

## Minutes of the sixth Ofgem Environmental Advisory Group meeting

**Date:** 28 October 2004

**Time:** 10.30 – 12.30hrs

**Place:** 9 Millbank, London

### **Present**

#### Chair

Sir John Mogg

#### Members

Andy Duff, RWE npower  
Neil Davies, Environment Agency  
Henry Derwent, Defra (part)  
Paul Ekins, Policy Studies Institute  
Paul Jefferiss, RSPB  
Eoin Lees, Eoin Lees Energy  
Ian Marchant, SSE  
Jeremy Nicholson, Energy Intensive  
Users Group  
John Roberts, United Utilities  
Philip Wright, Scottish Executive  
Graham White, DTI

#### Ofgem Authority members

Boaz Moselle

#### Ofgem staff

Virginia Graham  
Sarah Samuel  
Alex Thorne

### **Apologies**

Robin Bidwell, Gas and Electricity Markets Authority  
Juliet Davenport, Good Energy  
Rupert Fraser, Fibrowatt  
Bryony Worthington, Friends of the Earth

### **1. Chairman's welcome and opening address**

Sir John welcomed everyone to the meeting, and presented apologies received.

### **2. Minutes from previous meeting**

There were no comments from members regarding the minutes of the previous meeting.

### **3. Taking account of the environment in Ofgem's work**

Sir John introduced this item by saying that some commentators had a view that Ofgem was hostile to the environment and that he thought that this was an unfair perception. For instance, a lot of work had been going on in relation to the Distribution Price Control Review, the associated distributed generation incentive mechanisms and the area of transmission re-enforcement.

Boaz Moselle explained that the Authority had recently been discussing Ofgem's work in relation to the environment. This was timely due to changes in senior management and Authority membership. He mentioned also the new duty to contribute to sustainable development contained in the Energy Act 2004. In its discussions the Authority had renewed its commitment to contributing to the Government's environmental targets and agreed a more concrete framework for taking account of the environment in Ofgem's work in the future. This was based on a clear understanding of the legal interpretation of its duties.

Boaz Moselle explained that the statutory framework:

- places a clear upper bound on what actions the Authority can undertake in pursuit of its secondary objectives by making the principal objective overriding; but
- allows a significant level of discretion within that bound. The existence of that margin of discretion requires that Authority to make difficult judgements on a case-by-case basis, and on occasions, to reconcile between conflicting concerns.

On this basis, the Authority agreed to adopt a framework of rigorous and consistent analysis, to balance the objectives carefully and ensure that Ofgem continues to engage fully in the debate on wider environmental policies. The following procedural steps will be used to implement this agreement:

- policy appraisal – appraisal of all alternative decisions, in the light of all our statutory duties;
- evaluation – rigorous but proportionate evaluation of material environmental consequences. The use of a figure or range for the social cost of carbon would be incorporated, in line with the rest of government;
- responsibility within Government – Ofgem will consider its own roles and responsibilities alongside those of environmental regulators;
- balancing of duties – after being presented with the analysis, the Authority will make its decision. It may have to make difficult judgements within its range of discretion, and
- contribution to debate – continuing to engage in analysis and debate of environmental policies, championing approaches that would achieve environmental goals at least cost to customers.

Members raised the following issues:

#### Consumers' interests

- The principal duty overrides the secondary duties but only where there is a conflict between the two.
- Does the interpretation of principal objective as price and quality of service mean low bills or low unit price?
- If it means the latter, does it mean the lowest price today or the lowest price in the longer term?
- Is it true that legal interpretation of consumers' *interest* is so narrow?
- How transparent will the options be as a result of the procedural steps set out?
- Is Ofgem structurally prevented from contributing to sustainable development by the fact that the principal objective is overriding? (The principal duty constrains the options by giving priority to the economic leg)
- If this is so, how can you resolve this paradox?

- Given the above, what difference will the new duty be likely to have?
- How do you resolve the trade-off between current and future consumers?
- What issues does 'quality of service' include (for example, might it include the environmental quality of the energy source used to produce it)?
- In the context of price and quality of service, is this what customers want or what the regulator thinks they want?
- Ofgem can be less risk averse when influencing the debate.
- The trade off between present and future customers will impact on security of supply and will depend on investment decisions taken today.

#### Environment

- What does improving environmental policy mean?
- Is the interpretation presented the best there is, or is it rather conservative?
- Does Ofgem help achieve Government targets?
- There is still a perception that Ofgem does not take the environment as seriously as it should.
- The DPCR is a good example of where Ofgem has made a difference, but are there any others?

Sir John stated that Ofgem did not feel "structurally constrained" by its duties. The Secretary of State's social and environmental guidance is clear: in areas where the Government has a clearly stated policy, major decisions that may have significant financial implications on consumers or companies will be taken by Ministers.

Virginia Graham emphasised that the primary and secondary duties contain the elements of sustainability; the new sustainable development duty builds on these, and will help to emphasise the need to reach balanced solutions. Ofgem does not want to give the impression that it will not make a difference but equally it will not mean a radical change either.

Boaz rounded up by saying that it was not for Ofgem to question our principal objective and other duties. Ofgem has to work within the framework set by Parliament. This includes making judgements on a case-by-case basis. The Authority does have discretion below the 'ceiling' of the principal duty. The Authority also takes the Secretary of State's social and environmental guidance seriously. Nonetheless Ofgem is likely to be a relatively small player within the overall context of the government's environmental policy.

Sir John thanked everyone for a good debate and recognised that there was a consensus that Ofgem was being a little unambitious. He pointed out that this paper was a reflection of work in progress. He said that henceforth the Authority would be looking at issues on a case by case basis supported by rigorous analysis. One of the next steps would be to examine the EAP guidelines of 2001 and see if any changes were necessary.

#### EU – ETS

Sir John asked Henry Derwent to comment on the announcement the previous day regarding the EU Emissions Trading Scheme. Henry said that the Government was committed to a 'business as usual' basis for allocation of credits. Business as usual is a moving target and each round of analysis had given a higher value for business as usual. The decision has been taken at the highest level and will take many months to implement.

A number of points were raised by members and included:

- We seem to have gone backwards for phase 1.
- When will industry find out individual allocations? It is hard to run a business with this level of uncertainty.
- There has been a lack of consultation and the Government has upset almost every constituency.
- The cost of implementation will be greater now because of the inability to manage decisions over the next 2 – 3 years.
- Will this open the floodgates for other Member States to do the same?

Mr Derwent said that the Commission will take several months to analyse the calculations and he did not expect a firm decision before January 2005.

#### **4. Ofgem's current work on consumer information**

Sarah Samuel introduced this item and began with the work on consumption information. She stated that research has shown that customers would like consumption information on their bills in a fairly simple format – ideally a bar chart comparing consumption with the same period in the previous year. Ofgem is in the process of working with suppliers to evaluate the potential benefits to customers.

The Warm Plan is being undertaken by HelpCo and involves installing 200 smart meters in the homes of pre-payment meter customers. The project will monitor, amongst others, any reduction in consumption or price and market acceptance. It will report in the Spring of 2007.

Fuel mix disclosure is the only mandatory policy under this workstream and is required by the 2003 Electricity Liberalisation Directive. Sarah stated that the DTI has the responsibility of implementing the provisions to ensure that suppliers supply their customers with details of the fuel mix of their electricity supply. It is envisaged that this will be done through a supply licence condition implemented via the provisions of the European Communities Act. Currently, a revised draft licence condition is being amended by Ofgem and the DTI as a result of Ofgem's recent consultation.

Sir John asked for a clarification on the timings for the three projects. Sarah stated that Warm Plan reports in Spring 2007, fuel mix disclosure comes into force on 1 April 2005 and that on the consumption information work the likely timetable is starting a trial in autumn 2005, which will last for 1-2 years..

Members raised the following points:

- 'Need' is the wrong way to look at this, is it more about educating people and changing cultures?
- The bill is a statement of consumption – isn't it more about re-presenting the data in a statement of historical consumption?
- What is the quality of information like? Some bills are estimated.
- Try to make suppliers compete in this area – do not regulate.

Virginia Graham said that Ofgem is looking for suppliers to come forward and take part in trials to test the usefulness of historical consumption data, both for energy efficiency and for switching purposes. It will be taken forward on a voluntary basis but if nothing happens as a result of this then a regulatory route may be an option.

- It will only work if, when a customer switches, the new supplier has access to the previous supplier's data for the previous year.
- Some people do not see a link between turning on lights and the environmental consequences.
- Where would a supplier go if they wanted to include benchmarking data on their bills? Or if suppliers did not include this information, where would customers go?
- It would help if suppliers could reduce the amount of statutory information currently on bills.
- It is an opportunity for suppliers to differentiate.
- Difficult to display data in a understandable way - 95% of customers wouldn't understand the example fuel mix chart.
- What is the objective of the information? At the moment the policies are coming from different positions, without seeming to be aimed at a clear objective (awareness-raising, supplier-switching, energy conservation?), let alone any analysis of the best way of achieving it; one policy-driver (labelling) is bottom-up and the other (from the EU) is top-down. An overall carbon reduction framework is needed, set by Government, into which these policies can fit.
- A good overseas example is the Kansas City Power and Light company which has had smart meters for about seven years now.

Sarah responded that Ofgem is working with interested suppliers to ensure that the consumption information is kept simple and that any practicality issues are taken into account.

Sir John summed up by saying that he thought that there was a kind of paralysis here as the work is taking a long time and was too complicated. We need to know where we're trying to get to and agreed that some form of overall framework was needed.

## **5. Biomass as a renewable energy source**

Paul Ekins presented the conclusions from the recent special report from the Royal Commission on Environmental Pollution (RCEP) on *Biomass as a renewable energy source* (copies of the slides accompany these minutes). The RCEP report states that there has been insufficient development of biomass and that the UK needs to catch up with the rest of Europe. Biomass has a number of benefits including: the double benefit of heat and power, and a proven and readily available technology. It is also storable and portable.

The report highlights a number of recommendations in response to policy failures. These include: the introduction of a 'green heat' obligation similar to the Renewables Obligation, guaranteed purchase contracts and a relaxation of the co-firing blending rules under the RO.

Paul cited the example of Austria where biomass is 14% of total energy consumption. There are 17,500 biomass heating installations and 200 district heating plants.

As part of the Government response to the report, Defra has set up a task force led by Sir Ben Gill and assisted by John Roberts and Nick Hartley. John said that they were going to be starting soon and had had some initial meetings. They will not be going over the same ground as the RCEP but will be concentrating on the practical issues on how to take the work forward. They intend to issue a report in one year's time. There is also a parallel group in Scotland.

Members' comments on this item included:

- What about larger scale plant? Would there be planning issues here?
- There were a number of omissions from the report: what about biomass for transport? Is GM biomass feasible?
- There could be negative consequences for forest management if forest residues are used.
- Who would be obligated to supply heat?
- How would a heat obligation be enforced?
- One member said that domestic wood burning stoves are very expensive. Are prices in Austria lower?

Graham White stated that the DTI has a capital grants scheme which includes biomass. Even with grants the projects don't seem very encouraging. In another initiative the DTI had been looking to use biomass in homes not connected to the gas network but it has been difficult to put together viable projects as they are expensive. More work is needed in this area.

Henry Derwent provided a written response from Defra as he had to leave early. It said that supply chains must be established which is why co-firing is currently supported. All types of biomass can benefit from this measure. Defra has introduced the bio-energy infrastructure scheme to provide additional support. It went on to say that renewable heat will be considered in the review of the Climate Change Programme as Defra recognises that renewable heat has the potential to reduce CO<sub>2</sub> emissions.

Sir John concluded by saying that it was an interesting debate and that although a degree of government intervention is required to get the market started, it must be sustainable in the long run.

## **6. Any other business**

Paul Jefferiss said that he had a matter that he wished to raise but in view of the time he would raise it at the next meeting and may write a letter setting out his concerns in the meantime.

Jeremy Nicholson volunteered to prepare a paper on progress towards carbon reduction targets. His offer was accepted, and the precise scope will be the subject of further discussion.

## **7. Date of next meeting:** Thursday 17 February 2005 10.30 – 12.30