.

In all, there were about 200 EESoPs 3 schemes. Many of these demonstrated an innovative approach to achieving the required savings targets. During the forthcoming year, suppliers will be compiling completion reports for each scheme, and Ofgem – along with the Energy Savings Trust (EST) – will be assessing this information to check suppliers' compliance with their targets.

Examples of schemes that are innovative in the way they achieve the required savings targets include:

- **Powergen Lighting Energy Service Company (ESCo)** – this scheme provided a package of four energy efficient light bulbs to about 75,000 customers
- **London Electricity** – jointly funded with Tower Hamlets Council, this scheme involved replacing an existing heating system within a housing estate with a CHP-based community heating system to increase efficiency and improve warmth for residents, and
- **energy efficient appliance exchange scheme** – this is a nationwide scheme jointly funded by Eastern Energy, London Electricity, Norweb, Seeboard and SWEB and operated in partnership with the EST, energy efficiency advice centres, manufacturers and national retailers. The scheme encouraged customers to trade in existing inefficient fridges, freezers and fridge-freezers for energy saving models at a subsidised cost.

### *Energy Efficiency Commitment (EEC)*

During the year, Ofgem consulted on and finalised its procedures for administering the new EEC which replaced the EESoP programme in April 2002. Unlike the EESoP programme, the EEC is set by Ministers and will be administered by Ofgem. Supply companies will put forward schemes aimed at meeting their energy saving targets. Once approved by Ofgem, these schemes will be monitored to check compliance. Ofgem has also produced a technical guidance manual for suppliers, providing information on delivering energy efficiency measures.

At least 50 per cent of savings achieved under the EEC must be targeted at 'priority customers', ie those people who receive income-related benefits. The scheme is expected to deliver around £500 million in energy efficiency measures, at a cost of around £3.60 per customer per year for each fuel.

### *Encouraging green energy supply*

Ofgem is keen to ensure that customers can also play a part in helping encourage greener energy supplies, by having the choice to buy electricity produced from renewable sources. This year it issued guidelines which came into effect in April 2002 that aim to give domestic customers confidence when buying energy marketed as green by suppliers, following the introduction of the RO.

These guidelines will help suppliers design green energy offerings. Trading Standards services, the Advertising Standards Authority and other media bodies will enforce advertising guidelines and may take account of Ofgem recommendations. This will help the development of the market for green energy, which has already seen an estimated 60,000 customers opt for one of the currently available green supplies offered by electricity suppliers.

### **MAKING OFGEM 'GREENER'**

In the year, Ofgem worked towards achieving ISO 14001 certification for its internal environmental policies. This baseline was awarded in February 2002 and Ofgem is now working to show improvements. Ofgem has also contracted with a supplier to provide 10 per cent of its electricity from green sources.

## 4. Competition in wholesale markets

### Key achievements for 2001-2002 – Electricity

- New Electricity Trading Arrangements (NETA) completed first year of successful operation, with greater competition and falling wholesale prices
- Work progressed with smaller generators and demand-side participants to improve the way they operate under NETA
- Progress made towards creating British-wide wholesale electricity trading & transmission arrangements
- Reforms to electricity transmission network arrangements proposed to enhance long-term security of supply and reduce losses on system
- New incentive arrangements introduced for National Grid Company (NGC) to operate system more efficiently and economically

## Key achievements for 2001-2002 – Gas

- Strong financial incentives on Transco to invest in the transmission system in a more timely and effective manner introduced
- Plans for long-term capacity auctions developed
- Reforms to gas balancing regime taken forward to help ensure future secure and effective network operation
- Investigation into conduct of companies in gas capacity market found no evidence of abuse
- Need for improvements to capacity regime identified and addressed in system operator incentive plans

## Introduction

Wholesale electricity and gas costs make up a major part of customers' bills. Generation costs account for 42 per cent of the average domestic electricity bill, and gas production costs account for 45 per cent of the average domestic gas bill.

**Figure 4** Breakdown of domestic electricity bill

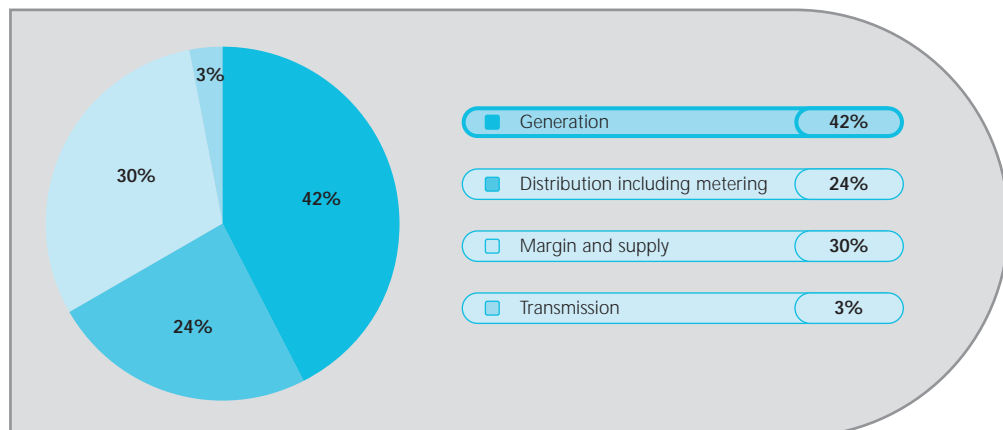
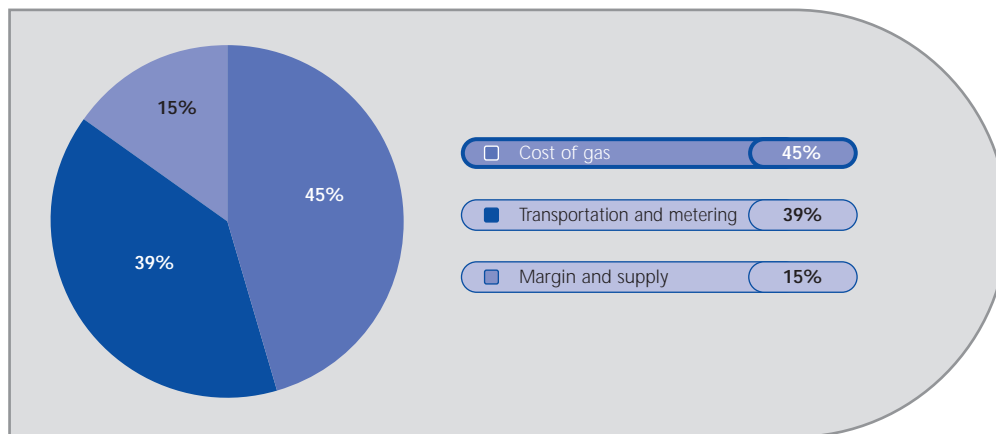




Figure 5 Breakdown of domestic gas bill



That is why work to improve the efficiency and competitiveness of the wholesale gas and electricity markets continued to be an important priority for Ofgem in 2001-2002. Another priority was to reorganise resources to place a greater emphasis on Ofgem's monitoring and compliance work to ensure that the new gas and electricity trading arrangements remain competitive and free from abuse.

### *Electricity*

NETA marked its first birthday on 27 March 2002. NETA operated successfully throughout the year and achieved its main aim of creating more competitive trading arrangements and putting pressure on wholesale prices.

The more flexible governance arrangements incorporated in the Balancing and Settlement Code (BSC), which replaced the inflexible arrangements under the Electricity Pool, also worked well, allowing the BSC rules to evolve effectively and in a timely way.

During the year, Ofgem carried out a two-month review of the initial impact of NETA on smaller generators and pursued measures to improve the way in which they operate under NETA. It also published a further review which looked at NETA's general performance in the three months after Go-Live.

Reforming the arrangements for access to the high voltage transmission network and charging for transmission losses was taken forward to help ensure that the full benefits of NETA are realised. The key objective of the reforms proposed during the year is to enhance long-term security of supply for all customers and reduce losses on the system.

At the same time, Ofgem implemented enhanced system operator incentives that further encourage NGC to operate the electricity transmission system efficiently and economically.

Progress was made during the year towards creating a single British market in electricity trading and transmission. Proposals were put forward to introduce British Electricity Trading and Transmission Arrangements (BETTA) which will create, for the first time, fully competitive British-wide market arrangements. The go-ahead for Government legislation to implement these reforms was given in April 2002 by the Secretary of State for Trade and Industry.

### *Gas*

All activity carried out during 2001-2002 was set against a backdrop of continuing high wholesale gas prices, which have doubled in the last two years. This rise has been caused primarily by high continental gas prices.

This situation cannot be directly addressed by Ofgem because it has no regulatory powers in continental Europe. However, Ofgem has continued to work with the Department of Trade and Industry (DTI) and other agencies to seek to promote policies that will lead to greater competition in continental Europe and, in turn, more competitive prices for domestic and business customers in Great Britain.

Ofgem introduced the final part of the Transco price control review process by announcing proposals for incentives on Transco in its role as system operator. These covered reforms to the longer term transmission exit and entry capacity regimes. Ofgem also continued to monitor the performance of short-term capacity auctions and introduced a number of improvements to the short-term capacity regime.

During the year, Ofgem built on the reforms to gas trading arrangements begun in 1999. Further proposals were put forward to improve the gas balancing regime. Several reforms and improvements to the regime were implemented by way of Network Code modifications in 2001-2002, with other reforms and code modifications being proposed.

## ELECTRICITY

### *New Electricity Trading Arrangements in England and Wales*

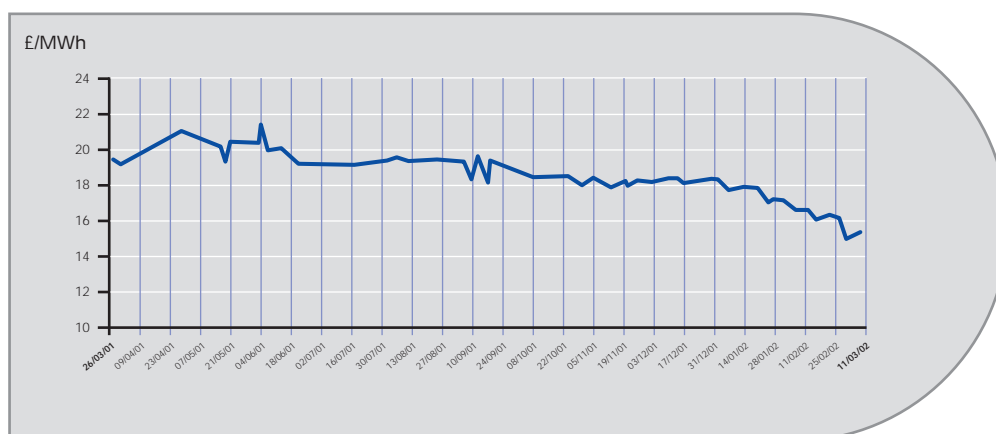
#### *NETA – one year on*

NETA created, for the first time, a market for trading electricity much like that for any other commodity. In its first year of operation, it has delivered more competition and placed considerable pressure on wholesale prices, which had been kept artificially high by the arrangements under the Electricity Pool which NETA replaced.

Greater competition and a generous generator capacity margin saw prices fall by some 18 per cent since Go-Live and by 40 per cent since reforms were proposed in 1998.

In the past 12 months, liquidity in forward markets has increased by 150 per cent. New NETA governance arrangements have worked well to allow for adjustments to be made quickly and as issues arose. The NETA systems also proved robust when faced with the collapse of Enron, the world's largest energy trader, only nine months after Go-Live.

**Figure 6** NETA Forward prices



The impact of NETA on customers' prices also began to be seen. Industrial and commercial contracts are most responsive to wholesale changes so have seen the fastest falls in prices. Domestic prices also started to fall but this picture is more complex:

- suppliers often have long-term wholesale contracts, which means changes in prices take time to feed through to customers
- domestic customers often pay for a joint 'dual fuel' package. Here, falls in wholesale electricity prices may be being offset by rises in wholesale gas prices, and
- new costs relating to Government environmental measures, such as the Energy Efficiency Commitment (EEC) and the Renewables Obligation (RO), have begun to feed through to customers' bills.

Work will continue in the forthcoming year to help ensure that price benefits continue to feed through to domestic customers and that the arrangements continue to operate effectively.

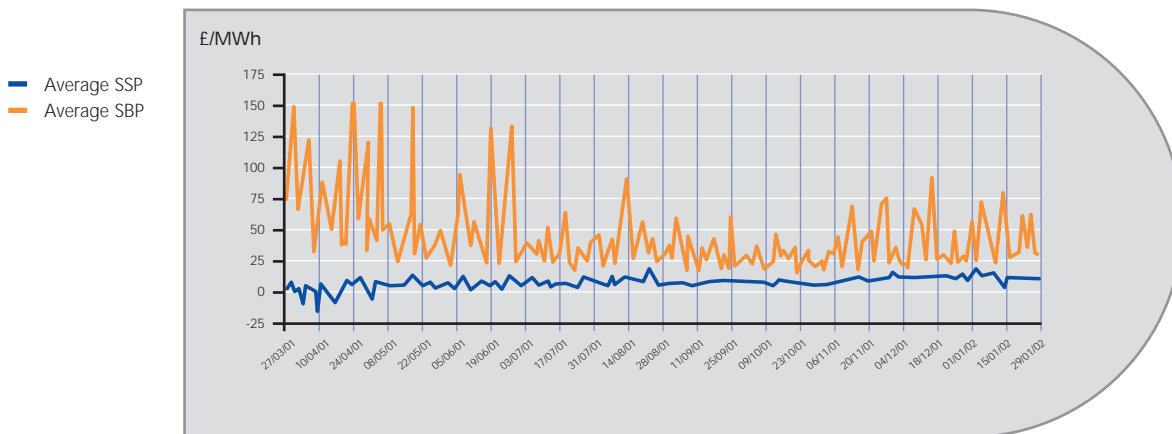
### *Balancing the system*

Under NETA, almost all electricity is bought and sold like any other commodity, by contracting between willing buyers and sellers in over-the-counter markets or in power exchanges. A small amount of sales, about two per cent, are made in the Balancing Mechanism, the tool that NGC has as system operator to ensure that supply and demand match on a second-by-second basis.

This market developed rapidly as generators, suppliers, traders and customers gained greater experience of operating in the new market, and as Ofgem-approved modifications to balancing and settlement rules took effect.

These factors led to a significant reduction in price volatility. For instance, the difference between the prices at which participants have to buy and sell electricity from NGC to balance their positions reduced from £70 per MWh at Go-Live, to £17 per MWh today. Overall, participants have managed their business so as not to be exposed to System Buy Price (SBP).

Figure 7 Imbalance prices



Costs of balancing the system on a daily basis also halved since Go-Live. This was the result of NGC responding to its incentives as system operator and greater competition in the provision of balancing services.

### *NETA governance*

The governance arrangements managed under the Balancing and Settlement Code (BSC) by ELEXON have also worked well. At the end of March 2002, participants had put forward 71 modification proposals to the BSC. Of those, 26 decisions were made and 13 approved by Ofgem, while 36 were still being processed.

These modifications – and others in the pipeline – will continue to improve the arrangements. One of the most significant modifications is the change to reduce gate closure from the present 3.5 hours to 1 hour. This change, which came into effect in July 2002, will help the demand-side as well as generators. It will particularly help intermittent generators, eg wind power generators, by limiting their risk of exposure to charges for being out of balance.

Ofgem continues to use its powers to approve modifications to the NETA rules and will regularly review the progress and impact of NETA on all generators – large and small – making changes where they are needed.

### *Demand-side participation*

During the year, some demand-side participants, typically large industrial customers who find it more profitable to sell their electricity than use it, began to actively participate in the balancing services.

A working group was set up by Ofgem in November 2001 to look at reviewing the range of options available to demand-side participants, identifying any obstacles to their participation in NETA and recommending measures to remove them.

### *Review of NETA and its impact on smaller generators*

Ofgem produced a report for the DTI on the experiences of smaller generators, including renewable and Combined Heat and Power (CHP) plants, operating under NETA, two months after Go-Live.

In the run up to the implementation of NETA on 27 March 2001, smaller generators and their representative organisations said that they would be particularly, and more adversely, affected than other generators by the new arrangements. However, the position of smaller generators needed to be looked at in the context of how NETA had performed as a whole since some, but not all, of the features affecting smaller generators are common to all generators. Against this background, the results of the analysis of smaller generators showed:

- export prices achieved by smaller generators who responded to Ofgem's survey were 17 per cent below those achieved under the Pool in the previous year. These reductions were somewhat smaller than for generation prices overall
- output fell substantially. Lower prices were one factor, but there was evidence that higher fuel costs, which had risen 14 per cent in the previous year, also contributed
- this particularly affected CHP generators whose main input is gas, the price of which has doubled in the last two years, and
- other than wind power, the output of smaller generators did not appear to be significantly less predictable than for other generators.

### *Consolidation*

The smaller generators' report, which was published in August 2001, identified that one of the main obstacles preventing them from participating in NETA was the difficulty they faced in using consolidation services that allow smaller generators to aggregate their output to sell it more competitively.

To tackle this issue, the Consolidation Working Group was set up. This group was chaired by Ofgem and included smaller generators, consolidators, suppliers, DTI, Department for Environment, Food and Rural Affairs (DEFRA), ELEXON and NGC. This group published a final report in February 2002 which set out ways to enable smaller generators to sell their electricity more flexibly and competitively under NETA, as well as measures to encourage the growth of consolidation services.

Much of the work needed to modify the BSC to help the development of consolidation services has now been carried out.

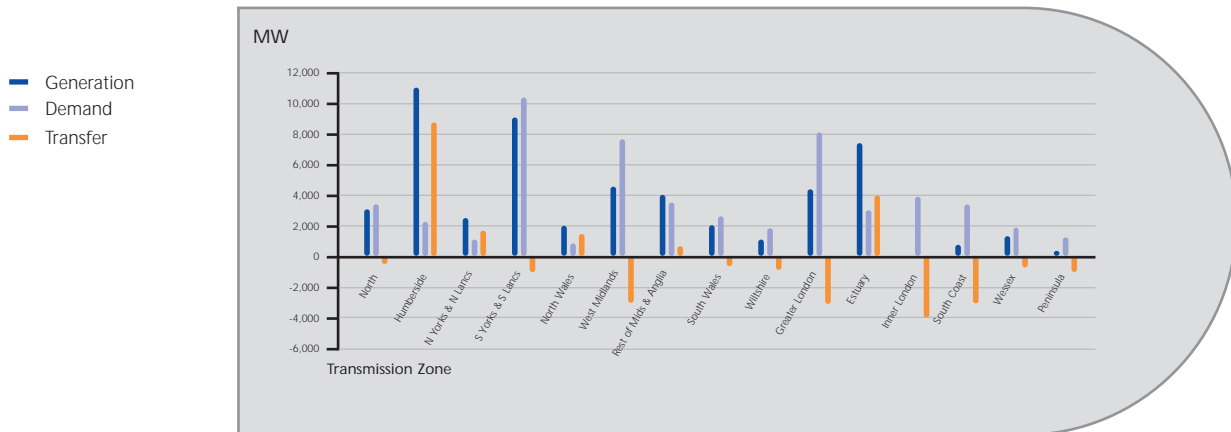
### *CUSC*

In November 2001, Ofgem and the DTI introduced the new Connection and Use of System Code (CUSC) to provide a contractual framework for connection to, and use of, the NGC's high voltage transmission system in England and Wales. The CUSC introduced more flexible governance arrangements to complement the introduction of NETA. It also clarified the role of Ofgem in settling disputes over access to the transmission system.

### *Transmission access and losses*

Ofgem put forward proposals during the year to reform the electricity transmission network arrangements in England and Wales. These reforms are aimed at giving generators and suppliers a right to firm, long-term access to the network to transport electricity and a fairer allocation of the costs of electricity losses between customers.

**Figure 8** This shows the demand, generation and transfer in each transmission zone between 2001 and 2002.



Highlights of the reforms included the following:

- for the first time, generators and shippers will have firm rights, in the form of long-term contracts with NGC, to the transmission network
- these rights will provide NGC with better signals about when and where to invest in the network – it will also have financial incentives to respond efficiently to these signals
- they also mean that generators and suppliers will be compensated for any failures to the network which mean they cannot deliver on their contracts
- the cost of electricity lost as heat as it travels along the wires, currently spread across all generators and suppliers, will be targeted at those whose locations and grid usage cause the losses, and
- this will encourage the development of smaller distributed generation – ‘off-Grid’ generation such as CHP plants, solar energy and small wind farms – which is not connected to NGC’s transmission system.

The proposals for new access arrangements are now being examined by a panel of industry experts who will be reporting later in the year. Modifications seeking to change the current losses arrangements have been made under the BSC and will be with Ofgem for consideration later in 2002.



### *NGC system operator incentives*

Final proposals were put forward in February 2002 for enhancing existing system operator incentives that will encourage NGC to operate the electricity transmission system more efficiently and economically.

The previous scheme, which came into operation when NETA was introduced and which expired in March 2002, was rolled over for one year from 1 April 2002 to 31 March 2003, with some specific adjustments.

Under Ofgem's final proposals, NGC was set a single cost target of £460 million for one year. Under the new scheme, NGC stands to gain greater financial rewards if it reduces its costs below that target but faces penalties if the costs exceed the target.

In the coming year, Ofgem will seek to introduce 'deep', investment-related System Operator (SO) incentives for NGC which will come into effect from April 2003 and are similar to those proposed for Transco from April 2002.

### *BETTA*

During the year, Ofgem worked to develop policy for BETTA. In April 2002, the Secretary of State for Trade and Industry announced that, subject to Parliamentary time being made available, primary legislation will be introduced to implement the BETTA reforms.

As well as preparing for this legislation, Ofgem worked in the year to develop the reforms required to bring BETTA into effect.

BETTA will be achieved by:

- extending NETA across Great Britain to encompass the Scottish market
- appointing a single system operator to run the high-voltage electricity transmission system. This is currently run in England and Wales by NGC and, in Scotland, by ScottishPower and Scottish and Southern Electricity, and
- reforming the way that generators and suppliers plug into the transmission system to ensure that they have fair and open access to the network, creating, for the first time, a British-wide transmission network.

These reforms will bring more competitive prices for Scottish customers and will create a wider market for both traditional and renewable generators in Scotland, which currently has a 70 per cent surplus generating capacity.

## GAS

### *Transco*

An important complement to the Transco price control review process (see Chapter 6) was new 'deep', investment-related system operator incentives for Transco in relation to the National Transmission System (NTS).

These proposals established stronger financial incentives for investment in the NTS, consistent with proposed new auction arrangements for selling long-term, firm entry capacity rights to shippers and producers. Prices that emerge from these auctions, and subsequent trading, should improve the information available to Transco and help it identify the need for extra investment.

The new Transco system operator incentive regime, final proposals for which were published in December 2001, also included revised exit and interruptibles arrangements and revised incentives covering Transco's day-to-day operation of its transmission system.

Ofgem's proposals mean that:

- **customers** benefit from
  - enhanced security of supply
  - lower system operator costs, which are passed through to customers and, potentially,
  - improved competition
- **Transco** benefits from
  - better signals to guide investment to meet its changing customer requirements
  - having to face less risks when making investment decisions
  - being able to earn significant extra revenues if it invests more in response to customer demand
  - earning extra revenue if it beats system operator cost targets, and
- **industry** benefits from
  - a gas transmission system which meets its changing needs
  - enhanced security of supply and lower system operator costs, and
  - the prospect of buying capacity on a long-term basis to meet its needs.

The new investment incentives arrangements represent an important development of the RPI-X form of price control. They provide baseline outputs and ensure better signals and rewards for more efficient investment.

### *Capacity auctions*

During 2001-2002, Transco continued holding short-term, six monthly auctions of entry capacity rights.

As part of the Transco system operator incentives proposals, Transco will have to offer for sale agreed levels of firm, tradeable entry capacity rights in a series of long, as well as shorter-term, auctions. Two alternative industry proposals to introduce longer-term capacity auctions have been consulted on. Subject to the outcome of those consultations, it is proposed that the first auctions for long-term capacity rights will be conducted later in the year.

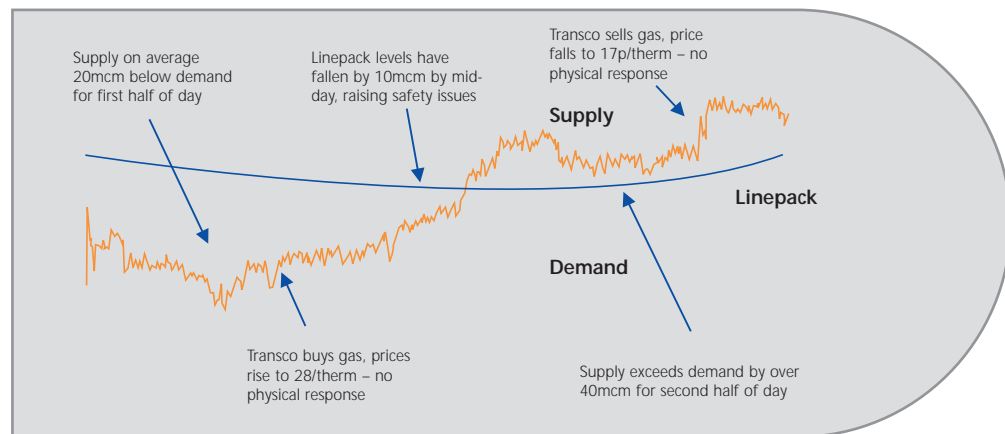
### *Gas balancing*

A significant concern for Ofgem during 2000-2001 was the way the gas balancing regime on Transco's NTS had been operating. Transco had expressed concern about the operation of the regime and suggested reform was necessary to help ensure the future secure and efficient operation of the gas pipeline network.

The problem was caused by 'within-day profiling'. This happens when shippers put on insufficient gas at the start of the day, resulting in Transco having to buy gas to keep the system in balance, raising prices. Towards the end of the day, more gas than is needed is then flowed on to the system resulting in Transco having to sell gas to keep the system in balance, at a reduced price. This means Transco makes a loss on the day.

At the same time, Ofgem was made aware of industry concerns about initial proposals to reform the regime that had been put forward in February 2001. To allow it sufficient time to consider those concerns while ensuring security of supply during the winter of 2001-2002, Ofgem sought and received assurances from Transco and NGC that security of supply could be maintained within existing arrangements.

**Figure 9** Example of within-day profiling



Transco continued to report problems with balancing the system efficiently which, in some circumstances, could have threatened within-day security of supply. Therefore, in February 2002, Ofgem published its revised proposals to reform the gas balancing regime.

Ofgem's proposals were designed to:

- provide improved commercial incentives for shippers to balance the gas they put on, and take off, the system throughout the day
- expose shippers to the full costs of any behaviour that forces Transco to take action to balance the system, and
- give Transco reliable, accurate information about what gas is being put on, and taken off, the system, allowing it to balance the system more efficiently.

Ofgem considered that to meet these objectives, the reforms should include:

- shorter balancing periods (less than 24 hours)
- sale of system linepack (storage of gas in the pipeline), and
- incentives for shippers to improve the information flows to Transco on which it bases its daily balancing actions.

These reforms are currently being considered by the Network Code modification review group that has been established to look at the problems with present balancing arrangements and to develop Code modifications to cover them. The group is expected to make recommendations on the way forward for the gas balancing regime later in the year.

### *Monitoring, investigations and compliance*

Ofgem devotes considerable resource to compliance and enforcement. For example, it monitors daily prices and trends in the competitive wholesale markets as well as carrying out specific investigations.

Following an investigation into the conduct of companies operating in the gas capacity market, Ofgem highlighted in November 2001 the need for improvements in the capacity regime.

The investigation was launched in October 2000 after system constraints forced Transco to buy back significant amounts of entry capacity from companies, often at very high prices. It also addressed concerns about companies being involved in anti-competitive behaviour that could harm customers. As a result of the investigation, Ofgem concluded that all of the companies investigated were able to provide satisfactory explanations for their conduct.

Ofgem identified where improvements to the capacity regime were needed that should, in the future, help to minimise the costs of future buy-backs and enable Transco to manage system constraints more effectively. Many of these improvements were addressed in reforms of Transco's role as system operator, published in December 2001.

Also during the year, Ofgem carried out an investigation into shippers' behaviour under the gas balancing regime. While no anti-competitive behaviour was proven, the investigation reinforced the case for reform to the balancing arrangements that had been progressed in the year.

### *Europe*

During the year, Ofgem played a major role within the Council of European Energy Regulators (CEER) and continued to take a full part in the processes the European Commission has established to create a single European energy market.

Ofgem's work in this area will remain a priority for the coming year and it will continue to argue strongly for the implementation of plans to liberalise the European energy market to enable efficient trade.

## 5. Competition in gas and electricity supply

### Key achievements for 2001-2002

- Competition firmly established in gas and electricity retail markets and now most effective 'regulator' of prices
- Remaining price controls on domestic gas and electricity suppliers lifted
- Customer transfer process improved to make it easier for customers to switch
- Marketing licence conditions extended for further two years to protect customers from unscrupulous sales practices
- Measures taken to protect customers from supplier failure

## Introduction

The gas retail market has been fully open to competition since 1998. The electricity retail market has been fully open since 1999. Subsequently, average annual domestic gas and electricity bills have both fallen by 13 per cent, in real terms.

**Figure 10** Average annual domestic bill including VAT

Average annual domestic electricity bill			Average annual domestic gas bill		
	Nominal terms	Real terms		Nominal terms	Real terms
April 1998	252	273	January 1996	327	381
April 2002	238	238	April 2002	333	333
Fall	14	35	Fall	-6	48
		13%			13%

*Based on average consumption of 3,300 KWh Standard Credit customer*

*Based on average consumption of 19,050 KWh Standard Credit/LatePay customer*

37 per cent of domestic gas and 38 per cent of domestic electricity customers have exercised their choice to switch suppliers. Switching rates are higher than in many other competitive markets in Britain and higher than achieved in any gas and electricity market anywhere else in the world.

Switching rates among lower income customers are broadly the same as rates for customers in other income brackets. The rate of switching among customers on prepayment meters (PPMs) is also broadly the same as for customers on standard tariffs.

The choice of tariffs for customers has also increased. There is now a much greater range of tariffs, services and payment options which demonstrates that innovation is a key benefit of competition.

With competition so established, price regulation was no longer justified. Therefore, during the year, Ofgem removed the remaining price controls on domestic gas and electricity suppliers so that no customer is now on a price-regulated tariff. Instead of direct price regulation, Ofgem will use competition law to protect customers.

**Figure 11** How competition is developing

	Switching in electricity – percentage of each group who are switchers		Switching in gas – percentage of each group who are switchers	
	1999	2001	1999	2001
Proportion of customers who have switched one or more times	11	38	25	37
<b>Special needs</b>				
Pensioner only	13	30	32	29
Disabled	13	44	30	35
Very low income	7	43	29	38
One parent family	11	43	24	39
<b>Social class</b>				
AB	14	36	20	37
C1	11	38	23	40
C2	9	41	29	37
DE	10	36	28	36
<b>Methods of payment</b>				
Direct debit	15	44	28	43
Cash cheque	11	32	28	32
PPM	3	31	14	28
Budget card/plan	6	40	23	32

*Research study conducted for Ofgem by MORI, published November 2001*

Ofgem also worked to increase customer confidence in the competitive market by improving the customer transfer process and extending the marketing licence condition for a further two years to protect customers from unscrupulous sales tactics.

Concerns from industrial and commercial customers about the development of competition prompted a decision to review arrangements for monitoring this market.

During the year, Ofgem passed responsibility for providing customer information and advice to the Gas and Electricity Consumers' Council, energywatch, the body with the primary responsibility for handling complaints and providing information services.



### *Future regulation of gas and electricity supply markets*

In November 2001, Ofgem announced the findings of its annual independent customer research into the state of domestic gas and electricity competition. During the year, it also carried out its own competitive market reviews. Together, they found:

- 15 million customers have switched supplier – a level of switching second only to car insurance
- switching has been across the board – customers on PPM tariffs are switching at broadly the same rate as customers on standard tariffs and customers on lower incomes are switching at the same rate as those who are better off
- 90 per cent of those who have switched have found it very easy, or easy
- 70 per cent of customers were buying their fuel through dual fuel deals
- PPM customers have at least four dual fuel deals available in any part of the country offering cheaper fuel than British Gas and the regional electricity supplier, and
- customers who have not switched have also gained as incumbent suppliers responded to the pressures of competition.

These findings led to the conclusion that competition was now the most effective ‘regulator’ of prices, and resulted in Ofgem’s decision in February 2002 to remove all remaining price controls on domestic gas and electricity suppliers from 1 April 2002.

Instead, it will now devote its resources to protecting customers through a combination of competition law, licence obligations (for example, those governing marketing and customer transfers) and general consumer law.

## PROTECTING CUSTOMERS IN THE FUTURE

### *Making the retail market work effectively*

#### *Customer transfers*

##### *Domestic*

Research shows that 90 per cent of people who change supplier find the process very easy, or easy. However, Ofgem has worked with the industry to improve further customer satisfaction with the transfer process. In June 2001, Ofgem and energywatch introduced a charter to improve co-operation between suppliers to resolve transfer problems quickly and efficiently.

##### *Industrial and commercial*

Following concerns expressed by some industrial and commercial customers about the electricity transfer process, Ofgem began working with the industry to review the way information held on distributors' systems is made available to customers. Ofgem also decided to review the process for the appointment of supplier agents and the transfer of standing data. This work will be taken forward in 2002-2003.

#### *Marketing*

In February 2002, Ofgem consulted on extending its marketing licence condition, which sets out the standards companies should adhere to while marketing energy to domestic customers. It decided to extend the condition for a further two years from 1 April 2002 to put pressure on suppliers to continue to adhere to best practice in sales and marketing.

The condition also allows Ofgem to take action against suppliers whose performance falls below acceptable standards. In the forthcoming year, Ofgem will be working towards ensuring that enforcement procedures under this condition are more transparent and responsive, which means suppliers will have no excuses if they fail to meet the high standards expected of them.

#### *Supplier failure*

During the year, Ofgem put significant resource into helping ensure that customers do not face a threat of disconnection if their supply company fails. The Utilities Act 2000 introduced important new protection and, during the year, Ofgem worked on a project to review the arrangements, across the gas and electricity supply chain, to put measures in place that are relevant and effective.

The collapse in November 2001 of Enron brought the importance of this work into sharp focus. In this case, no customers of its supply arm, Enron Direct, faced a loss of supply.

### *Market monitoring and research*

#### *Domestic customers*

Ofgem monitors the retail market by conducting regular market reviews and customer research, as well as analysing complaints data supplied by energywatch. It also monitors suppliers' Codes of Practice on a quarterly basis to ensure they meet their licence obligations to provide help and advice to vulnerable customers.

Ofgem constantly reviews the retail market, identifying the areas where customer take-up is slow. Its MORI survey showed that older people were switching at somewhat lower rates than the rest of the population. As a result, Ofgem began planning a joint campaign with Age Concern to encourage older people to take advantage of the competitive market. Similar work is planned with rural customers and those customers for whom English is not their first language.

#### *Industrial and commercial customers*

Evidence collected up to 2000 suggested that the industrial and commercial market was effectively competitive and, in the light of this, Ofgem ceased systematic collection of data about these markets. However, competition concerns from industrial customers prompted Ofgem to decide to resume and strengthen its monitoring work in this area.

### *Customer information and advice*

#### *energywatch*

Up to 2001, Ofgem provided information to domestic customers on the range of tariffs and competitive offers in the supply market, as well as general advice on how to switch supplier. The statutory responsibility to provide this service to consumers has now passed to energywatch.

Ofgem monitors the complaints data that is supplied by energywatch on a constant basis and uses these statistics to target its enforcement action.

## *Enforcement*

Ofgem has enforcement powers as a sectoral regulator and as a Competition Authority. In addition, Ofgem can publicise instances of bad behaviour towards customers by the companies it regulates. Ofgem may also use consumer protection powers which it exercises concurrently with the Office of Fair Trading (OFT). Specific powers include:

- licence enforcement action against the companies by provisional or final order
- the power to impose a financial penalty of up to 10 per cent of UK turnover for breaches of the Competition Act 1998
- the new power to impose financial penalties for breaches of the Electricity Act 1989 and the revised power to impose financial penalties under the Gas Act 1986
- to apply for a ‘stop now’ order when a company contravenes consumer legislation, and
- the power to revoke a licence granted under the Electricity Act 1989 or the Gas Act 1986.

## *npower*

In January 2001, Ofgem took enforcement action against npower after unacceptably high levels of complaints from customers about its doorstep selling activities. Ofgem insisted that npower took immediate action to reduce the number of complaints and it agreed with the company a range of undertakings to improve its performance.

As a result of this initiative, npower significantly improved its performance across a number of aspects in its management of direct selling. Ofgem will continue to monitor npower's performance carefully – along with any other company causing concern.

In June 2002, Ofgem announced measures to establish new complaints thresholds which, if exceeded, will result in immediate action against the company concerned. The measures will also tighten the deadlines on companies to put their house in order. Ofgem will use its powers, only recently made available, to impose financial penalties if the problem cannot otherwise be resolved.

## 6. Regulating monopolies

### Key achievements – 2001-2002

- Significant development of the traditional RPI-X form of price regulation achieved
- In gas, final proposals for Transco price control introduced stronger investment incentives and new guaranteed outputs for customers
- New guaranteed and overall standards of performance in gas and electricity introduced to further protect customers
- In electricity, Information and Incentives Project (IIP) completed, placing stronger incentives on companies to meet quality of service targets
- Work undertaken to improve best practice in asset risk management

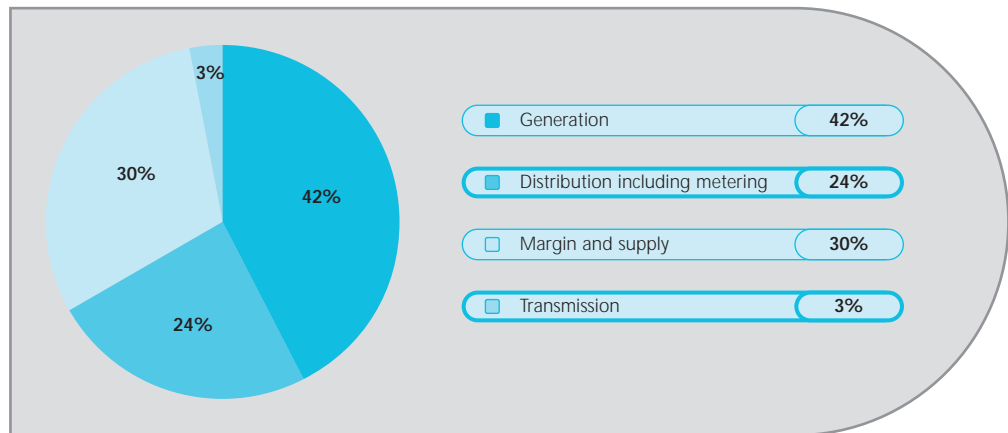
## Introduction

Where effective competition is not practicable, Ofgem continues to regulate through price controls and incentive schemes to ensure that consumers receive value for money and a secure and reliable service.

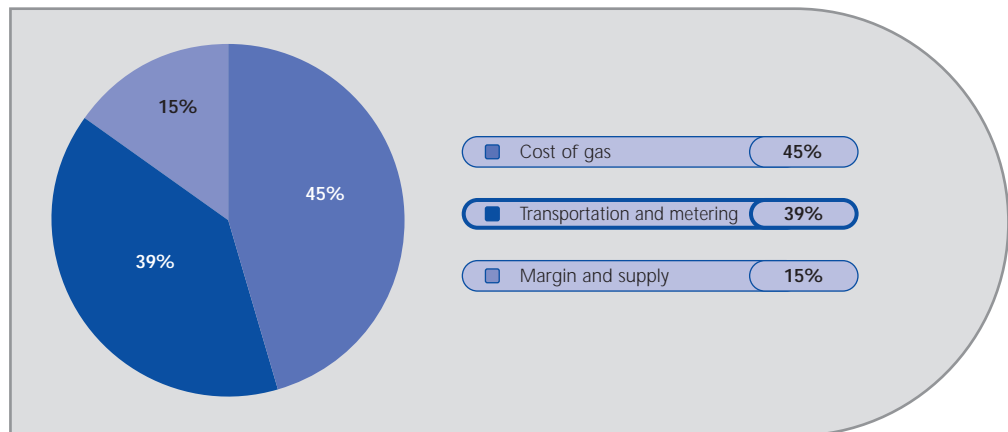
This applies to the monopoly businesses which include National Grid Company (NGC), the two Scottish electricity transmission companies, the electricity distribution companies and Transco. Together, these companies operate the large majority of the pipes and wires bringing gas and electricity to homes and businesses.

The cost of transmitting electricity makes up 27 per cent of the average domestic bill. The cost of transporting gas to customers' homes makes up 39 per cent of the average domestic bill.

**Figure 12** Breakdown of domestic electricity bill



**Figure 13** Breakdown of domestic gas bill



In the year, the National Audit Office (NAO) published a report on 'Pipes and Wires', covering utility networks generally, which showed that consumers have benefited from lower prices, more reliable service and greater network investment as a result of the way these networks are regulated, and identified a number of issues which the regulators will be considering further.

During the year, Ofgem has continued to develop the traditional RPI-X form of price regulation. It has introduced new incentive regimes for more efficient investment, set new quality of supply standards and guaranteed outputs for customers, and implemented incentives to improve environmental performance and monitoring.

### *Gas transportation*

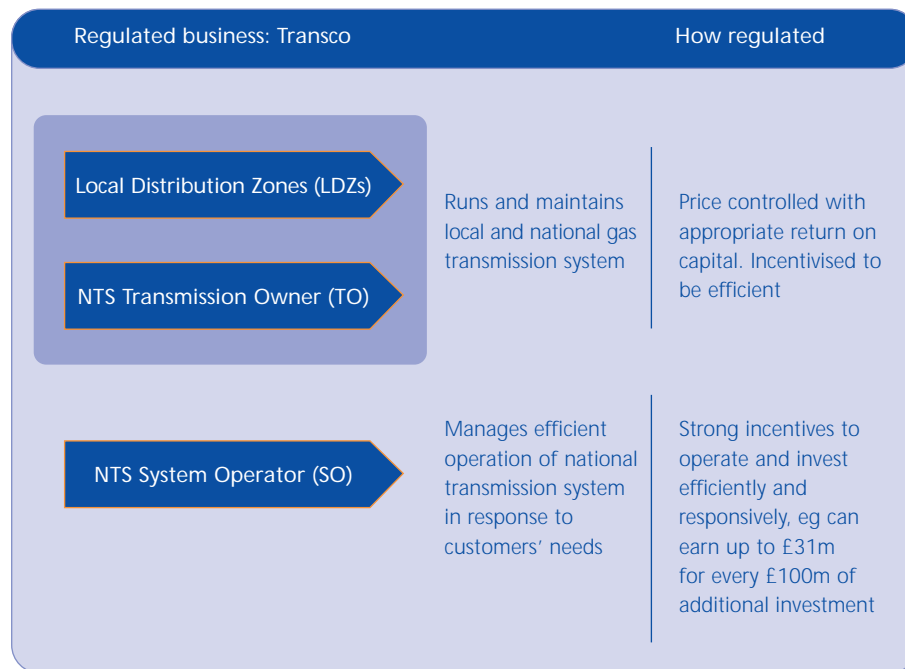
Priorities for 2001-2002 were to complete the ongoing work to review the five year price control on Transco and begin work to review the regulation of Independent Gas Transporters (IGTs).

### *Transco*

It is important that customers receive good value for money from Transco and that the company has incentives to improve its efficiency. At the same time, Ofgem must ensure that Transco operates efficiently, so that it can finance its activities and make the necessary investment to develop the gas network to meet future demand.

Final proposals for the price control on Transco were announced in September 2001. The final part of this process was the announcement in December 2001 of new incentive arrangement proposals that apply to Transco's role as operator of the National Transmission System (NTS) (see Chapter 4).

**Figure 14** New model of regulation for Transco



The price control proposals delivered:

- protection for customers on price, quality of service and security of supply – reflecting Ofgem’s primary concerns and duties
- a reduction in Transco’s revenues of four per cent in the first year, and two per cent per annum thereafter, equivalent to a £5 a year reduction in domestic customers’ bills (before adjustment for prior year over-recovery)
- new quality of service targets and output measures
  - for domestic customers, this means guaranteed and overall standards of service, eg in relation to the number and duration of interruptions to supply
  - for shippers, producers and large customers, this means new incentives for Transco to invest in the National Transmission System (NTS) to meet future demand
- a reasonable allocation between current and future Transco customers of the significant costs of the mains replacement programme, agreed with the Health and Safety Executive (HSE) to meet safety requirements, and
- a cost of capital commensurate with the risks of Transco’s business.

These new arrangements make a valuable contribution to ensuring a safe and secure gas supply.



### *Improving services for gas customers*

New Guaranteed and Overall Standards of Performance were implemented from April 2002. These standards cover areas such as telephone responses to emergency calls, notification of planned interruptions and informing customers when they will be reconnected.

There was also welcome news in November 2001 for customers who find themselves without gas through the actions of a third party. For the first time, as a result of work by Ofgem, they can now receive compensation. Following discussions with Ofgem, Transco clarified arrangements to ensure that all domestic customers who find themselves without gas through the actions of a third party, such as a water company or a cable operator, should receive £20 compensation from Transco for every 24 hours they are off supply.

Work also began on establishing similar quality of supply incentives on Transco as have been developed for electricity distributors. These will place financial penalties on Transco if it fails to meet quality of service targets, and will provide rewards when these targets are exceeded.

### *Independent Gas Transporters (IGTs)*

Ofgem began work to review the regulation of IGTs, who between them transport gas from off-takes on Transco's system to about 240,000 households in Great Britain. Consultation began in 2001 to consider issues relating to quality of service. A further document was published at the start of 2002 on the cost of capital for IGTs.

Ofgem has now introduced new Guaranteed Standards of Performance for IGTs to mirror those that apply to Transco. These standards ensure that customers receive the best possible service from their gas transporters and can claim compensation if the standards are not met.

### *Electricity transmission and distribution*

Monitoring the transmission and distribution price controls continued throughout the year. Work on the structure of electricity distribution charges was deferred so that any conclusions from this work can be taken into account when Ofgem considers changes to the regulatory regime to encourage the development of distributed generation (see Chapter 3).

### *Improving services for electricity customers*

#### *Information and Incentives Project (IIP)*

The final part of the IIP was completed in December 2001. This new scheme places financial penalties on electricity distributors who fail to meet quality of service targets, and provides longer-term incentives for those who exceed the targets, in particular if they achieve fewer and shorter power cuts. The scheme took effect from April 2002.

#### *Multiple interruptions*

In addition to the IIP, further protection has been introduced for electricity customers who experience multiple interruptions to their supply.

The two new measures introduced from April 2002 are:

- a Guaranteed Standard that will provide compensation to customers who experience four or more interruptions of greater than three hours' duration a year, and
- an Overall Standard to measure a distribution company's overall performance in minimising the number of multiple interruptions on its network.

### *Regulatory accounts*

Proposals to develop the form and content of the regulatory accounts for electricity distribution companies were published during the year. The objective of these reforms is to improve the quality of information on the costs of network monopolies, which will allow a better comparison to be made between the information in the accounts and the assumptions underlying the price controls.

Work continues on similar proposals for NGC and the Scottish electricity transmission companies.

### *Asset risk management*

In addition to planned work for 2001-2002, an important initiative was undertaken during the year to improve best practice in asset risk management.

Maintaining the integrity of network assets is one of the key responsibilities of the gas and electricity network companies. Effective risk management is aimed at ensuring that all assets – such as pipes and wires – work properly, meet acceptable performance standards and have minimal risk of failure, both now and in the longer term.

Because this is important to the interests of all consumers, Ofgem plans to issue an annual survey to gauge the current status of asset risk management among companies, with the intention of identifying and encouraging good practice.

This will also contribute to Ofgem's wide-ranging work to ensure security of supply, and the long-term well-being of the nationally important energy infrastructure.

## 7. Competition and industrial structures

### Key achievements – 2001-2002

- Work on separating electricity supply and distribution businesses completed
- Metering strategy put in place to help remove barriers to effective competition in metering and meter reading
- Competition in electricity connections progressed
- Policy on how to handle further distribution company mergers implemented

## Introduction

Establishing appropriate industrial structures that promote rather than obstruct competition is essential to Ofgem's work. For example, it is widely accepted that the benefits brought about by competition in gas supply would have been impossible without the separation of the gas transportation business from the gas supply business.

This year saw further work to extend the scope of competition and promote industrial structures that make it easier for competition to develop further in energy supply and other areas including metering, meter reading, connections and storage.

Ofgem has worked on a major programme to separate the supply and distribution businesses of the 14 former Public Electricity Suppliers (PESs). This work, aimed at enabling all suppliers to have equal access to the distribution network, is now complete.

## Metering

Competition in metering services can deliver significant benefits to customers, including lower prices through reductions in the £800 million annual cost of metering. More competitive arrangements can also bring improvements in the standards of service and can stimulate the development of 'smart' meters.

In the long-term, these could bring further social and environmental benefits by helping to give customers more control over their use of gas and electricity and by providing alternatives to existing prepayment meters (PPMs).

Ofgem published a metering strategy with the objective of securing competition in gas and electricity metering services, as well as encouraging innovation. A key element of this strategy is Ofgem's work to support industry discussions on reviews of electricity and gas metering arrangements aimed at overcoming barriers to effective competition.

In January, Ofgem announced proposed reforms to rules governing the retail gas markets which were prompted by the need to improve the way gas suppliers exchange information about a customer's supply point. This need resulted from changes to the structure of the industry, particularly the separation of Transco's transportation and metering businesses, and by suppliers now seeking alternative meter service providers.

The proposed changes to the rules relating to metering will support the work being carried out by the industry and Ofgem under the Review of Gas Metering Arrangements (RGMA) project to produce industry-wide standards to facilitate the development of competition in this area. Under the Review of Electricity Metering Arrangements (REMA), work continued on discussing with the industry the required industry processes to support competition in electricity metering.

### *Connections*

The costs of new connections to gas and electricity supplies are about £400 million a year – £300 million for electricity and around £100 million for gas. These costs are borne by customers.

Competition in this area will benefit customers by putting pressure on prices, improving quality of service and encouraging innovation.

In electricity, work is under way through an electricity connections steering group, to take forward Ofgem's proposals to facilitate competition. While competition is developing, there are still barriers for electricity connections generally.

Where it is working well is in opening up the market for electric street light connections. This work helps local authorities get a better deal for their street lighting and continued during the year.

In gas, progress was made in the year to introduce a registration scheme of qualified Utility Infrastructure Providers (UIPs).

While competition is flourishing in some areas, such as gas connections for new housing developments, barriers still exist for lower value and simple one-off domestic gas connections.

### *Corporate transactions*

Ofgem has continued important work in considering proposals for business transactions and new financial models, providing advice to the Office of Fair Trading (OFT) and the Department of Trade and Industry (DTI) and liaising with the European Commission on how to protect customers' interests.

Since 1995, corporate transactions have resulted in some of the original 14 regional distribution companies becoming jointly owned or operated. At the end of March 2002, there were only nine independent company groups. The prospect of further mergers or similar transactions will reduce Ofgem's ability to compare company performances when setting price controls.

To compensate for this, in November 2001, Ofgem consulted on whether companies should reduce their charges on completion of a merger or similar transaction by an agreed amount, in addition to passing on savings brought about by efficiency gains from the merger.

Final proposals on the regulatory steps Ofgem will take following any future merger, or similar transaction, were announced in April 2002. These proposals mean that Ofgem will modify the licences of each company affected by a merger to reduce the amount of money they can earn by a total of £32 million.

**Figure 15** Proposed mergers and acquisitions consulted on by Ofgem during the period of the report

Date	Proposal
June 2001	Centrica and TotalFinaElf's purchase of Humber Power Limited
July 2001	International Power plc's proposed purchase of TXU Europe's Rugeley B power station
Aug 2001 & Oct 2001	Dynegy Inc's proposed purchase of BG Storage Ltd
Aug 2001	Northern Electric plc's proposed purchase of Yorkshire's electricity distribution business from Innogy Holdings plc Innogy Holdings plc's proposed purchase of the electricity supply business of Northern Electric plc
Sept 2001	Centrica plc's proposed purchase of TXU Europe's King's Lynn and Peterborough power stations
Oct 2001	AEP Energy Services UK Generation Limited's proposed purchase of Ferrybridge and Fiddlers Ferry power stations from Edison First Power E:on AG's proposed purchase of Powergen plc
Nov 2001	Calpine UK Holdings Limited's purchase of Saltend Cogeneration Company Limited London Power Company plc's proposed purchase of TXU Europe (Hood No. 2) Limited's West Burton power station London Electricity Group plc's proposed purchase of Eastern Electricity plc (Eastern's electricity distribution business) and its 50 per cent shareholding in 24Seven Utility Services Limited Utilicorp United Inc and Deutsche Bank AG's proposed purchase of FirstEnergy Corp's Avon Energy Partners Holdings (Midlands electricity distribution business)
Jan 2002	British Gas Trading Limited's purchase of the gas and electricity supply businesses of Enron Direct Limited
Mar 2002	British Nuclear Fuels Limited's purchase of Scottish & Southern Energy plc's 50 per cent share of Fellside Heat and Power

This will be spread equally across all companies in the merged group over a five year period. Ofgem expects customers to continue to benefit from the efficiency savings generated by the merger through the price control process.

### *Utilities Act 2000*

During the year, significant work was carried out towards completing the preparation of statutory instruments and orders resulting from the introduction of the Utilities Act.

This work confirmed most of the remaining powers Ofgem had been given under the Act. The power to impose financial penalties was given in April 2002. Social and environmental guidance was laid before Parliament in June 2002 but will not take effect before the autumn. The collective licence modification procedures remain outstanding.



## 8. Building Ofgem

### Key achievements for 2001-2002

- First year of Authority governance for Ofgem successfully completed
- Commitment to careful cost control and resource management continues
- Ofgem working to principles of best practice in regulation recommended by Better Regulation Task Force
- Recruitment and reward strategy successful in reducing staff turnover
- Improvements made to explaining Ofgem's work

## Introduction

Ofgem is governed by the Gas and Electricity Markets Authority. In addition to taking overall responsibility for Ofgem's performance, the Authority determines strategy and policy priorities.

Developing Ofgem as an efficient and effective regulator is important in building the confidence of customers, regulated companies and those on whom Ofgem's work has an impact. Much progress was made in this area during the year.

Ofgem continued to work to control costs carefully and manage resources efficiently. Recommendations from an efficiency review of regulators commissioned by HM Treasury in 1999-2000 have, where appropriate, been implemented.

Ofgem also continued to work in a number of areas to attract, develop and retain the calibre of people it needs to achieve the organisation's objectives.

Improvements were made to the way in which the organisation is structured and a number of key work processes were reviewed. Investment was made in the retention of corporate knowledge and improvements continue to be made to the way it communicates and presents its work.

## Governance

Ofgem completed the first year of governance under the Gas and Electricity Markets Authority. As well as governing Ofgem's activity, the Authority is a source of advice and judgement which has significantly strengthened Ofgem's work. This governance demonstrates Ofgem's continuing commitment to de-personalising regulation.

The Authority consists of six non-executive and five executive directors. In April 2002, Lord Currie stepped down as a non-executive director after providing Ofgem with invaluable advice and help. His replacement, Professor Leonard Waverman, was appointed in May 2002.

## Efficiency

Ofgem is committed to ensuring that costs are controlled carefully and resources are managed efficiently – this was a high priority for 2001-2002 and will continue to be so.

Ofgem contributed to the efficiency review of regulators undertaken by HM Treasury. The review showed that the UK regulators are professionally-run organisations and demonstrated many examples of good practice. It also made recommendations about how efficiency could be further improved.

Ofgem's response to the review, published in April 2001, detailed action it had already taken in light of the review's recommendations to improve efficiency and highlighted further action to be taken in 2001-2002.

In July 2001, the Government's Better Regulation Task Force (BRTF) published a report on economic regulators. Ofgem broadly welcomed the report's findings as it highlighted principles which Ofgem already practises and activity that it already undertakes.

BRTF principles which Ofgem already commits to include:

- Ofgem withdraws from regulation wherever it can – the gas and electricity industries are more deregulated than any other utility sector
- it is managed by an Authority, consisting of executive and non-executive members
- it has always consulted extensively, in a variety of ways, with all the different audiences affected by Ofgem's work
- it sets out the rationale behind policy proposals, and
- it prioritises its work programmes, highlights them in an annual Plan and Budget and reports on their progress in an open and transparent manner.

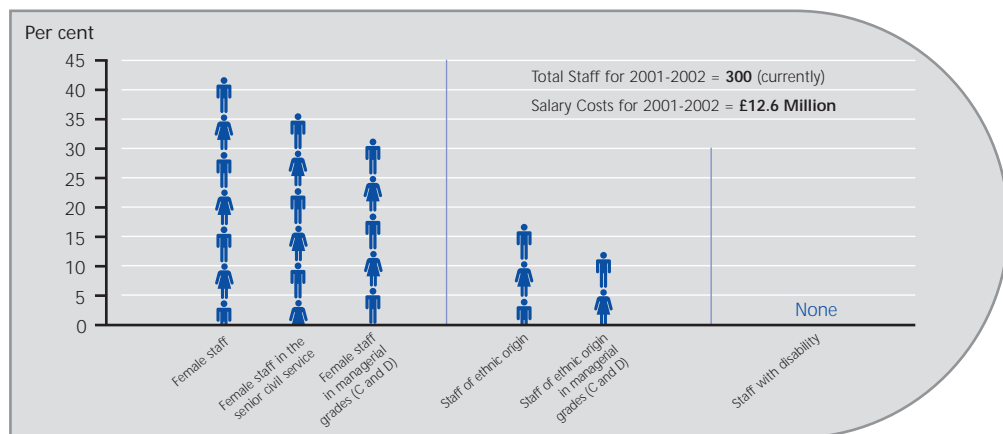
### *Staff development*

During the year, Ofgem continued to recruit, and worked to retain, good staff, with a continuing emphasis on professionalism and necessary specialist skills, for example in the legal and regulatory economics fields, especially at senior levels. A new reward strategy was adopted, allowing greater flexibility and responsiveness, and creating greater stability within Ofgem's workforce.

Ofgem put in place new recruitment and retention strategies which led to improvements to the recruitment process, including greater use of the Internet and new advertising and information packs.

Ofgem recruits on the basis of fair and open competition and selection on merit, in accordance with the Recruitment Code laid down by the Civil Service Commissioners – and there are internal checks to ensure compliance with this Code. During the year, Ofgem successfully underwent an independent audit on behalf of the Office of Civil Service Commissioners.

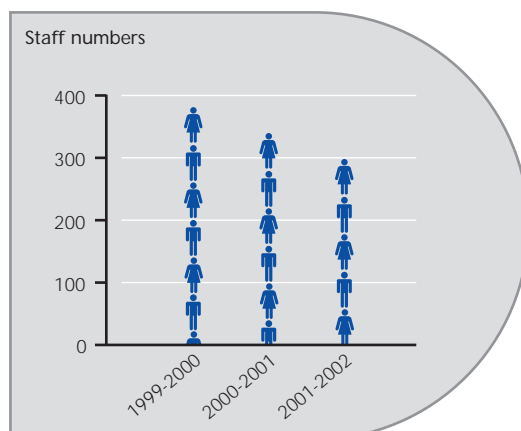
**Figure 16** Equal opportunity issues



During 2001-2002, Ofgem recruited 45 members of staff. Between April 2001 and March 2002, Ofgem did not use any of the exceptions to fair and open competition permitted under the Recruitment Code.

Overall staff numbers – which at the time of the merger were around 380 (excluding staff transferred to energywatch) – fell during 2001-2002 to an average of 303. At the same time, Ofgem reduced costs for use of agency staff from £776,000 to £420,000. Turnover figures were reduced from 20 per cent to 16 per cent. A recent survey on turnover within central Government showed the average to be 16.6 per cent.

**Figure 17** Average staff numbers, excluding those transferred to energywatch



## *Building corporate knowledge and explaining Ofgem's work*

### *Knowledge management*

A strategy to build corporate knowledge by developing new systems and resources to support this was a key priority for the year. This work improved access to relevant and reliable information and increased the quality and efficiency of decision making.

### *Communications*

A communications strategy was developed and implemented in support of the priorities for 2001-2002. It also focused on promoting the distinctive but complementary roles of Ofgem and energywatch, and on continuing to develop best practice standards for consultation.

During the year, Ofgem worked to explain its plans and proposals in a more user-friendly way – in policy documents, through factsheets, the website and other communications vehicles. It continued to report its progress against the deliverables in its annual plan and budget and report on any changes to priorities and timetables.

Ofgem gave evidence during the year to a range of Parliamentary committees, including the Public Accounts Committee and the Trade and Industry Select Committee. Numerous workshops and seminars were held to explain its policies to a range of constituents, including the industry, consumer bodies and trade organisations.

### *Technical advice*

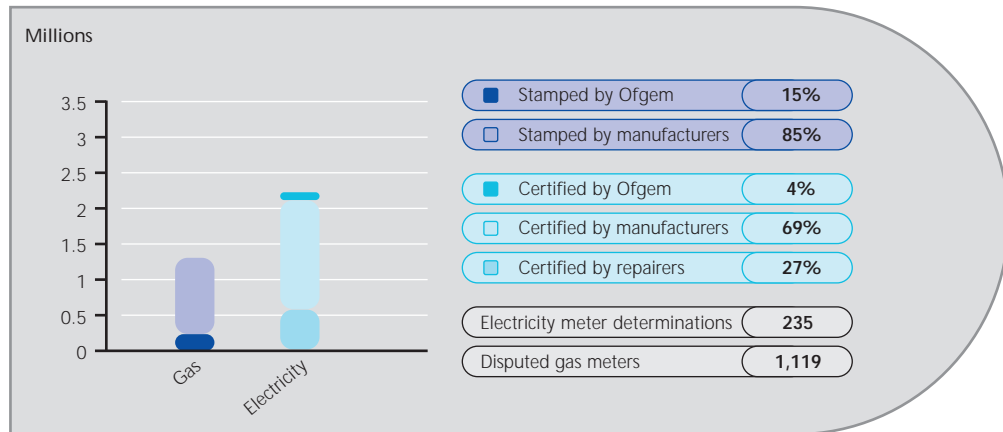
Technical advice and services are currently provided primarily by an Ofgem-staffed Technical Directorate which contributes to Ofgem's wider policy development and is responsible for specific services, including:

- approval for new types of gas and electricity meter
- certifying gas and electricity meters for accuracy
- determining disputes about the accuracy of gas and electricity meters, and
- testing gas quality.

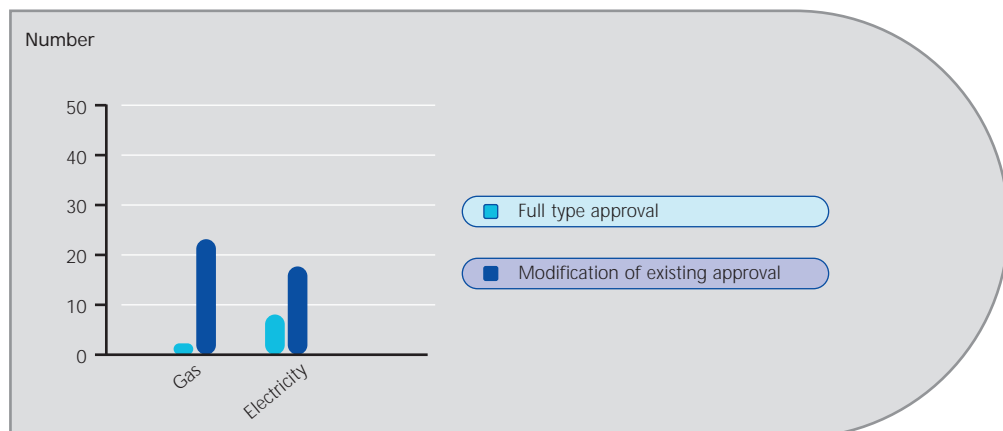
Work to review the range of services and determine whether external providers can add greater value continued during the year. It is expected that this will be completed in 2002-2003. This work is aimed at securing technical services as cost-effectively as possible while giving close attention to the impact on staff involved.

## Meter disputes and determinations

**Figure 18** Number of meters stamped/certified (1 April 2001 to 31 March 2002)



**Figure 19** Meter approvals and modifications (1 April 2001 to 31 March 2002)



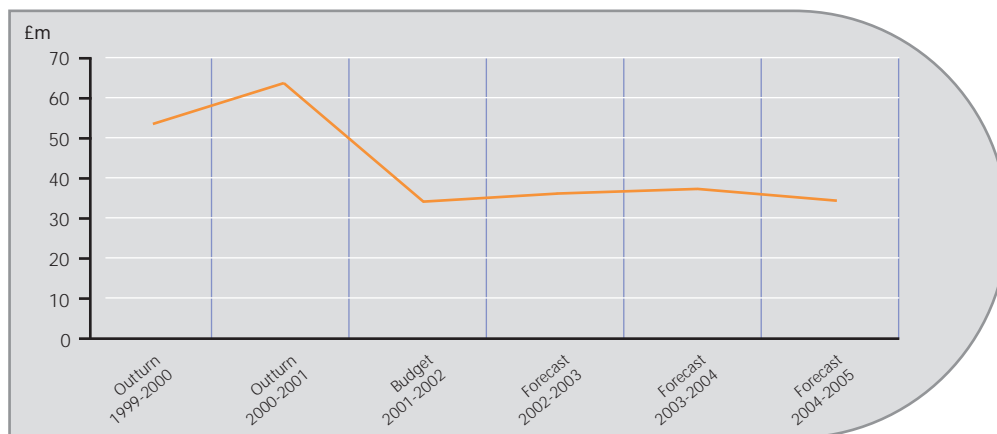
## Financial review

The costs of Ofgem need to be seen in the context of what it achieves. The range of activities remain as wide as ever. The benefits that Ofgem brings are correspondingly large and outweigh its costs significantly. Ofgem's costs represent around 0.1 per cent of industry turnover which stands at almost £37 billion a year.

In 2001-2002, Ofgem received income of £68.5 million, of which £62.2 million was received from licence fees. Of this, £22.4 million was collected on behalf of the Department of Trade and Industry (DTI) to meet energywatch and other DTI costs. Other Ofgem income, mainly from property and charges for technical fees, totalled £6.3 million.

Operating costs in 2001-2002 amounted to £37.6 million, compared with £62.1 million in 2000-2001. Payroll (34 per cent), contractors (17 per cent) and accommodation (31 per cent) accounted for 82 per cent of the total. The steep fall in costs in 2001-2002 was largely due to the completion of the major New Electricity Trading Arrangements (NETA) project in 2000-2001.

**Figure 20** Ofgem trend in spend



Ofgem's original resource budget, as approved by Parliament following a consultation process with industry and other interested parties, amounted to £36.6 million. The resource budget was subsequently increased to £38.7 million to cover additional provisions.

More detailed information on costs can be found in Ofgem's Resource Accounts, published in Appendix 1.

Ofgem's performance against its deliverables is detailed in Chapter 9.

## 9. Key milestones and outcomes

### Key:

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Q1 – Quarter One – April-June 2001

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Q2 – Quarter Two – July-September 2001

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Q3 – Quarter Three – October-December 2001

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Q4 – Quarter Four – January-March 2002

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### Social and environmental action (Chapter 3)

<b>Deliverables</b>	<b>Target</b>	<b>Progress</b>
<i>Social action</i>		
Develop new Codes of Practice for electricity consumer issues	Q2	achieved by target date
Disseminate and act on the results of the seven research projects under Social Action Plan	Q3	achieved Q4
Publish proposals on reducing debt blocking	Q4	delayed, expected Q2 2002
Publish second annual report on the Social Action Plan	Q4	achieved by target date

## Social and environmental action (continued)

Deliverables	Target	Progress
<i>Environmental action</i>		
Implement Environmental Action Plan following publication (from Q1)	Q1	achieved Q2
Accredit generators whose output qualifies for exemption from the Climate Change Levy (CCL)	Q1	achieved by target date
Issue certificates for qualifying renewable electricity generated for CCL exemption	Q1	achieved by target date
Respond to initial recommendations of the Government working group on distributed generation	Q1	achieved by target date
Agree concordat with the Environment Agency (EA) and the Scottish Environment Protection Agency (SEPA)	Q2	EA concordat agreed SEPA concordat delayed
Accredit generators whose output qualifies for the renewables obligation	Q3	achieved by target date
Issue certificates for qualifying renewable electricity generated for renewables obligation	Q3	achieved by target date
Put in place programme of work to respond, as appropriate, to recommendations of Government working group on distributed generation	Q3	achieved by target date
Publish first annual report under the Environmental Action Plan	Q4	delayed, expected Q1 2002
Publish guidelines on best practice on energy efficiency advice	Q4	delayed, expected Q1 2002
Finalise procedures for implementing the new Energy Efficiency Commitment programme	Q4	achieved by target date

## Competition in wholesale markets (Chapter 4)

<b>Deliverables</b>	<b>Target</b>	<b>Progress</b>
Complete review of effect of NETA on smaller generators	Q1	achieved Q2
Publish responses to British Electricity Trading and Transmission Arrangements (BETTA) proposals	Q1	achieved by target date
Consult on proposals for Anglo-Scottish interconnector auctions	Q1	achieved Q3
Publish final proposals on long-term investment signals	Q1	achieved by target date
Publish initial proposals on exit and interruptibles capacity regime	Q1	achieved Q2
Publish final proposals on Anglo-Scottish interconnector auctions	Q2	achieved Q3
Publish decision document on exit and interruptibles capacity regime	Q2	achieved by target date
Set framework for new transmission access regime	Q3	proposals document published February 2002. Industry taking work forward through governance arrangements
Complete review of NETA	Q4	deliverable inaccurate. Unable to undertake end of year review within year. Scheduled for Q2 2002
Implement new NGC System Operator incentives	Q4	achieved by target date
Publish interim proposals on reforms required to implement BETTA (timing dependent on agreement of transmission access arrangements)	Q4	BETTA implementation proposals published December 2001. Further paper Q1 2002
Implement exit and interruptibles capacity regime	Q4	Delayed – pending implementation of licence condition
Begin phased implementation of new gas balancing arrangements	Q4	Delayed due to further discussion with industry

## Competition in gas and electricity supply (Chapter 5)

<b>Deliverables</b>	<b>Target</b>	<b>Progress</b>
Carry out survey of electricity and gas retail supply	Q1	achieved Q2
Publish decision document on improving customer transfers	Q1	achieved by target date
Publish consultation document on supplier failures	Q1	achieved by target date
Review regulatory regime in retail supply	Q2	delayed – rescheduled in 2002-2003 timetable
Publish second consultation paper on business separation licence changes	Q2	achieved by target date
Publish recommendations for revising regulatory regime in retail supply	Q3	delayed – rescheduled in 2002-2003 timetable
Publish initial proposals on price regulation of the former Public Electricity Suppliers (PESs) supply businesses	Q3	achieved by target date
Publish initial proposals for future regulation of marketing	Q3	achieved Q4
Publish decision document on supplier failures	Q3	decision document no longer required
Publish final proposals on price regulation of the former PES supply businesses	Q4	achieved by target date
Publish decision document on future regulation of marketing	Q4	delayed, expected Q3 2002

## Regulating monopolies (Chapter 6)

<b>Deliverables</b>	<b>Target</b>	<b>Progress</b>
Publish draft proposals under Transco price control review	Q1	achieved by target date
Publish initial proposals on structure of electricity distribution charges	Q1	work on hold due to revised work priorities – revised timetable agreed for 2002-2003
Publish initial proposals on incentive regimes under Information and Incentives Project (IIP)	Q1	achieved Q2
Consult on revised regulatory accounting licence conditions, including regulatory accounting guidelines, for the electricity distribution businesses	Q1	regulatory accounting guidelines published July 2001. Consultation on revised licence conditions delayed to 2002-2003 due to delay in the Collective Licence Modifications process
Publish final proposals under Transco price control review. Implementation planned for April 2002	Q2	achieved by target date
Publish final proposals on structure of electricity distribution charges	Q2	work on hold due to revised work priorities – revised timetable agreed for 2002-2003
Implement revised regulatory accounting licence conditions, including regulatory accounting guidelines, for the electricity distribution businesses	Q2	delayed to 2002-2003 due to delay in the CLM process
Consult on regulatory accounting guidelines for the National Grid Company (NGC) and the Scottish transmission businesses	Q2	to be published Q1 2002-2003. Delayed due to discussions with the companies concerned
Publish final proposals on incentive regimes under IIP project	Q3	achieved by target date
Issue regulatory accounting guidelines for NGC and the Scottish transmission businesses	Q3	delayed, expected Q2 2002
Carry out initial consultation and survey about Independent Gas Transporters (IGT) regulation	Q4	achieved by target date – commenced February 2002

## Competition and industrial structures (Chapter 7)

<b>Deliverables</b>	<b>Target</b>	<b>Progress</b>
Complete preparation of statutory instruments and orders resulting from the introduction of the Utilities Act (subject to the Department of Trade and Industry [DTI] timetable)	Q1	achieved Q2
Modify standard licences for all licensees (subject to DTI timetable)	Q1	achieved Q2
Publish metering policy proposals	Q2	achieved by Q3
Publish final proposals on business separation licence changes	Q3	achieved Q4
Publish metering decision document	Q3	superseded by six monthly metering strategy update papers
Implement business separation licence conditions	Q4	achieved by target date

## Building Ofgem (Chapter 8)

<b>Deliverables</b>	<b>Target</b>	<b>Progress</b>
Implement, where appropriate, the recommendations of the Treasury's efficiency review of all regulators (from Q1)	Q1	achieved by target date
Implement learning and development and reward strategies (from Q1)	Q1	achieved by target date
Implement strategy to build Ofgem's corporate knowledge (from Q1)	Q1	achieved by target date
Implement corporate communications strategy to support priorities for 2001-2002 (from Q1)	Q1	achieved by target date
Complete review of Technical directorate	Q3	delayed – phase 2 commenced Q4
Consult on Plan and Budget	Q3	achieved by target date
Implement conclusions from review of Technical directorate	Q4	delayed – phase 2 commenced Q4
Obtain Investors in People accreditation	Q4	delayed, expected Q1 2002
Publish Plan and Budget	Q4	delayed, expected Q1 2002