

Andy MacFaul,
Head of Government Affairs,
Ofgem,
9 Millbank,
London SW1P 3GE

Your reference:

Our reference:

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Direct line : 020 7717 6241

Dear Mr MacFaul

OFGEM'S THREE-YEAR STRATEGY 2005-2008

The Chairman of Ofgem, Sir John Mogg, sent an open letter on 5th August inviting views from stakeholders on Ofgem's strategy for 2005-2008. HSE also notes that the draft strategy will be published in January 2005 and a detailed response to the document will be provided at that time.

The Health and Safety Executive (HSE) believes there are several important areas of work that will provide challenges to the gas and electricity industries and the Authority alike. Ofgem's role and statutory duties will also continue to evolve as new legislation, such as the Energy Bill, is introduced and implemented in response to specific changes required in the utility industries. Equally a continued dependence should be placed on the application of well-established legal requirements in both new and existing environments, however. This, as Ofgem recognises, places a greater emphasis on applying the Government's principles of better regulation encompassing proportionality, accountability, consistency, transparency and targeting, and also contributes to reducing the burden on industry.

Ofgem's commitment to undertake Impact Assessments is one example of transparency and more effective consultation and their use should result in Ofgem's work over the next three years being characterised by considered evaluation of the impact of its policies on industry. The guidelines also make reference to consulting with key stakeholders and introducing a minimum consultation period. The changing nature of the gas and electricity networks coupled with new and increased ownership makes such consultation even more important. Both Ofgem and HSE also need to continue to invest in working partnerships with other government departments, regulators, industry trade bodies and other interested parties in order to apply and clarify existing legal requirements in these changing structures. Where Ofgem decides to withdraw from the regulation of markets in the belief that competition is providing an effective economic control there will remain a need to monitor companies' activities, however. In this environment both Ofgem's and HSE's interest will be that companies do not gain a competitive advantage by reducing their commitment to health and safety either directly or indirectly through their capital maintenance and asset replacement programmes.

Several projects in which HSE has an active interest will no doubt receive priority attention and resource from Ofgem at the outset of the next three-year plan. It will be important to monitor the development of the extended trading and transmission arrangements (BETTA) both in the 'Go Active' period leading up to 'Go Live' next year and beyond. Whilst the necessary structures and arrangements appear complete, HSE believes that it is important for Ofgem to maintain its resource investment as the responsibilities and interfaces between the various parties are worked out and realised on a daily basis. User experience may reveal the need for minor adjustments to procedures and it is important that these are recognised and raised by the key parties and then acted upon at an early stage. The use and application of the new STC code and the modified existing codes will also need to be monitored and the change management arrangements implemented if necessary.

Similarly, now that the sale of Transco's gas distribution networks has been confirmed the arrangements and operational procedures of the new network owners will need to be established and monitored. If the sales are approved by the Authority in November 2004 HSE will need to be satisfied that all parties have addressed public safety issues, including the provision of emergency services and the ongoing mains replacement programme. This will be ascertained via review and assessment of the relevant safety cases. Both Ofgem and HSE will then need to continue to monitor and evaluate the operation of the new industry structure.

HSE has also worked closely with Ofgem and Transco in reviewing the network capacity in winter months, specifically the security standard obligation to meet a '1 in 50' winter demand. Discussions have centred on security of supply issues and minimising the risk of a gas supply emergency. HSE's safety case considerations do not extend to the continuity or security of supply for Britain as a whole, but only to ensuring that the risk of a supply emergency is minimised. Security of supply is for others to consider and Ofgem will play an important role here. If, as Ofgem plans, new arrangements are in place for this winter then these will need to be monitored both for 2004/05 and in future years to review their effectiveness. Again an ongoing commitment of resource will be required here.

In the development of renewable energy technology the Distributed Generation Co-ordination Group and the Technical Steering Group have been important priorities for Ofgem. With the anticipated changes to both of these groups Ofgem will need to decide the most appropriate method and forum for taking forward the Government's targets for renewable electricity generation and reduced carbon dioxide emissions. A clear lead will be required from the Department of Trade and Industry especially as new and existing technologies are developed and potentially become more cost effective. This may lead to a refocusing of priorities for generation and Government and industry will need to adapt accordingly. The safe incorporation of these technologies into the existing networks will remain HSE's priority.

Introduction of the new price control for the electricity distribution networks in April 2005 will obviously remain one of Ofgem's main priorities. This will be followed by the aligned price controls for the gas and electricity transmission companies in April 2007 and for the gas distribution network operators in April 2008. Ofgem has already stated its intention to balance the need for capital investment and maintenance of the networks by operators against a requirement for efficiency. Ofgem has also recognised the need to set financial incentives at an appropriate level and link them with outputs such that the rewards available for companies do not encourage reduced or deferred investment. The intention to remove overall standards of quality of service and performance targets and replace them with reporting requirements under the Incentives and Information scheme will need to be monitored to assess its effectiveness. An ongoing evaluation of the rewards and penalties applied to planned and unplanned interruptions will also be needed and again the correct balance must be found between encouraging improvements to the quality and reliability of service with the routine maintenance required for network reinforcement or repair.

I hope these comments are helpful to the process of drafting Ofgem's strategy and HSE looks forward to its publication next year.

Yours sincerely

Mike Leppard
Policy adviser