



ofgem E-Serve

Promoting choice and value

for all gas and electricity customers

Forward Work Programme 2012-13

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Overview:

GEMA is legally required to publish a forward work programme before each financial year containing a general description of the projects it intends to undertake and their objectives.

This summary of key proposed projects for the 2012-13 year is published solely to meet the statutory requirement to consult on a forward work programme.

Introduction

Many aspects of the GB gas and electricity markets, and of the role of the Gas and Electricity Markets Authority (GEMA) in relation to them, are currently under Government review in the context of the Electricity Market Reform. Nevertheless GEMA is legally required to publish a forward work programme before each financial year containing a general description of the projects it intends to undertake and their objectives. This summary of key proposed projects for the 2012-13 year is published solely to meet that statutory requirement.

Ofgem is grateful for the responses received on the draft of the plan published in December 2011 and these are published on our web site. It is important to recognise that aspects of the plan may change. This document does not cover the many substantial and critical ongoing activities of GEMA, nor are we required to include the routine activities in the exercise of GEMA's functions.

Ensuring that Britain's energy market is competitive and works efficiently, and is integrated with neighbouring EU markets, to protect the interests of gas and electricity consumers (current and future) will remain central to GEMA's work when reformulating its strategy in response to the changes once they have been made. A full Corporate Strategy and Plan will be formulated when the key decisions have been taken by Government.

In May 2011 the Department of Energy and Climate Change (DECC) concluded its review of Ofgem and confirmed its commitment to independent regulation and the critical role Ofgem will play to help realise the Government's energy and climate change objectives. DECC also published the findings of its Delivery Landscape Review. We welcome the positive comments about both our role as regulator and the strong role E-Serve plays in delivering environmental programmes on behalf of DECC.

Following its review of GEMA, we are working with Government on the governance arrangements surrounding the development of a 'Strategy and Policy Statement'. This will enable the Government to set the context for energy policy, provide clarity on the respective roles and responsibilities of Government and the regulator, and specify outcomes for the regulator to deliver.

In October 2011, the EU Third Package Directives were transposed into British law. These make changes to our powers and duties as National Regulatory Authority (NRA), to be exercised impartially and independent of Government and industry. As NRA we now have duties to remove the barriers to cross-border trade, to promote well functioning European gas and electricity markets, and to co-operate with other NRAs through the Agency for Co-operation of Energy Regulators (ACER).

The Corporate Strategy and Plan published in March 2011 included four strategic priorities to protect the interests of consumers:

- contributing to the achievement of a **low carbon** energy sector
- helping to maintain the **security** of Britain's energy supplies
- promoting **quality and value** for all consumers
- ensuring the timely and efficient **delivery of Government programmes for a sustainable energy sector.**

These priorities remain valid and thus the programme is based on them, identifying the key projects which Ofgem plans to undertake in 2012-13. An estimate of the overall expenditure which GEMA expects to incur to deliver those projects and its routine activities in the exercise of its functions is also provided.

Any questions about this document should be addressed to:

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1. Contributing to the achievement of a low carbon energy sector

1.1. EU and UK targets for curbing greenhouse gas emissions and increasing renewable power provide the overall policy direction for the energy sector. One of the Government's key goals is to reduce carbon emissions. In the context of its other duties, Ofgem will work hard to promote a cost-effective switch to low carbon energy on a timescale consistent with the Government's targets.

1.2. We will continue to pursue our cross-cutting sustainability duties to protect present and future consumers. These include using our powers to promote low carbon energy usage, give consideration to other environmental impacts (such as visual amenity) and to protect vulnerable consumers in particular. In addition to our regular work with consumers, we will pursue these goals across all of the projects identified in this programme. Of particular relevance are the Low Carbon Network Fund and the sustainability objectives embedded in the new 'RIIO' (Revenue = Incentives + Innovation + Outputs) approach to price control reviews designed to encourage the required investment.

1.3. We will continue to encourage demand-reduction measures and informed consumer participation in them. We will continue to work with Government on the detail of the Green Deal and issues raised by the development of new markets, such as renewable heat, which will have an important role in meeting Britain's renewable targets.

1.4. Ofgem will continue to work on a regulatory regime for investment in interconnection with neighbouring markets which can play an important role in managing GB's transition to a low carbon energy sector.

1.5. Consistent with the Government's goal of minimising fuel poverty, we will aim to ensure that the financial burden of moving towards a low carbon sector does not fall disproportionately on those least able to pay.

Key projects planned for 2012-2013

Ofgem's work on RIIO, interconnection investment, smart grids, smart meters, transmission charging, system operation, electricity market reform, offshore transmission and delivery of new and existing Government environmental programmes will all make a major contribution to achieving sustainability objectives. Our projects are described in the following sections.

2. Helping to maintain the security of Britain's energy supplies

2.1. Changes in energy markets are likely to impact future security of supply for Britain's consumers. These changes include: declines in indigenous gas production, increasing reliance on gas imports from continental Europe and beyond, greater interconnection with neighbouring countries and increasing liquefied natural gas import capacity. There are also changing perspectives on nuclear both here and in Europe especially in light of Fukushima, the impact of emissions policy, especially on coal, and the demands of achieving renewables targets, including the handling of intermittency.

2.2. Well functioning markets in continental Europe are vital to Britain's security of supply. The European third package created a new legal framework; it provides for legally binding network codes, designed to remove barriers to cross-trade and integrate national markets. Collectively these network codes will form the basis of the target model for Europe's gas and electricity markets. Ofgem will continue to take a leading role on ACER's Board and in its working groups, and look at what the European target model means for GB markets.

2.3. In 2010 Ofgem's Project Discovery estimated that £200 billion of investment may be needed in Britain's energy infrastructure by 2020. It also identified a range of options to deliver security of supply and environmental objectives. The Government is developing its proposals for electricity security of supply in its Electricity Market Reform programme. We expect to continue to work with Government to ensure that these proposals are aligned to consumer interests.

2.4. Our approach to the RIIO price control reviews will facilitate the necessary investment in networks by establishing a clear strategy for each review early in the process. This will govern our approach and assessment of network company business plans throughout the reviews. All parties, including investors, will benefit from increased certainty and clarity about how we are making regulatory decisions.

2.5. The Government has also asked us to review whether action is needed to ensure that medium to long-term gas supplies for consumers remain secure.

2.6. We will continue to work with government, industry and the research community to identify the impact and risks around technological and market developments which will be important in shaping the energy landscape.

Key projects planned for 2012-13

- We plan to report to Government, following our **review of Gas Security of Supply**. Our review aims to assess whether there may be a need to enhance the security of gas supply in the medium to long-term.

- Ofgem is currently undertaking a Significant Code Review (SCR) in relation to the market incentives in the event of a Gas deficit emergency. In conjunction with the review of Gas Security of Supply, we expect to develop the proposed **Gas cash out** arrangements better to reflect the value of security of supply to customers, incentivising investment in measures to reduce the likelihood, duration and extent of any Gas deficit emergency.
- The Government has published its **Electricity Market Reform** proposals and we are working with Government and industry as the regulator to seek to ensure that these fundamental reforms to generation encourage investment in low carbon generation and enhance security of electricity supply in alignment with consumer interests.
- We plan to conduct a significant code review, which will develop proposals to improve **Electricity Cash Out** arrangements that keep the electricity system balanced.
- We are working with ACER and European regulators on the development of **European network codes** to remove the barriers to cross-border trade and to promote market integration.
- We plan to assess the implications of the **European target model** for the GB market and regulatory arrangements.

3. Promoting quality and value for all consumers

3.1. Upward pressure on global energy prices, driven principally by rapidly increasing demand for energy in the industrialising countries, has had an impact on British consumers' ability to meet their fuel bills. Measures to meet low carbon targets, combat fuel poverty, ensure security of supply and secure the investment needed are all providing further upwards pressure on prices. In this environment, it is important for consumers to know that the market is working effectively. Our Retail Markets Review consultation document published in March 2011 concluded that the market was not fully effective and proposed radical remedies. Implementing these fundamental changes to the retail market will be a major focus of our work in 2012-13. The design and management of energy networks will require significant change to adapt to changing sources of gas supply, changing patterns of electricity generation, especially to achieve low carbon generation, and to changing patterns of demand. Our recently developed approach to setting and monitoring the amount of revenue network companies can recover from customers, known as 'RIIO' will be a further major focus of our work.

3.2. Transmission and system operation charges are in danger of becoming an increasingly significant part of consumers' bills. We therefore have several projects aimed at reforming these charges to ensure value for money for all consumers. These will be developed in line with European policies for energy markets.

3.3. We will continue to report on the way companies meet their obligations and where necessary take action - including enforcement action - to make sure that companies treat customers fairly and deal with complaints effectively. With the scale of challenges facing consumers and the industry, this aspect of our work has, regrettably, grown significantly and we will be reviewing ways in which to make enforcement action swift and more effective whilst remaining fair and transparent.

Key projects planned for 2012-13

We plan to consult upon and implement the various proposed reforms to the gas and electricity retail markets identified in our **Retail Markets Review** published 2011. These include measures to improve tariff comparability, strengthen the remedies implemented in our previous Probe and improve reporting transparency. The objectives of this project are to enhance competition, improve consumer engagement and confidence and protect vulnerable and disengaged customers. Separately we will also consult in the year on the development of a vulnerable consumer strategy.

- We plan to publish and implement our recommended reforms to enhance **liquidity** in the wholesale electricity markets. These reforms are designed to ensure adequate liquidity to permit non-vertically integrated energy suppliers to compete effectively, to encourage competition between the major energy suppliers, and to provide transparency of wholesale energy prices and costs.

- We expect to conclude a number of **mis-selling investigations**. Our enforcement activities are carried out with a view to ensuring that energy market participants meet their obligations towards consumers and ensure that energy markets are as competitive as possible.
- With the current increase in enforcement cases, we plan to progress our **review of the enforcement process** aimed at delivering targeted, swift and transparent improvements to the operation of energy markets across the widening range of compliance issues that we pursue.
- We will continue to engage constructively with DECC on its regulatory design for **smart meter rollout**, and start taking on new regulatory functions during 2012-13 as the Secretary of State begins to implement the regulatory changes required for rollout. We will also progress our smarter markets strategy review to identify how we can best contribute to ensuring that wider reforms enabled or required by smart metering are progressed in an effective and co-ordinated way.
- We will finalise the first **transmission price control (RIIO-T1)** for the next eight years for the four gas and electricity transmission companies. We will also finalise the **gas distribution price control (RIIO-GD1)** for the gas distribution networks. These will be aimed specifically at ensuring that the transmission and gas distribution companies play a full role in facilitating a sustainable energy sector whilst maintaining value for money for current and future consumers.
- Our **price control review for electricity distribution (RIIO-ED1)** will commence in 2012 with a consultation on the key issues the review needs to address. We will be looking to understand how the current incentives are working and, in particular, what changes we should make to incentivise companies to meet the new demands which will be placed on them through the take up of low carbon technologies.
- We will continue our work through the **Smart Grid Forum**, which we chair jointly with DECC, to explore the value that smart grids could provide to the entire energy chain. In parallel, and drawing on the lessons arising from the smart grid demonstration projects funded through the **Low Carbon Networks Fund**, we will consider the regulatory changes that might be needed to facilitate smart grid development.
- We will continue to allow funding for the build out and reinforcement of the electricity transmission network through our **Transmission Investment Incentives (TII)** Review where this drives demonstrable value to consumers.
- We expect to conclude **Project TransmiT** by reaching a decision whether to make any change to the charging methodology for the use of transmission assets. The project aims to identify the best methodology to facilitate the transition to a low carbon energy sector, whilst maintaining safe and secure supply and value for money energy services for consumers.
- We will review the regulation of the gas and electricity **System Operators**, in order to set longer-term incentives that allow for interactions with transmission owners and developments in the role of the system operator.

- We expect to conclude our work on **investment in cross-border electricity interconnection** looking at the principles of a cap and floor regime. This will facilitate the transition to a low carbon energy sector and promote market integration.

In addition to our work outlined above on the development of European framework guidelines and network codes, and considering the implications of the European target model for GB markets, we will also be responsible for enforcing the new European rules, including:

- the **certification of Transmission System Operators** which we expect largely to complete in 2012-13
- implementation of EU regulation on **wholesale energy market integrity** (REMIT) designed to protect against market abuse
- **Transmission System Operators** compliance with the European Third Package requirements, particularly in relation to cross border activities.

4. Ensuring the timely and efficient delivery of Government programmes for a sustainable energy sector

4.1. Ofgem E-Serve was set up to use our regulatory and industry expertise to support the delivery of rapidly growing Government climate change programmes and to manage the regulatory regime for offshore electricity transmission networks. Ofgem E-Serve implements, administers and ensures compliance for a number of programmes, such as Feed-In Tariffs, the Renewables Obligation and the Carbon Emissions Reduction Target. These programmes are vital to meeting the UK's challenging environmental targets.

4.2. Ofgem E-Serve will seek to maintain its strong two-way relationship with Government and with Ofgem's own regulatory activity and will continue to build public and industry confidence. We are ready to work with Government, as required, on developing and delivering new initiatives, such as those related to the Energy Company Obligation.

Key projects planned for 2012-13

- Ofgem will continue to manage the **offshore transmission** regime. This includes running competitive tender processes for the right to own and operate the transmission links connecting offshore windfarms to the GB market and further development of the enduring regime.
- We will work to implement conclusions from our joint project with DECC, in relation to **offshore coordination** which are expected in February 2012 and to adapt the existing offshore transmission regime during 2012.
- Ofgem will continue to develop and administer the **Renewable Heat Incentive** efficiently and will provide systems which are robust in protecting from risks including risks of fraud.
- Ofgem will work with DECC to ensure that the **Energy Company Obligation** scheme is well-designed and allows for efficient and robust delivery.
- Ofgem E-Serve will continue to work with Government and industry to seek to deliver the **Carbon Emissions Reduction Target** and the **Community Energy Saving Programme** targets and sub-targets.

Budgets and Spend

Funding

1.1. Ofgem's budget is funded by fees collected from licensed energy companies. Ofgem E-Serve's costs are met from a variety of sources, predominantly either from the schemes themselves, such as the offshore wind programme, or from DECC's budget. We also receive a contribution from DEFRA to cover our share of the costs of running the headquarters building shared by Ofgem and DEFRA.

Five year plan

1.2. Ofgem's estimated gross costs for the next five year period are set out below.

Figure 1: Ofgem's expenditure

£m	2011-12 Planned	2012-13	2013-14	2014-15	2015-16	2016-17
Smarter Grids & Governance	18.4	19.7	19.2	19.1	17.9	17.9
Markets	15.8	20.3	19.5	19.6	20.0	20.5
Sustainable Development	7.9	10.6	10.7	10.2	10.6	10.9
Scotland, Wales & the Regions	1.4	1.4	1.5	1.5	1.5	1.5
OFGEM E-SERVE	28.5	25.2	25.3	26.2	27.0	28.9
Gross Total	72.0	77.2	76.2	76.6	77.0	79.7
Contingent spend RMR & DECC projects		5.0				
		82.2				

1.3. As described in this Forward Work Programme, there are some very substantial projects planned for 2012-13. These include a major programme of work to enhance competition and improve consumer confidence in the retail market (RMR), and changes resulting from implementation of the Government's fundamental reform of the electricity market. The period will also include delivery or development work on three major price control reviews under the new RIIO price control approach.

Cost control regime

1.4. 2009-10 was the last year of Ofgem's first five year cost control regime. We saved a total of £11.9 million over the five year period.

1.5. GEMA has determined that Ofgem should operate a further five year cost control regime running from 2010-11 to 2014-15. GEMA also determined that the regime should continue on the basis of RPI-3 per cent with a maximum year-end carryover of any savings of £5 million. We anticipate savings of at least £12.5 million from this

regime. In 2012-13 budgeted gross expenditure of £82.2m exceeds the adjusted budget ceiling by £2.3 million and this will be offset by agreed carryover savings brought forward.

Figure 2: Ofgem's RPI-3 per cent Calculation

£m Rate Applied	2010-11 2.4%	2011-12 4.8%	2012-13 4.8%	2013-14 2.5%	2014- 15 2.5%
Baseline	£81.5	£81.0	£73.5	£79.9	£79.4
Adjustment for: Smart Meters	-	(£9.6)	-	-	-
Offshore	-	£1.0	-	-	-
EMR	-	-	0.6	-	-
DECC projects	-	-	4.5	-	-
RPI	£2.0	£3.4	£3.8	£2.0	£2.0
Baseline +RPI	£83.5	£75.8	£82.4	£81.9	£81.4
Less X (3%)	(£2.5)	(£2.3)	(£2.5)	(£2.5)	(£2.4)
Budget Ceiling	£81.0	£73.5	£79.9	£79.4	£79.0

1.6. RPI was determined as 2.4 per cent for 2010-11 and 4.8 per cent for both 2011-12 and 2012-13. RPI has been estimated at 2.5 per cent for later years and will be adjusted to the prevailing (December) rates.

Appendix - Feedback Questionnaire

1.1. Ofgem considers that consultation is at the heart of good policy development. We are keen to consider any comments or complaints about the manner in which this consultation has been conducted. In any case we would be keen to get your answers to the following questions:

1. Do you have any comments about the overall process, which was adopted for this consultation?
2. Do you have any comments about the overall tone and content of the report?
3. Was the report easy to read and understand, could it have been better written?
4. To what extent did the report's conclusions provide a balanced view?
5. To what extent did the report make reasoned recommendations for improvement?
6. Please add any further comments?

1.2. Please send your comments to:

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