Minutes of a Meeting of the Gas and Electricity Markets Authority

Thursday, 8 May 2014 at 8.15 am

Cardiff

Introductory remarks by the Chairman

1. The Chairman noted that there were no apologies for absence. Declarations of interest were recorded from a Member whose institution was in receipt of some funding from the energy industry; and from another Member who had an independent role on a Committee advising a Bank on the protection of customers’ interests in respect of two investment funds.

2. The Authority offered their congratulations on the appointment of Jim Keohane to the Board of the recently established Low Carbon Company as an independent Non-Executive Director and noted the main roles of the Company in respect of aspects of DECC’s EMR plans.

3. The Authority also welcomed the recent appointment of Andrew Wright as Group Finance Director from 22 April, thanking him again for his successful period as interim CEO over the past 10 months.

4. The Dinner with the Minister and a range of senior-level energy interests in Wales, hosted by the Authority the previous evening, had been useful. There was a wish for there to be more contacts with the Welsh Government at a number of levels on matters of mutual interest on energy and its regulation. These points would be followed up accordingly.

5. The Chairman briefed the Authority on a range of points from his recent visit to Australia, including regulatory developments on the handling of switching, smart metering and tariff matters. A number of the points raised by the Chairman in his regular contacts with DECC at senior level were also explained and noted.

6. An external study was in progress on Ofgem’s communications activities. The Chairman noted that the consultant would be pleased to talk to NEDs during the process of gathering views for his analysis. It was hoped that he could attend the June meeting as an observer.

Minutes of the Authority Meeting held in April 2014

7. The minutes of the April meeting of the Authority were agreed as drafted.
Reports from the Chief Executive and Senior Partners, Group Finance Director and Managing Director/E-Serve

8. The Chief Executive in his presentation to the Authority addressed two key issues. The first included the main findings of a recent externally commissioned study on staff pay and conditions in Ofgem, dealing with the recent and positive responses from the staff survey, staff turnover data, pay benchmarks and comparators, and issues on pay flexibility. The second issue noted the plans for addressing strategy development and its timing, with planned discussions among the Senior Management Team, and the plans for the Authority Awayday in July.

9. E-Serve’s monthly report provided a brief on the main business areas for E-Serve and the Information Management and Technology Group. On renewable electricity, the position on potential legal matters arising from certain FIT accreditations was noted; and the work in progress with Markets Division in assessing EMR activities to be performed by E-Serve, and with DECC and the Low Carbon Contracts Company.

10. On offshore issues, discussions were continuing with the developers on the completion of the Thanet project under Tender Round 1. Independent studies of TR1 had been completed on the OFTO model and its direct cost savings, as compared to merchant or price control approaches. These had indicated savings of £200-400m on a total lifetime OFTO income of the order of £1.5bn, due mainly to efficient operating strategies from increased competition, as well as more efficient risk allocation. These analyses would shortly be published. In respect of certification, recent contacts with DECC and others were noted in respect of the unbundling requirements of EU legislation.

11. The Authority noted that the Non-Domestic RHI scheme had been running for two years with the approval of some 4000 applications during that period, and with annual payments of about £60m in 2013/4. Audits of non-compliant applications – largely due to incorrect records or metering errors though with minimal financial impact – were being examined with DECC. The Domestic RHI scheme had been launched on 9 April with over 100 enquiries on the first day of operation and accreditations across all four eligible technologies. Anticipated accreditations for the first year of the scheme are 50,000. Feedback on the website and the guidance material had been positive from users and social websites. Discussions were progressing with DECC on certain eligibility criteria.

12. On energy efficiency and social programmes. The Authority noted that the DECC consultation on changes to ECO legislation had recently closed, dealing with proposed reforms and their indicated savings. Ofgem had commented on how the suggested changes could be implemented under E-Serve’s administration of the Scheme. Meanwhile, activity on the ECO
scheme continued at a high rate with nearly 100,000 measures notified in April. Work was also in progress to resolve the decision-making framework for certain cavity insulation measures whose agreement and consequently funding currently on hold. On the planned Government Electricity Rebates, DECC were soon to consult on the proposed implementing measures, and preparations were in hand including on monitoring and compliance with the proposed new licence conditions.

13. On the MoU with DECC, detailed guidelines for financial engagement and the change control framework were now in place, and funding decisions for 2014/15 were well advanced. An audit of E-Serve’s capability had shown further improvements across the board, with some proposals for internal system changes suggested.

14. **Sustainability Division’s report** first briefed the Authority on the plans to publish a final decision on enhancing consumer protection in the green and renewable tariffs market. These were aimed at improving transparency, improving evidence of supply and the creation of additional environmental benefits. This work had followed the Ofgem Green Tariff Guidelines of 2009 and had been based on consumer research and the need seen for a mandatory approach to ensure consistency of approach for these kinds of tariff.

15. On HR matters, Ofgem’s Single Equality scheme had been published in May 2013 setting out the Ofgem approach and action plan, as required under the Equality Act 2010. All actions were now complete and the Authority noted a separate information paper on both the action plan and its achievements on awareness, training and induction, and compliance measures and processes across all policies.

16. It was understood that DECC would soon be publishing their Fuel Poverty Strategy. This was expected to confirm a continuing commitment to supplier-led delivery of energy efficiency measures and the Warm Homes Discount, with increased data-sharing to improve knowledge about households in fuel poverty. The Authority would be briefed further for its next meeting.

17. **Market Division’s report** covered its monthly sets of data on key energy market developments. NEDs had been consulted on the scope and detail of further reports and views were welcomed.

18. On the RMR measures, the large energy suppliers were all now compliant with the “clearer” reforms introduced at the end of March. Ofgem had recently announced the “Be an Energy Shopper campaign” which had received positive reactions, judged by press comments and website interest. A request had been received from one supplier seeking
derogation from the current 4 tariff licence provisions. The request was being examined and would be subject to consultation.

19. On EMR, work continued to progress with DECC on the roles envisaged for Ofgem though some additional proposals were under examination which would need to be resolved before the planned “go-live” date which DECC had in mind.

20. Progress was being made in settling the methodologies to underpin new mid-decade balancing services. Consideration of volume aspects were advanced; and discussions would continue on procurement matters.

21. Some aspects of REMIT – including the provisions for market participants to register with Ofgem – would be entering into force on July, and DECC were considering powers in respect of non-compliance. Consideration was also being given by DECC to the need for criminal sanctions on insider dealing and market manipulation, plus enforcement powers, on which, it was understood, the Department would soon consult.

22. Finally, the Authority noted that the NAO were working on a report on balancing services, at the suggestion of the ECC Select Committee, setting out a guide to these services, their costs and the processes for managing constraints.

23. Distribution Division’s briefing updated the Authority on progress in analysing the revised and resubmitted business plans of distribution companies under RIIO- ED1. A meeting had been planned that month of the price control Committee of the Authority with the companies concerned, this providing an opportunity to probe them on their revisions as part of the process of reaching final proposed settlements, in due course.

24. The Authority noted the growing interest in the potential for distribution companies to undertake anticipatory investment. A useful high-level workshop had taken place involving the main governmental and regulatory players and its outcomes and follow-up were reported - including issues raised by Ofgem on the present structures for dealing with requests for investing ahead, and the importance of evidence of efficiency and customer benefit.

25. The Authority was presented with the results of the recent round of innovation competitions, following screening of applications for funding under the Network Innovation Competitions and the Low Carbon Network Fund. Short-listed projects would soon be announced. Those through this stage were now eligible to move to full submission by late July when an expert Panel would evaluate the proposals, leading to recommendations
on awards and funding. The Authority would be further briefed on the results and suitable publicity plans.

26. **Transmission Division** reported on Ofgem’s work on the revised and increased costs of the planned Beauly-Denny transmission line. There had been a public enquiry about the proposed plans; and the subsequent imposition of planning controls had led to both delays and rising costs. A request for additional funding from the joint project partner, SSE, been approved in 2011. A paper would now come forward to the Authority at its next meeting analysing the case presented by Scottish Power for extra funding under the same TIRG scheme.

27. ACER had published a consultation paper the previous month with its views and proposals for European regulation of energy markets to 2025. There were three key proposals for regulatory action:

- the further development of gas and electricity market models, with the flexibility needed to accommodate renewable generation;
- a review of governance and regulation of those seen as important in the delivery European energy market regulation – such as the European networks of gas and electricity transmission operators, and the power exchanges;
- the proposals for 24 hour customer switching by 2025, with framework for demand response and a review of distribution companies’ roles.

The Authority noted that ACER planned to publish its conclusions in September.

28. On interconnectors, it was noted that final investment decisions by National Grid on the UK-Belgium interconnector would be taken in late Autumn. Work was progressing on cap and floor proposals as discussed at the previous Authority meeting.

29. The **Group Finance Director** led the Authority in expressing thanks to Paul Heseltine, as Leader of the Finance Team, for the lengthy and productive period during which he had lead on all finance and audit matters, following the departure of the former Finance Director in 2012. The monthly report covered the full year 2013/14 budgetary summary and projected outcome, subject to NAO audit, and the main factors underlying the outcome figures were explained. A breakdown of the 2014/15 Corporate Budget was provided dealing with estimates for licence fee costs and income and other projected receipts; and E-Serve costs and income licence fee costs. The assumptions underpinning the figuring were noted. A breakdown was also provided on staff headcount planned for 2014/15, and vacancy levels compared to plan.
30. The Authority noted the major projects portfolio summary, providing assurance reports and delivery confidence. The Group Finance Director also set out his broad plans for the months ahead, including the high priority work priority on overall future strategy; embedding risk and audit factors; activity based costings; resource allocation; future cost controls following the final year of the RPI-3 formula; modelling and its use by Ofgem; and aspects of knowledge management across the organisation.

**Strategy and Policy Statement**

31. At this item, the Authority reviewed the current draft of a Strategy and Policy Statement, now in internal consultation, to be published after the Summer by DECC setting out the Government’s strategic priorities for energy policy as provided by the Energy Act 2013. This also covered Ofgem’s suggested role in contributing to and delivering policies and outcomes. A number of points were proposed and others made on the draft as it now stood, and it was agreed that these should be pursued with DECC in correspondence.

**Capacity Assessment**

32. The Authority resumed its discussions at the April meeting on the report to be made to the Secretary of State on electricity capacity margins, with a planned date of publication of late June. The Authority had decided to continue to make use of the scenarios for the coming five years on the assessments made by National Grid. It was now provided with further information on the sensitivity analyses and considered initial drafts of the key messages in the report.

**Memoranda of Understanding**

33. The Authority had before it drafts of three Memoranda of Understanding, designed to strengthen its relations with its main partners, and providing accountable bases for joint work. These were as follows:

- The arrangements planned for funding and resourcing joint working with the UK’s economic regulators through the UK Regulators’ Network (UKRN);
- An MOU governing the working links with the Competition and Markets Authority which had taken over responsibilities from OFT and the Competition Commission as from April 2014, and with new powers under the Enterprise and Regulatory Reform Act 2013;
- A proposed MOU with the Citizen’s Advice Services – Citizens Advice and the Scottish Association of Citizens Advice Bureaux - given that the functions of Consumer Futures were being transferred to these bodies though with responsibilities unchanged.
The Authority agreed that it was important to work cooperatively the CMA and other economic regulators represented within the new UKRN group. The productive relationship with the Consumer Focus should be maintained as the new administrative arrangements came into effect, given that the new bodies would be representing the views of consumers, investigating consumer complaints and sharing views to help facilitate regulatory and enforcement activities. The Authority accordingly approved the three draft MoUs, asking the Executive to take these forward, dealing bilaterally as necessary with any minor drafting points.

Audit Committee

The Chair of the Audit Committee explained that following revisions to the Corporate Governance Code in central Government, public sector Boards were now being tasked to set their organisations’ risk frameworks, including risk appetite, and for ensuring that appropriate controls were in place on risk management. The Audit Committee had considered this guidance and had also taken into account existing HMT guidance - this proposing that Audit Committees be changed to Audit and Risk Assurance Committees with a more explicit responsibility for risk-related matters.

Accordingly, the Committee were now proposing new terms of reference and designation for the Committee. These new Terms of Reference had been approved by SMT and the changes now better reflected both central advice and would provide support to the Authority’s work and accountabilities in relation to strategic risk management. The Authority approved the text, with the addition of the membership of the Group Finance Director.

Fast and reliable switching

At this item, the Authority continued the discussion at its April meeting on potential reforms to supplier switching; and was briefed further on aspects of the benefits and timing issues, and the steps for presenting any changes. The Authority recognised that switching - and its ease, speed and reliability - formed a significant part of consumers’ experience of retail energy markets. Current processes were slow (about 5 weeks, on average); they lacked efficiency for all, since different processes existed for gas and electricity; they were dependent on IT systems designed in the late 1990s and much-amended processes; and there were resultant reliability problems, with delays in consumer billing, some erroneous transfers and a number of abandoned switches.

Given these difficulties and their impact on consumer engagement, and the potential for supporting improved retail market competition, the Authority agreed there must be a comprehensive overhaul and re-engineering of the current processes – which had been in existence since
the late 1990s. The ambition, ultimately, should be the delivery of a reliable and next day switching platform. HMG were supportive and as were ACER, supported by the Council of European Energy Regulators.

39. The Authority recognised that there were a number of different approaches and timeframes for delivering this ambition, and agreed that the consultation should be used to take a sounding on the best way forward. It was noted that Ofgem was making changes to require reliable 3 week switching by Summer 2014, and that the industry was working on changes to halve switching times by the end of the year. There were therefore timing considerations, the link to the roll out of smart metering systems, the need to allow IT system re-development, cost and cost/benefit considerations, and the models for creating ideally a new and centralised switching platform and its control and governance.

40. The Authority agreed that, consistent with its vision for smarter markets, and in line with consumers’ expectations from energy markets, there should be an early consultation on the options for next day switching, together with a consultation seeking views on how reforms could be implemented quickly. It looked forward to further debate on the results, noting the importance and potential benefits of these proposals, and the value of fully communicating these plans.

**Annual Report and Accounts 2013/14**

41. The Authority considered a note on and draft of the draft Annual Report and Accounts 2013/14. This document was still subject to NAO review, and was due to be laid before Parliament in late June. The Audit Committee had seen the report and some drafting changes had been incorporated. The Chairman’s Forward and Chief Executive’s introduction would be prepared shortly, subject to Authority approval of the emerging draft.

42. The Authority approved the current of the draft report, Members agreeing to submit any final drafting comments quickly. The Chairman was authorised to agree the final version of the text in liaison with the Chair of the Audit Committee.

**Reviewing competition in electricity connectors**

43. A note for the Authority explained Ofgem’s plans to start a review of competition in the market for new connections to the electricity distribution networks. The background to the issues, including measures to improve competition introduced during the DPCR5 price control review, was noted. The outcome of the competition tests required of DNOs to end 2013 were explained, and the variability of these. Ofgem had already announced that it would assess the market; and the plan now was to
make an announcement of the review in June, gather and analyse the evidence, and present this to the Authority at the end of 2014 with recommendations.

44. The Authority asked to be kept in touch closely with the exercise, noting the importance of effective and timely connections, recalling the problems which some developers and businesses were reporting, though the improvements being achieved by some DNOs in some areas.

Enforcement cases

45. The Authority reviewed its monthly schedule of current enforcement cases and the progress being made. The cases now in consideration under the settlement procedures were noted, as well as recent determinations made.

Other business and dates of next meetings

46. There was no other business. The Chairman noted the plans for forthcoming meetings as follows:

- The next Authority meeting would be at **8.15 am on Thursday, 12 June**;
- There was possibly a need for a conference by telephone link on the potential market investigation reference, in the light of the June meeting and consultation responses. If necessary, this would be at **9.00 am on Thursday 26 June**;
- The Authority Awayday would be on **Wednesday, 9 July** – starting with a session, involving first NEDs alone at **8.15 am**, to discuss performance evaluation and governance matters. The reminder of the day would be devoted to strategy themes;
- The Authority would meet on **Thursday, 10 July at 8.15 am**.

Those present

David Gray (Chairman)
Dermot Nolan (Chief Executive)
David Fisk
Paul Grout
David Harker
Sarah Harrison
John Howard
Jim Keohane
Keith Lough
Andrew Wright
Those attending

Rachel Fletcher
Hannah Nixon
Bob Hull
Martin Crouch

Others present or attending via audio link (*)

Paul Heseltine (Annual Report/FIN report)*
Patricia Ochoa (Capacity Assessment)
Philippa Pickford ("")
Andy MacFaul (SPS)
Carola Geist-Divver ("")*
Cecelia Parker Aranha ("")*
Victoria Ellis (MoUs)*
Mark Wagstaff ("")*
Marcus Clements ("")*
Rob Church (Next Day switching)
Grant McEachran ("")*
Andrew Wallace ("")*

David Ashbourne (Legal Adviser to the Authority)
Tony Burne (Secretary to the Authority)