

**ofgem**

Making a positive difference  
for energy consumers



**2019-20**

Office of Gas and Electricity Markets (Ofgem)  
**Annual Report and Accounts**





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# 2019-20

Office of Gas and Electricity Markets (Ofgem)  
**Annual Report and Accounts**

(For the year ended 31 March 2020)

Accounts presented to the House of Commons pursuant to section 6(4) of the Government Resources and Accounts Act 2000

Annual Report presented to the House of Commons by Command of her Majesty

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# About us

**Ofgem is Great Britain's independent energy regulator.**

We work to protect consumers, especially vulnerable people, by ensuring they are treated fairly and benefit from a cleaner, greener environment.

In order to do this our strategic vision commits us to:

- Protect consumers, especially the vulnerable, by stamping out sharp practice and ensuring fair treatment.
- Facilitate decarbonisation efforts to deliver a net zero economy at the lowest cost to consumers
- Enable competition and innovation, which drive down prices and result in new products and services

# Chair's foreword

## Martin Cave

The past twelve months have been exceptionally busy for the energy sector. No more so than recently as we have turned our attention to working closely with the sector and with our partners in government to ensure that consumers are protected through the Coronavirus (Covid-19) crisis. I would like to pass on my thanks for the way in which both staff at Ofgem and all those working across the sector, especially the engineers and other frontline staff, are rising to this challenge on behalf of the homes and businesses that rely on energy as an essential service during this difficult period.

Whilst the Covid-19 crisis has been our priority for the last few months, we look forward to supporting the recovery by returning our focus to the enduring challenges facing the energy sector. We set out our strategic approach to these challenges last July in our Strategic Narrative, covering the period 2019 to 2023. It set out Ofgem's three strategic priorities, putting decarbonisation on a level footing with protecting consumers, and enabling competition and innovation; it also set out our vision for a more agile organisation to deliver on these priorities.

I was delighted in February when Jonathan Brearley started his five-year as our new Chief Executive Officer (CEO), to guide us through the next five years by spearheading our immediate priority of protecting consumers today and helping the sector to build a low carbon energy system for future generations.

In his short time at the helm, Jonathan has already set out an ambitious programme, not just to ensure that Ofgem plays a full role in paving the way for the energy sector to decarbonise at the lowest cost to consumers, but also in modernising and improving our own ways of working as an organisation.

I am also delighted to welcome Myriam Madden and Barry Panayi to the Ofgem Board, both of whom are already proving to be invaluable additions. We are very pleased to have them as colleagues.

I am confident that this new leadership, at both board and executive level, will equip Ofgem well to deliver the outcomes we seek to achieve for consumers in this unprecedented time. In addition to ensuring consumers get good value and fair treatment from energy suppliers, we all share a determination to demonstrate how independent regulation can help tackle climate change, and to do so in a spirit of co-ordination and co-operation, the value of which has been clearly seen through the Covid-19 crisis.

I would also like to take this opportunity to thank Dermot Nolan on behalf of the board for the enormous contribution he made as our Chief Executive.

In the last year, Keith Lough also stepped down from the Board. In his seven years as a member of the Board, and as Chair of our Audit and Risk Assurance Committee, Keith made a tremendous contribution to the organisation. We thank him for this and wish him well for the future. I look forward to working with Ofgem colleagues, government, the energy sector and energy customers on the important challenges we face today and in the future.

*Martin Cave*

**Martin Cave**

Chair



# Chief Executive Officer's Report

## Jonathan Brearley

In February I started my five-year term as Ofgem Chief Executive. It is a huge privilege to be taking up the role, and a huge responsibility too, particularly at this critical time.

Over the past few months we have all seen the widespread impact that coronavirus is having on our lives and those around us. I would like to once again thank all those working in Ofgem and across the industry to respond to the crisis at this difficult time.

We have been working closely and collaboratively with government, the energy industry, consumer bodies and other stakeholders to protect consumers throughout this period. This has involved reprioritising our own work programme and working with industry to ensure they can focus on protecting customers, keeping staff safe and maintaining our world-class security and reliability of energy supplies.

Our principal objective – both in responding to coronavirus and in our wider work – remains the same: to protect the interests of consumers today and in the future.

There are a number of key actions we have taken to achieve this over the last year:

### Facilitating net zero at lowest cost to consumers:

Protecting consumers includes helping to hit the net zero target. On my first day as CEO we published our first ever Decarbonisation Action Plan. It sets out the steps we are taking to help the energy sector deliver net zero and fairly spread the cost of a low carbon energy system between today's and tomorrow's consumers.

Over the last year, our delivery of renewable energy schemes on behalf of our partners in government, worth over £9bn annually, has also continued to make a significant contribution to the decarbonisation of energy, as well as to the cost of energy for some of the most vulnerable.

### Maintaining security of supply:

Maintaining the security and reliability of our energy supply is fundamental for consumers. In August 2019, a power outage caused interruptions to over 1 million consumers' electricity supply. We used our powers to establish the circumstances and causes of the outage and the lessons that can be learned to improve the resilience of Great Britain's energy network.

To meet the demands of the future energy system, we have continued to develop reforms to electricity network charging so that networks are used efficiently and flexibly and allow consumers to benefit from new technologies and services. This year we have also confirmed the framework we will use to set the next price control for Great Britain's electricity distribution networks, as well as the methodology for calculating the next round of network price controls for the transmission and gas distribution networks. Together, these will enable network companies to continue to operate a safe and resilient network and help deliver a net zero economy at the lowest cost to consumers.

### Protecting consumers:

Of course, protecting consumers by stamping out sharp practice and ensuring fair treatment, particularly for those in vulnerable situations, remains core to Ofgem's role. This year we published our updated Consumer Vulnerability Strategy, which sets out our priorities to ensure vulnerable consumers are supported and receive fair outcomes as the market continues to evolve.

We have also introduced automatic compensation for consumers who experience problems when switching supplier, brought in tough new entry tests for suppliers entering the market, and set out proposals for financial checks and tests for existing suppliers to drive up customer service standards and reduce the risk of supplier failure.



Where suppliers have ceased to trade, we have taken swift action to protect their customers and transfer them to a new supplier. And where energy companies have failed their customers, we have taken robust and decisive action – securing over £60 million in fines and redress for consumers.

Our ability to do any of this work depends on the efficiency, effectiveness and resilience of our systems, processes, resources and, most of all, our people. I am very proud to lead such a talented and committed group of colleagues. For them – and for the consumers we serve – I am determined to make Ofgem the most effective organisation it can be. There are a number of areas in which we must improve, not least in keeping apace with a sector that is changing at an incredible speed and ensuring that our internal systems and process are as robust as they can be. As Chief Executive, I am determined that we will do so.

As I look back over the last year, I must pay tribute to my predecessor Dermot Nolan who left Ofgem after six years as Chief Executive. He made an enormous contribution to Ofgem's work, particularly in ensuring that Ofgem was doing everything within our powers to support vulnerable consumers.

This year we have also said goodbye to our Chief Operating Officer Sarah Cox and our Chief Economist Joe Perkins. We thank them both for their outstanding service and wish them well for the future. We have been pleased to welcome Neil Kenward to Ofgem, as our new Director of Strategy and Decarbonisation.

The current crisis reminds us not just how fundamental the energy industry is to the welfare of customers today, but also its importance to the economic and environmental future of the UK, particularly as the country recovers from the coronavirus outbreak. I look forward to working with you all in the coming months and years on the incredible opportunities and challenges ahead of us.



**Jonathan Brearley**  
Chief Executive



# Performance Report

## Overview

The purpose of our performance report is to describe the work we undertook during 2019-20 towards meeting our objectives, along with our strategic approach and the principal risks that we have faced.

As the independent energy regulator of Great Britain, our priorities are defined by our core objective to protect the interests of current and future energy consumers. This shapes the work that we do and helps consumers benefit from:

- **Lower bills**
- **Lower environmental impacts**
- **Improved reliability and safety**
- **Better quality of service**
- **Better social outcomes**

During 2019-20, we focused our work around four key priorities that deliver these positive outcomes for consumers. Our key priorities were:

- **Making retail markets work for all**
- **Enabling future markets and system arrangements**
- **Network preparedness and performance**
- **Excellence in our statutory and core functions**

In addition to these priorities, we had two further overarching priority in 2019-20. Firstly, we responded to the United Kingdom's (UK) planned withdrawal from the European Union (EU), with the aim of ensuring that our regulatory framework would be effective in a range of potential EU Exit scenarios. Secondly, we focused, and continue to focus on ensuring that the energy industry could effectively respond to the Covid-19 crisis. To do this, we worked collaboratively with government, the energy industry, consumer organisations and other stakeholders, to protect consumers, especially the vulnerable, and to maintain Britain's supply of electricity and gas.

### Some of our key achievements and areas of progress during the year include:

- Continuing to **protect of 11 million consumers** with the default tariff price cap (page 14), saving families around **£75-£100** on dual fuel bills, in 2019, totalling around **£1 billion**
- Securing around **£60 million** through our enforcement activity, including our first ever penalty under the REMIT wholesale market rules, and a **record £44 million** from Cadent for leaving residents in high-rise tower blocks without gas
- Continuing to ensure that customers of failed suppliers had continuity of energy supply through nine **Supplier of Last Resort** processes (page 20), which working to improve suppliers' financial resilience and service quality through our supplier licensing review
- Publishing our **2025 Consumer Vulnerability Strategy**, with an aim to introduce new rules to help those at risk of self-disconnection (page 11)
- Assisting 85 different organisations to navigate the regulatory framework for the energy sector through our **Innovation Link service**, so that they could trial new products, services and business models (page 13)
- Confirming our approach to calculating the next round of network price controls, which should **save consumers £6 billion** over the course of RII0-2 (page 18)
- Appointing three new bidders under our offshore transmission owners regime, which will result in around **£1.2 million** investment and **1.5 Gigawatts** in connected, renewable electricity generation
- Finalising a decision on our targeted charging review, which means the cost of maintaining the electricity grid will be spread more fairly and consumers will save **£300 million**, from 2021.
- Processing over **13,000 accreditations** for our Domestic Renewable Heat Incentive scheme and **1,299** for the non-domestic scheme, along with over **250,000** Energy Company measure (page 22).

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We also launched our Smart Export Guarantee scheme, and through our assurance work, we prevented over **£600 million** of errors in scheme applications.

We published our **Strategic Narrative** in July 2019, identifying Ofgem's strategic priorities as: **protecting consumers; decarbonising at lowest cost;** and to help ensure effective delivery of these, **enabling competition and innovation**. These priorities are already driving our work, as set out for example in Ofgem's **Decarbonisation Action Plan**, which was published in February this year.

As part of our work towards the above consumer outcomes and key work priorities, we continued to monitor and mitigate risk to the delivery of our strategic and operational objectives. During a year in which Ofgem undertook an internal structure reorganisation, we saw concerted strains on our internal control mechanisms, which we are committed to improving. Further details on our risk management during the year can be found on page 42.

Our Key Performance Indicators (KPIs) can be found in Appendix I (see page 103).

# Chapter 1: Making retail markets work for all

## Our aim

Consumers engage with the energy system first and foremost through the retail market. Our aim is for the market to deliver good outcomes for all consumers – whether or not they engage to make active decisions to change their supplier or tariff. In practical terms, this means delivering a fair, functioning market, and driving significant improvements in protections for consumers.

There were two aspects of our work to making retail markets work for all, during 2019-20:

### **A. Improving current licensing arrangements to protect consumers and ensure that regulatory burdens are proportionate**

#### Supplier licensing review

In June 2018, we announced our intention to review the energy supplier licensing arrangements to ensure appropriate protections are in place to minimise the likelihood and impact of disorderly supplier market exits and poor customer service. The Supplier Licensing Review (SLR) covers conditions for entering the market, ongoing requirements and exit arrangements. We consulted on changes to the licensing requirements for suppliers in the initial phase of the review, which was completed in 2019.

This resulted in new entry arrangements for energy suppliers coming into effect in July 2019, through the creation of new Gas and Electricity Applications Regulations. The new arrangements include enhanced requirements on new entrants to demonstrate that they can resource their plans to enter the market and prove that they understand the regulatory arrangements and their obligations. The new arrangements also include a strengthened ‘fit and proper’ test for licence applicants.

We have continued our work on ongoing and exit arrangements throughout the year, developing and consulting on a package of proposals intended to raise ongoing standards around financial resilience and

customer service in the supplier market and to review our exit arrangements to ensure that they work in the interests of energy consumers. These proposals aim to ensure that suppliers have effective risk management processes in place; maintain appropriate governance and increased accountability and increase Ofgem’s oversight of the market arrangements.

We expect to progress to statutory consultation to consider a comprehensive package of measures to benefit customers by raising standards in these areas.<sup>1</sup> We had planned to publish this consultation in March 2020 but it has been delayed as a result of Covid-19. We will aim to implement new arrangements quickly where we can and where possible, for new obligations and protections to be in place for winter this year, including a new high-level principle to drive suppliers towards taking action that mitigates the extent of costs to be mutualised in the event of failure. We will keep under review the timing of our further work on cost mutualisation protection proposals, and what additional measures may be appropriate to build on this proposed new high-level principle.

#### Microbusiness and the energy market

In May 2019, we announced a strategic review of the microbusiness energy market, to better understand and address the issues faced by microbusinesses, so that they are able to access a competitive retail markets and secure adequate levels of protection.

Complexity in the market – with its wide variety of contracts and lack of accessible information about pricing – means some microbusinesses find it hard and costly to engage in the market to find a better deal. Following contributions from stakeholders, we have been developing detailed policy proposals to address the key issues that we identified through the review. We intend to publish a policy consultation on these proposals following the Covid-19 crisis.

### **B. Understanding where consumers’ needs are not being met and developing effective policy solutions to address them**

<sup>1</sup> In light of Covid-19, we have taken the decision to delay the publication of the statutory consultation.

## Vulnerable consumers

Vulnerable consumers can face barriers to accessing an affordable and stable energy supply for a variety of reasons. In October 2019, we published a new Consumer Vulnerability Strategy to replace our 2013 strategy. This strategy will guide our work until 2025. Our aim is that consumers in vulnerable situations do not lose out in the transition to a decarbonised system.

Building on our already extensive work delivered under the 2013 strategy, the new strategy focuses on five areas where, by 2025, we aim to drive strong improvements for consumers in vulnerable situations:

- Improving identification of vulnerability and smart use of data
- Supporting those struggling with their energy bills
- Driving significant improvements in customer service for vulnerable groups
- Encouraging positive and inclusive innovation
- Working with partners to tackle issues that cut across sectors.

Each of these five themes are underpinned by outcomes that we want to see realised throughout the lifespan of the strategy.

## Consumer engagement in the energy market

During the year, we continued to develop initiatives for consumers to access and share their energy data in a safe and convenient way, which will enable new products and services to emerge.

We also continued to use information that we gain from research and trials to improve consumer engagement in the energy market. This included the encouraging results from the latest “collective switch” trials. These trials demonstrated that offering disengaged energy consumers an exclusive offer, via a series of personalised letters highlighting the individuals’ potential savings, significantly increased rates of consumers choosing to switch to a fixed tariff.

We are now conducting research looking at the key role consumers will play in the decarbonisation of the energy system. The majority of consumers will need to change their behaviour in some way in order to deliver net zero, and we are investigating how best this can be achieved.

# Chapter 2: Enabling future markets and system arrangements

## Our aim

During 2019-20, the energy system continued to go through rapid change – from both a planned perspective to achieve carbon reduction and manage increased diversity of energy sources – but also from more innovative forces such as new business models, new technological applications and the increasing digitalisation of consumer data.

As Great Britain's energy regulator, we continued to support and enable innovations that work in the consumer interest, whilst maintaining a focus on fair allocation of costs, consumer protections and system security.

There were four aspects of our work to enabling future markets and system arrangements:

- A. Implementing new systems and rules for a smarter, more flexible energy system
- B. Working with innovators and stakeholders to develop sustainable energy solutions and systems for future consumers
- C. Developing improved network access, charging and system operation arrangements to enable efficient future energy markets
- D. System stability and security

### **A. Implementing new systems and rules for a smarter, more flexible energy system**

## Smart metering

Smart meters are a vital upgrade to our national energy infrastructure, which will support a more flexible and resilient energy system. They are a critical tool in modernising the way we all use energy and aiding the transformation of the retail energy market. Because smart meters give consumers near real time information, they enable consumers to better manage their energy usage and they eliminate estimated billing, meaning consumers will only be billed for the energy they actually use.

Ofgem continues to provide regulatory oversight of the smart meter rollout. Our ongoing aim is to ensure that the rollout results in the best possible outcomes for consumers. We are monitoring supplier compliance with their smart metering licence obligations for both progress in delivering installations and the quality of the experience that they offer their customers.

To date, suppliers have installed 20.6 million smart and advanced meters in domestic and small non-domestic premises. In the last year, industry has been transitioning from installing SMETS1 meters to SMETS2 and over 4.3 million SMETS2 meters have now been installed.

During the year, the Department for Business, Energy & Industrial Strategy (BEIS) consulted on a new policy framework for the smart meter rollout, which would see the rollout continue beyond 2020 and we consulted on a new reporting framework in line with BEIS's proposals. In January, suppliers reported on progress against their rollout plans. The reports reflected the challenge suppliers had faced in transitioning from SMETS1 to SMETS2 meters. Failure by a supplier to achieve its binding annual milestones could result in Ofgem taking enforcement action.

We also continue to regulate the Data Communications Company (the "DCC"), which provides a monopoly licensed service for GB-wide smart metering communications services. We regulate DCC's revenue through an annual ex-post price control, which assesses DCC's performance, and whether its costs in the previous year were economic and efficient. In our 2018-19 price control decision, total costs for RY18/19 (excluding pass-through costs) were £375m. As a result of disallowances and other reductions to DCC's allowed revenues, consumers will benefit from pass through savings of £5.363m. In addition, we have also disallowed a total of £218.4m in forecast internal costs (RY21/22 onwards).

Progress was made on the design of new market-wide settlement reform arrangements, which will build on opportunities provided by the smart meter rollout. These will incentivise electricity suppliers to develop new tariffs and services, which will help consumers to take advantage of times when electricity is cheaper to generate or transport, which should generate savings for both consumers and the electricity system as a whole.

Ofgem has also published a consultation on the draft impact assessment for the implementation of market-wide half-hourly settlement, alongside proposals for the implementation and timetable for its introduction. The published Impact Assessment puts the likely benefit to consumers of the introduction of market-wide half hourly settlement at between £1.6 billion and £4.5 billion over 25 years.

## **B. Working with innovators and stakeholders to develop sustainable energy solutions and systems for future consumers**

### Decarbonisation Action Plan

In February 2020, we published our Decarbonisation Action Plan. The Plan sets out nine actions that will help the energy networks become ready to deliver net zero, support HM Government in tackling the question of how to decarbonise heat and transport and encourage innovation to provide new low carbon products and services for consumers. The plan recognises that there are trade-offs to overcome, such as fairly spreading the cost of a low carbon energy system between consumers now and in the future.

The nine actions are:

1. Build adaptability into our network price controls, to ensure network companies invest efficiently and are able to adapt to changes in technology and infrastructure.
2. Set up a regulatory fund to unlock investment in innovative solutions to tackle climate change.
3. Explore, with government and industry, opportunities for greater coordination to enable rapid expansion of an offshore grid at lowest cost.
4. Harness our existing knowledge and expertise to help government and the industry develop cost-effective and low risk options to decarbonise heating.

5. Continue to review how our energy systems are managed to ensure that they are fit for a net-zero future.
6. Create a more flexible electricity system, to ensure that consumers will benefit from the lowest cost transition to a reliable net-zero system.
7. Develop a regulatory strategy on electric vehicles, to support roll out and maximise the benefits to consumers.
8. Support innovation and experimentation, particularly in the retail market, to create low carbon products and services that will directly benefit consumers.
9. Respond to the need to take big decisions facing a deeply uncertain future by becoming more adaptive in the way we work and in our regulatory approaches.

We had originally planned to carry out these actions over eighteen months, starting in April 2020. Due to the Covid-19 crisis, some actions may now take slightly longer. To provide stakeholders with greater clarity for when we intend to deliver these decarbonisation actions, we will publish an update to our Forward Work Programme in due course.

### Supporting innovation

We have continued to adapt our approach to regulation to better enable the innovation needed to create products and services that help consumers use energy in ways that support decarbonisation.

Through our Innovation Link, we continued to provide our “Fast, Frank Feedback” service, helping innovators to understand whether their idea is possible or not under existing rules and regulations. We have now supported over 350 innovators in the three years the Link has been running. Satisfaction with the Link’s services remains high. Over the past year, we have seen several former clients enter the market and launch innovative new services.

For example, in October 2019, Liberty Global (parent company of Virgin Media) announced a trial project that utilises the existing network infrastructure of Virgin Media to provide on-street electric vehicle charging points.

In addition, UrbanChain began to market software to local authorities and energy suppliers with Energy Company Obligation and Warm Home Discount obligations designed to detect potential and actual fuel poor households in the UK.

In February 2020, we set out our plans to offer an expanded and refreshed “Regulation Sandbox” service. The sandbox allows innovators to trial or launch new products and services without some of the usual energy sector rulebook applying.

Based on our experience of running two previous application rounds, the refreshed sandbox service will be better able to meet its users’ needs. Unlike its predecessor, it will be an on-demand service, available when innovators want it rather than following strict application timetables.

The scope of the sandbox service will incorporate new capabilities in industry codes. Temporary relief will also be available from some of the rules in the Balancing and Settlement Code and the Distribution Connection and Use of System Agreement. In keeping with one-stop-shop principles, we are the single point of entry to all sandbox tools and will coordinate involvement from the code bodies. We also set out our intention to consult shortly on increasing the range of rules that Ofgem can provide relief from – in order to help experimentation, trialling and testing to flourish.

Through our feedback work, we often encounter similar issues facing innovators. In order to be more efficient and so that our service has a greater impact, we developed our “broadcast” service, where we speak to many innovators at once. We also published two new guidance pieces – one explaining the different routes to entering the retail electricity market, and the other, how regulations apply in different scenarios where electricity is sold to electric vehicle users.

Interest remains high in our services for innovators and our experiments in adaptive regulation. In the last year, we shared our insights with 15 regulators from different sectors and jurisdictions. Overall, we have now engaged with 27 bodies from 12 countries, covering five continents.

## Default tariff price cap

Ofgem introduced the default tariff cap on 1 January 2019, protecting over 11 million customers on standard variable, or default tariffs from being overcharged for their energy. We adjust the level of the cap every six months to reflect changes in the underlying costs of supplying energy. In February 2020, we set the level of the cap for the fourth period, which came into effect on 1 April 2020.

The Competition and Markets Authority (CMA) conducted a review of the Prepayment Meter (PPM) cap, which protects customers with prepayment meters, and in July 2019 decided to adopt the majority of the default tariff cap methodology to set the PPM cap.

In October 2019, one component of the cap was contested in a judicial review brought by one of the suppliers. The supplier successfully challenged the allowance in cap for wholesale energy during the first 3 month cap period. The judge required Ofgem to reassess the allowance in the light of the new data available. We are currently consulting on the revised wholesale energy allowance and will make a decision following the consultation in August.

During the year, we also consulted on how to assess whether the domestic retail market is able to deliver effective competition, or whether price protection continues to be required. The Domestic Gas and Electricity (Tariff Cap) Act 2018 requires Ofgem to submit a report and recommendation to the Secretary of State by August 2020, on whether the cap should be extended by a further year.

## Regulatory frameworks

During the year, Ofgem carried out a joint review with BEIS to consider the design of future retail market arrangements, to ensure that it is fit for the future. We published a consultation in July 2019, setting out the key challenges that we need to address and the outcomes we want the retail energy market to deliver, including:

- How the regulatory framework could be changed to better facilitate the launch of innovation products and services, that could support decarbonisation.



- Market distortions, and where implementing reforms could improve the functioning of the sector.
- How the retail market can deliver a good deal for all consumers, including fair prices and good levels of service.

Having carefully considered responses to the consultation, in February 2020, we announced a package of measures designed to promote innovations in the retail energy market. In addition, we stand ready to assist BEIS in developing possible legislative changes that support the needs of tomorrow's consumers and provide flexibility for innovators to develop new business models, products and services.

During the year, we also began consolidating and rationalising the Retail Energy Code, to put in place a third iteration, to be launched alongside the faster switching arrangements in 2021. Excellent progress was made on the Faster and More Reliable Switching Programme which has now entered the testing phase.

### **C. Developing improved network access, charging and system operation arrangements to enable efficient future energy markets**

#### **Networks**

To meet the demands of the future energy system, we continued to develop reforms to our rules, which underpin industry access to electricity networks and the charges levied for using the system through our two closely linked Significant Code Reviews: the Access and Forward-Looking Charges Review and the Targeted Charging Review (TCR).

Working closely with a range of stakeholders, we developed reforms for access to the electricity network and Forward-Looking Charging arrangements. We also published working papers to outline our initial thinking on key options for these reforms, before setting out our shortlisted policy options. We expect to consult on our draft conclusions during 2020-21.

For our Targeted Charging Review, we sought views on proposals that we had refined, before publishing a decision in December 2019. The aims of these reforms are to ensure that residual charges are shared fairly amongst those who use the electricity network and to remove harmful distortions from the network charging regime. Proposed modifications will be assessed between 2020 and 2022.

In May 2019, new gas transmission charging proposals were submitted to Ofgem for consideration by industry, for reforms to reflect the changing use of the network and compliance with EU code harmonisation tariff structures (UNC0678). We then published proposals as part of a consultation that closed in late February 2020. We expect to make a final decision during 2020-21.

#### **Systems**

Following its legal separation from the National Grid in April 2019, the Electricity System Operator (the "ESO") is now responsible for balancing electricity supply and demand in real time, in a manner that avoids fluctuations or disruption of supply.

As part of our oversight role, we consulted on changes to refine the ESO's principles-based incentives framework and published a decision in March 2019. Shortly afterwards, the ESO Performance Panel published its first evaluation for the ESO's performance for the 2018-19 regulatory year. Ofgem also commented on the ESO's draft forward plan for 2020-21, encouraging it to develop a transparent and stretching plan to address stakeholder feedback.

We continued to monitor how distribution network operators actively managed their networks, to allow innovators and flexibility providers to play their role in delivering a more efficient energy system. Our aim is that this will be a key feature of the next electricity distribution network price control (see page 18).

## D. System stability and security

### Withdrawal from the EU

In the lead up to the UK's withdrawal from the EU on 31 January 2020, we worked with HM Government and industry to ensure that the regulatory structure would continue to work effectively after withdrawal and that any exit issues were properly understood and managed appropriately. Some of our key work streams included, and continue to include:

- Consequential changes to energy company licences
- Engaging with code administrators and panels to support their preparations
- Continued compliance with Regulation on Wholesale Energy Markets Integration and Transparency (REMIT) regulations (see page Appendix II)
- Engaging with interconnector operators and our regulatory counterparts
- Advising HM Government on the impact on regulatory Statutory Instruments.

### The Capacity Market

The Capacity Market – part of HM Government's electricity market reform policy – ensures that sufficient electricity capacity is available to meet demand. It is intended to incentivise investment in more sustainable, low carbon electricity capacity at the least cost to consumers, and to ensure that our electricity supply is secure for the future. The Market is governed by the Electricity Capacity Market Regulations 2014 (the "rules"), which Ofgem manages through our rule change process. During the year, we continued our five-year review of the rules to improve the Capacity Market, by making participation simpler for providers, improving competition and liquidity in the mechanism, and for the benefit of consumers. In July 2019, we published a Forward Work Plan on our review and a follow up letter in October on the rule change process, particularly for changes to the governance process, including prequalification, secondary trading and systems development needed from the Delivery Body.

### Electricity system stability

"Black Start" is the process used to recover from an event, which results in the full or partial shutdown of the electricity transmission system. When needed, isolated power stations are "started" individually without an external power supply, and gradually reconnected in order to re-energise the system. Following its submission from the ESO, Ofgem approved the "Black Start" strategy and procurement methodologies in July 2019. The strategy's aim is to ensure that there is an effective system security framework in place for restoring energy supply to homes and businesses in the event of such a total system failure.

### Cyber Security and Resilience

In May 2018, Ofgem and BEIS became the joint Competent Authority under the Networks and Information Systems (NIS) Regulations 2018, which implements the 2016 EU Directive on the security of network and information systems. The goal of the NIS Regulations is to ensure Operators of Essential Services (OES) take appropriate and proportionate technical and organisational measures to manage risks posed to the security of the network and information systems on which their essential service relies, as well as prevent and minimise the impact of incidents. Our role is to monitor OES progress and where necessary through enforcement, ensure compliance with the regulation. As we have built out our team, we have taken on additional responsibilities, including monitoring Cyber aspects of the Smart Energy Code ("SEC") and provide expertise into the RIIO price control team. During this past year, we have engaged in over 100 energy company workshops and published Ofgem NIS Guidance, RIIO-2 Cyber Resilience Guidelines and a NIS Draft Inspection Framework for Downstream Gas and Electricity.

# Chapter 3: Network preparedness and performance

## Our aim

At a time of significant change for regulated networks, our aim has been to ensure network companies deliver system security, innovation and value for money for consumers. We did this through effective administration of existing price controls (RIIO-1), as well as by developing an approach to our new set of price controls (RIIO-2) and introducing more competition in network activities. Together, this can improve outcomes for consumers and deliver a resilient, cost-effective network, fit for the future.

There were two aspects of our work, to achieve the best value for the interest of current and future consumers by using competition to deliver value for money and to help prepare networks for the future.

### A. Using competition to deliver value for money

A significant and rapidly growing share of UK electricity generation is coming from renewables, such as wind and solar power. Integrating these new power sources into the system requires a step change in network investment and a more dynamic approach to the development of the transmission network. We use competition where possible, to minimise costs to consumers.

## Offshore competition

Ofgem runs a competitive tender process for granting offshore transmission operator (“OFTO”) licences.

During the year:

- A transmission licence was granted for the Galloper Wind Farm as part of Tender Round 5.
- A “minded to” Notice for modifications to Walney Extension transmission licence was issued as part of Tender Round 5.
- A preferred bidder was selected during Tender Round 5 for the Rampion Wind Farm Project (the last for that Tender Round).
- Preferred bidders were also selected during Tender Round 6 for the Beatrice and Hornsea Offshore Wind Farm projects.

## Onshore competition

We continued to assess how competition models could be applied to “strategic wider works” project proposals that are submitted to Ofgem, to create additional capacity in the network. These large onshore transmission investment projects are central to the development of our RIIO-2 electricity transmissions price control framework.

During the year:

- We consulted, and published our decisions in May 2020, on the regulatory delivery model and our assessment of capital costs for the Hinkley-Seabank transmission project – proposed by National Grid Electricity Transmission – was published.
- We consulted on our minded-to position to approve a new electricity transmission link to Shetland proposed by Scottish Hydro Electricity Transmission. We also agreed a proposal from Scottish Hydro Electric Powers Distribution to contribute financially towards the Shetland link, if it is built. That contribution would reflect the benefits (for example in terms of security of supply) that Shetland demand consumers would derive from the link.
- We asked the Electricity System Operator (ESO) to deliver detailed proposals, by February 2021, on how to develop and implement ‘early competitions’ to identify network or non-network solutions to issues on the electricity transmission system. This work started in October 2019 and the ESO is due to consult on arrangements in summer 2020.

## B. Preparing networks for the future

### Network price controls

During the year, we continued to work closely with stakeholders to develop our RIIO-2 framework – our next set of network price controls – that will succeed the current RIIO-1 framework, which will end in April 2021 for gas distribution, gas and electricity transmission and in 2023 for electricity distribution. RIIO (Revenue = Incentives + Innovation + Outputs) is Ofgem's performance-based framework to set price controls for companies running the gas and electricity networks. A more detailed explanation of our RIIO frameworks can be found on our website.

Our objective for RIIO-2 is to ensure that these regulated network companies deliver value for money services that both existing and future consumers want, giving due attention to mitigating the impact of networks on the environment, maintaining network resilience, safety and reliability; and designing networks that they can play a full role in addressing consumer vulnerability issues.

We have sought to achieve this objective by:

- Giving consumers a stronger voice in setting outputs, shaping and assessing business plans.
- Allowing network companies to earn returns that are fair and represent good value for consumers, reflecting the risks they face and prevailing market conditions.
- Incentivising network companies to respond in ways that benefit consumers to the risks and opportunities created by potentially dramatic changes in how networks are used.
- Using framework or competition to drive innovation and efficiency.
- Simplifying the price controls by focusing on items of greatest value to consumers.

As well as developing our new price controls for gas and electricity distribution including transmission, we have also been developing separate price controls for the ESO and National Grid Electricity Transmission, with the aim of promoting a whole-system approach to price controls.

During the year, to develop our RIIO-2 price controls, we:

- Published and consulted on sector-specific methodologies (for electricity and gas transmission, and gas distribution, and for the electricity system operator) and tools for cost assessment for the price controls.
- Published the framework for the electricity distribution price controls (ED-2)
- Held cross-sector working group workshops for decarbonisation, customer and social needs, asset management and costs assessment.
- Received initial business plans from network companies, which were reviewed by challenge groups and subject to “calls for evidence” that sought views from stakeholders.
- Received final business plans from network companies, before publishing our initial and final decisions, on how we would apply the RIIO-2 framework to each network.

Moving forward, we plan to publish draft determinations in July 2020 for the next gas distribution, gas and electricity transmission and for the ESO price controls, that are due to start in April 2021. We also plan to set out the detailed methodology in July 2020 for the electricity distribution price control that starts two years later.

## Interconnectors

Increased interconnection will provide increased capacity, flexibility and resilience to our electricity system. Following the establishment of our Cap and Floor regime for new investment in electricity interconnectors, we have continued to work with developers to deliver regulatory approval for new interconnector links as these projects progress through construction and operation.

During the year:

- Following a consultation on our “minded to” position on Nemo Link’s post-construction review for its electricity interconnector, we published a decision, specifying our determined values and setting the final Cap and Floor levels.
- We published a consultation paper on proposed changes to the electricity interconnector licence held by National Grid IFA2, to implement the Cap and Floor regime, between the GB and French transmission systems, jointly developed with Réseau de Transport d’Électricité. A decision is expected in 2020.

## Network security

In line with our Decarbonisation Action Plan, we continued to provide advice to help HM Government decide on future funding models for low carbon sources of power. This includes a regulated asset base (RAB) funding model for nuclear power projects, and potentially other technologies such as carbon capture and storage.

## Responding to network performance issues

Following a major power outage in August 2019 we carried out an investigation to establish the circumstances and causes and the lessons that can be learned to improve the resilience of Great Britain’s energy network. The investigation also looked at the compliance of the licensed parties involved with their licence and code obligations. In January 2020 we set out our key findings, this included that the licensees below did not appear to have met their licence and code requirements and the event highlighted the importance of robust industry compliance processes.

- Hornsea 1 Limited and RWE Generation UK plc have each acknowledged the role they respectively played in contributing to the outage, and agreed to make voluntary payments of £4.5m each to the Energy Industry Voluntary Redress Scheme.
- Eastern Power Networks plc and South Eastern Power Networks plc have each acknowledged a technical breach of their requirements and agreed to make voluntary payments of £1.5m in aggregate to the Energy Industry Voluntary Redress Scheme.

In May 2019, we also concluded our investigation into Cadent Plc’s misreporting and procedural shortcomings in relation to its management of High Rise Multiple Occupancy Buildings on its network. Cadent took steps to investigate and rectify the issues at a cost of £3.6m which they covered in full, and made a payment of £3m into the Energy Saving Trust Voluntary Redress Fund in recognition of its shortcomings.

# Chapter 4: Excellence in statutory and core functions

## Our aim

At a time of significant change and uncertainty, it is imperative that consumers can rely on the regulator to protect their interests and ensure good value and services from the energy market.

To ensure this level of protection is maintained, we remained committed to achieving excellence in the delivery of our core and statutory functions. These functions include market monitoring, compliance, enforcement and delivery of initiatives and schemes in partnership with HM Government.

There were four aspects of our work to ensure excellent across our statutory and core functions:

- A. Ensuring effective licensing and market arrangements
- B. Proactive market monitoring and consumer protection
- C. Effectively delivering renewable energy and social programmes
- D. Enhancing our industry-specialist skills and capabilities.

### A. Ensuring effective licensing and market arrangements

Ofgem's licensing and market arrangements are in place to help ensure that the energy network remains reliable and safe to use, and that customers remain connected to an ever more efficient network, while being protected from poor practices.

As set out in on page 10, we carried out a review of retail supplier licencing arrangements, and brought new entry requirements into effect in July 2019. We also continued to consult on ongoing requirements and exit arrangements, to ensure that suppliers have effective risk management processes in place, maintain appropriate governance arrangements, increase their accountability, maintain market oversight and improve the Supplier of Last Resort (SoLR) experience for affected consumers.

For our wholesale market arrangements, we considered new gas transmission charging proposals from industry and published a responding proposal for comment, to reflect the changing use of the network and compliance with EU code harmonisation tariff structures (see page 16).

We also developed and published contingency arrangements for the REMIT investigations, should the UK leave the EU with no agreed deal. Whilst leaving the EU with an agreement remains HM Government's stated intention, as a responsible regulator, we have planned for all eventualities, including a 'no deal scenario'.

### B. Proactive market monitoring and consumer protection

Through our ongoing monitoring of the retail energy market, our goal is to maintain an evidence-based understanding of market trends and the health of individual retail energy suppliers, so that we are able to respond effectively to protect consumers.

During the year, we remained committed to emphasising to energy companies their duty to put their consumers first – through our engagement and monitoring approach – in line with their regulatory obligations. Our aim was, as always, to see increased awareness of their obligations to consumers, and in their ability to identify risks and manage them effectively. When things go wrong, consumers must be treated with respect, in good time, and where necessary, offered suitable redress. To inform this, we continued to monitor both the wholesale and retail energy markets.

Where energy companies fail to act within their obligations, we carry out compliance casework, which in some cases, required enforcement activity. In 2019-20 we concluded 37 compliance and enforcement cases where money was paid back to customers as refunds and/or compensation, and / or money was paid as a penalty or to the voluntary redress fund. We also issued four Provisional Orders and nine Final Orders in this time period. The consumer benefits of this work was £71 million.

Appendix II sets out the enforcement activity that we carried out in 2019-20, a summary of actions taken as a result of our wholesale and retail market monitoring, and our compliance activity. In line with our statutory reporting obligations, this Appendix includes a summary of final and provisional orders made by the Authority in the 2019-20 reporting year together with a summary of the penalties the Authority imposed during the same period.

We also continued to ensure best value for consumers through the energy networks, including the effective delivery of the four price controls under our RIIO-1 framework. During the year, we received requests for new funding from all six electricity Distribution Network Operators (“DNOs”) during the 2019 “reopener” window covering a range of projects within the electricity distribution price control. Our decisions in October 2019 confirmed that we would allow £64 million of funding for DNOs to invest in physical site security, street works and rail electrification projects, but refuse around £258 million for projects we considered to be poorly justified or provide insufficient value for money for consumers.

### **C. Effectively delivering renewable energy and social programmes**

Ofgem delivers a portfolio of renewable energy schemes and social programmes on behalf of our partners in government. These schemes are worth over £9bn annually and over the last decade have made a significant contribution to the decarbonisation of energy and the cost of heating for some of the most vulnerable. The relationship we have with our government partners is founded on the delivery of good value for taxpayers' money, both in our administration and also ensuring that we protect public funds when we pay scheme participants. It is underpinned by a clear objective to protect the interests of consumers.

Given the scale of this work, we have grown our capacity and capability into a significant dedicated work hub that stretches across both our Glasgow and London offices.

We have worked closely with our government partners to establish our delivery priorities and our risk appetite. This resulted in a set of clear priorities which we worked towards over the last year

These are to:

- Protect the public purse:
  - o Investment in assurance across audit, risk, fraud and compliance
  - o Independently control and assure the landscape we manage.
- Deliver our legislative agenda:
  - o Engage the market and enable access to the schemes we administer
  - o Focus on robust and timely processing of applications.
- Make legally sound decisions:
  - o Apply our risk appetite to protect the public purse in ways which are lawful, but which may be tested.
- Ensure any legislative change is enacted:
  - o Managing any changes to regulation, preparing guidance and engaging our stakeholders
  - o Continuation of all scheme legislative reporting.
- Enable applicants and participants to access the schemes:
  - o Maintaining our systems to enable easy public access
  - o Rewrite two of our key registers.

Whilst we made considerable achievement against these priorities, we also faced considerable budget constraints, which meant that we had to de-prioritise our systems development, stakeholder engagement, and increase some of our processing times. In particular, we focused on the protection of the public purse, introducing a full statistical auditing programme on the renewable heat incentives (RHI) whilst also supporting the Northern Ireland Department of the Economy's work on inspecting RHI sites supported by their scheme.

## Renewable Electricity

The Renewables Obligation (RO) and the Feed-In Tariff (FIT) schemes are now closed to new entrants, but will continue to provide support for eligible renewable electricity over the coming decades.

We continue to administer both schemes, ensuring ongoing compliance, for the accredited generators that make up the equivalent of over 31% of all UK electricity supply in 2018-19. During 2018-19, the combined value of these schemes was £7.4bn.

This was the ninth year of the FIT scheme. The total capacity deployed under the scheme grew from 6.02 gigawatts in year eight to 6.21 gigawatts in year nine, an increase of 3%. Electricity generated by FIT installations totalled 8,454 gigawatt hours in total.

We issued 105.9 million RO certificates based on 79.1 terawatt hours of renewable generation. When combined with the 8.45 terawatt hours generated by FIT installations, this figure rises to 31.8% of the overall.

During 2018-19, 21 suppliers did not meet their obligations, which resulted in a shortfall of £97.5 million in the buy-out fund. This shortfall triggered mutualisation for the second time in the RO scheme's history.

In January 2020, HM Government introduced the Smart Export Guarantee, which ensures obligated suppliers provide generators, of under 5 megawatts, a positive price for the electricity that they export to the grid. Unlike previous electricity support schemes, this is a market-led scheme with Ofgem's role focused on supplier compliance, as such no accreditation information is recorded.

## Renewable Heat Incentive

The Domestic RHI scheme was introduced in 2014 and as of 31 March 2020, we have made 76,000 accreditations since the scheme was launched. Since 2014, the scheme has generated more than 44,544 gigawatt hours of renewable heat.

As of December 2019, more than 19,800 participants were registered on the Non-Domestic RHI scheme, providing over £2.3 billion support for those transferring renewable heat.

Additionally, the Non-Domestic RHI scheme supports the injection of Biogas to grid. Over the last year, this has supported over 90 sites of injecting "green gas". To aid our registration of these sites and ensure that plants only receive support when they are eligible, we launched a "call for evidence" on the commissioning of biogas plants, in order to seek to identify common processes, to aid our registration of these sites and ensure that plants only receive support when they are eligible.

We continued to support the administration of the Northern Ireland RHI scheme, including the inspection programme. In the lead up to the Northern Ireland RHI inquiry report publication in March 2020, we worked closely with the Northern Ireland Government to address the concerns that had been raised through the course of the inquiry and are considering any implications for the future administration of our schemes and for Ofgem more widely.

## Energy Efficiency and Social Programmes

Our administration of the Energy Company Obligation (ECO) continued throughout the year, providing support to vulnerable consumers and helping them to reduce the cost of heating their homes. After the launch of the third phase of this scheme, January 2020 saw a step-change in our delivery, to include a third-party stakeholder. TrustMark – a quality assurance body – will now be delivering compliance oversight of all retrofit measures delivered onto the scheme. We worked closely with TrustMark to ensure that we could rely on its processes in order to assume the consumer protection and quality standards we have introduced as part of our ECO scheme administration.

We have also worked with a panel of experts to assess 48 applications for additional support for innovation measures.

We continue to administer the Warm Home Discount, which provided £140 to each of over 2.2 million vulnerable consumers, in or at risk of fuel poverty. Over its lifetime, the scheme has provided over £2.45 billion of direct support to vulnerable consumers and industry initiatives.



## Assurance

Our E-serve Assurance Hub has now implemented the system of checks and controls known as the “Three Lines of Defence”, with the aim of ensuring our internal processes and decision-making are robust and that our risks are well managed.

During the year, we built our data analytical capability, deploying it to identify trends in non-compliance and to begin to understand the data that we collect from scheme participants more thoroughly. Our goal is for this to assist us separating errors from genuine non-compliance and fraudulent activities.

Over the last year, we conducted over 2500 audits on both scheme participants and also obligated suppliers. With a 20% increase in statistical audits on the domestic RHI and a 50% increase in targeted audits for FIT generators. Additionally, given some delays in the 2018-19 programme of audits this meant that we needed to progress these in parallel with our 2019-20 audits.

We report on the level of error and misrepresentation our administration detects and prevents. Over the last financial year, our work prevented over £601 million of error and detected over £4.4 million, which we can look to address with scheme participants. The largest amount of this comes from the RO (~£0.5 billion) and so prevents this from being passed on to bill payers. This overall error figure is mainly due to robust decisions to reject applications made in our operations hub and action taken by our assurance and compliance hub to correct errors, for example where participants in our schemes make mistakes in submitting data to us.

## Technology

We have commenced work on the re-write of the IT system that underpins our administration of the renewable electricity schemes, which will eventually replace our register, which has now been in place for over ten years. This work has been in close engagement with HM Government's digital strategy team, which aims to produce a more user-centric product. By taking an “Agile” approach to this system's development, we should be able to reuse components designed for this system across other schemes, such as the system underpinning the non-domestic RHI scheme, the rebuild of which we had to de-prioritise in 2019-20.

### **D. Enhancing our industry-specialist skills and capabilities**

During the year, we continued to deploy the expertise of our staff to ensure that our support and delivery services effectively contributed to our policy development. This included advice from legal, economic, engineering, behavioural research, data and cyber security specialist colleagues.

In particular, we continued to deliver quality assurance of business-critical models, impact assessment and evaluation, in line with recommendations in the HM Treasury review of quality assurance of Government analytical models<sup>2</sup> Through this work, we support our policy teams to develop their analytical models and review their cost-benefit analysis and impact assessments.

<sup>2</sup> <https://www.gov.uk/government/publications/review-of-quality-assurance-of-government-models>

## Chapter 5: Our GB stakeholders

Stakeholder engagement remains at the heart of our work so that we consider a broad range of views in our work to regulate the energy system. Due to Covid-19, we reviewed our engagement to reduce burdens on the sector and shift remaining engagement to virtual platforms. The majority of engagement described below took place before the Covid-19 pandemic.

### Consumer and stakeholder engagement

In 2019-20 we have continued to hold events and workshops across Great Britain to speak to different stakeholders as part of our decision making processes. This year we held four energy conferences in Port Talbot, Birmingham, Glasgow and London to consult on our Forward Work Programme and Decarbonisation Action Plan. These were well attended by the energy sector. We also proactively invited those groups that are sometimes under represented at our events such as smaller consumer and charity groups and large Industrial and Commercial customers to ensure they were part of the discussions.

As part of the decarbonisation action plan we invited future energy consumers through a young professional's panel to debate the challenges and trade-offs of decarbonisation in the energy sector. We also partnered with the educational charity 'Inspiring the Future' so that local school children presented at the events on their views on decarbonisation and were part of the table discussions.

We continued our engagement programme for our senior leaders with them visiting stakeholders and consumers across Great Britain. This included visits to rural Northumberland to hear of the challenges in rural fuel poverty. We saw some impressive, innovative projects in energy on Anglesey including the Morlais Marine Demonstration Zone. We've continued to meet regularly with Citizens Advice Scotland and their bureaus to hear directly from consumers about the challenges they are facing and we visited a convenience store in Surrey to discuss the microbusiness review.

As with previous years, the Authority held meetings in Cardiff, Glasgow and for the first time this year in the North East. As well as the board meetings, the members visited a number of local stakeholders to

gain valuable insight into the work being done at community level. In Wales, they visited an innovative energy system solution - Llangattock Local Energy and on the same trip also visited the FREEDOM Hybrid Heating Project in Bridgend and the Penycymoedd Windfarm & Energy Park. In Sunderland, they met consumers who had benefited from energy schemes and saw another heat network in Loch Lomond, Scotland. We also held meetings for government officials and local stakeholders to discuss the local challenges in the energy sector.

This year we have been working with local charities in Glasgow and London through volunteering and fundraising. A number of consumer groups and charities have also presented to our staff about their work with consumers and the challenges they face as well as the successful implementation of Ofgem policies or delivery of environmental and social schemes.

We continue to run a number of working groups to meet key stakeholder groups such as large users and academics. We also speak at a large number of events across the country; keynote speeches from our senior team can be found on our website.

We have held a number of webinars over the year. Since Covid-19, we have significantly increased digital engagement and we will continue to engage virtually with stakeholders across Great Britain trialling new technology to improve interaction and discussions.

### Government engagement

Our work involves regular engagement with government departments and ministers (most notably with BEIS) and we have continued to share our insight and expertise as the energy regulator over the last year. Ofgem is accountable to Parliament, and our external relations team act as a dedicated point of contact for elected representatives across Great Britain. We work to ensure a regular dialogue on Ofgem's action to protect consumers, and the development of our Forward Work Programme. We have contributed written and oral evidence to relevant parliamentary inquiries, provided speakers at cross party groups, as well as holding meetings with individual MPs/MSPs/AMs and their staff on energy issues at a national and constituency level.

# Chapter 6: Consumer Impact Report (CIR)

## Demonstrating the benefits we deliver

As the sector regulator, Ofgem does everything it can to deliver good value for energy consumers and ensure that the energy market works as well as it can for everyone. We are funded by a licence fee that we levy on the energy industry and ultimately, consumers pay for this through their energy bills. Therefore, it is important that we earn consumers' trust by demonstrating the benefits that we bring for the money that they pay. Our third Consumer Impact Report (CIR) for the financial year 2019-20 was published in June 2020.

Our work spans the entire energy system. We consider hundreds of complex issues every year, and our decisions have a major influence on how the energy system works. **We are confident that overall, we deliver real value for energy consumers in Great Britain.**

## Identifying and assessing the benefits we deliver for consumers

We follow a rigorous process to assess the expected net benefits of our major decisions. This follows a framework called Impact Assessment. It uses guidance from HM Treasury to ensure a consistent, high standard of analysis of the expected benefits and costs of our decisions. We aim to work out the net benefit in £ to consumers that the decision could generate compared to the costs of implementing it. However, it is often not possible to do so, and therefore we also consider these consumer benefits in a more qualitative way, looking beyond the financial numbers. This is just as important as the quantified benefits – and a prime example of this is our work for consumers in vulnerable situations, which delivers significant benefits, but they are difficult to quantify.

Another example is our monitoring and compliance work, where the direct benefits of action taken against companies may be modest, but the deterrence effect of our willingness to act is likely to generate considerably greater benefits. The process is not perfect. For example, some of our major decisions will last for years – in a fast moving energy sector, and a changing society, how can we be sure that the benefits we expect today will actually happen? And how can we be sure that decisions we have taken in the past are delivering benefits now? This is a challenge we recognise. That is why we work closely with academic experts and other stakeholders to make sure our assessment processes reflect current best practice. We also intend to conduct post-implementation reviews of some of Ofgem's key regulatory decisions to check that interventions delivered the benefits that were expected.

## How much in £ is expected to be delivered for consumers?

Sometimes our decisions are of major significance following years of work (for example on the future of a network price control) and sometimes they are tweaks to how we already expect the market to operate. As the scale of the impact of our decision-making is lumpy, with the number of major regulatory decisions varying from one year to the next, but the benefits of these decisions are generally long-lasting, we assess the £ benefit of our decisions taken over a multi-year period. In this year's CIR, we assess decisions taken over the three year period from 2017-18 (when we first published the CIR) to 2019-20. We expect the decisions we have taken in these years to deliver on average £3,821.7 million of benefits to consumers. We do not expect these to occur solely within these three years, but will accrue over longer periods of time. Given Ofgem's average costs since 2017-18 of £99.8 million, this gives a benefit:cost ratio of 38.3.

## An overview of the benefits we have delivered

During financial year 2019-20, Ofgem delivered the following quantifiable benefits for consumers.

In the **retail market**, we introduced the second tranche of the Guaranteed Standards of Performance, relating to delayed switches between energy suppliers, responsibility for erroneous switches, and failure to issue a final bill on a timely basis. We expect these standards to act as an incentive to improve suppliers' behaviour and contribute to further increasing consumers' willingness to engage with the market, while encouraging suppliers to improve their systems. We expect the measures will deliver consumer benefits of £63 million over one year along with other non-monetised benefits.

We launched a review of our approach to licensing and regulating suppliers in 2018 to raise standards around financial resilience and customer service. This will help to drive up standards for consumers, and potentially reduce disruptive exits by suppliers. The first stage of our review concluded in July 2019 with reforms to our licence application process, which will help us increase our scrutiny of potential new entrants. All of this helps our Strategic Narrative<sup>3</sup> priority of 'protecting consumers, especially those in vulnerable circumstances, by stamping out sharp practice and ensuring fair treatment', and '**enabling competition and innovation**, which drives down prices and result in new products and services.'

In **networks regulation and the wider energy system**, we disallowed around £5.6m of costs as a result of the price control on the Data and Communication Company (DCC). We reduced the revenue cap and floor on the Nemo Link GB-Belgium interconnector, by reducing consumer exposure to risk and increasing the chances of cap payments throughout the 25-year regulatory regime. In October 2019, we disallowed around £258m of funding requests by electricity distribution network companies for projects that we did not think were properly justified or provided poor value for money.

We suspended the Secure and Promote Market Making Obligation (MMO) which took effect on 18 November 2019 to avoid disproportionate and potentially unfair costs. These measures help our Strategic Narrative priorities of '**protecting consumers**' and '**enabling competition and innovation**'. Our **enforcement and compliance** activities prevent and remedy unlawful or anticompetitive conduct and breaches of licence conditions. We want consumers to benefit from timely resolution of any harm to them from these breaches and an improved supplier-customer relationship. For the enforcement and compliance decisions we took between April 2019 and March 2020, we expect the consumer benefits to be about £71 million.

We also work to address **vulnerable consumers**' needs. We have a statutory duty to consider the needs of certain more vulnerable groups of consumers such as those with disabilities or long-term health conditions, of pensionable age, on low incomes or living in rural areas. We have expanded this to include a wider range of vulnerability, including transient vulnerability, such as job loss, bereavement or short term mental ill health.

We published our new **Consumer Vulnerability Strategy** in 2019 and it sets out our priorities until 2025 to ensure consumers in vulnerable situations are at the heart of our work.

Furthermore, we **administer green energy and social programmes** on behalf of the UK government which tackle fuel poverty in Great Britain and assist consumers in more vulnerable situations. The government extended the Warm Home Discount (WHD) scheme until March 2021 as part of its Fuel Poverty Strategy. The Energy Company Obligation (ECO) scheme will continue until March 2022 and obligates larger suppliers to deliver energy efficiency measures to households in Great Britain. Our work for vulnerable consumers also helps meet our Strategic Narrative priority of 'protecting consumers, especially those in vulnerable circumstances, by stamping out sharp practice and ensuring fair treatment'.

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<sup>3</sup> Ofgem (2019) 'Strategic Narrative' p.8 <https://www.ofgem.gov.uk/system/files/docs/2019/07/our-strategic-narrative-2019-23.pdf>

## Looking to next year

There are three additional areas of our work in 2019-20- 2020-21 that we expect to have a significant positive impact on our work for consumers in future years:

- Work on **networks and the energy system** (Targeted Charging Review, RII02 network price control, and cap and floor regime) that we could include in our assessment of consumer benefits.
- Our February 2020 **Decarbonisation Action Plan**, which sets out the initial action we will take to help achieve net zero greenhouse gas emissions by 2050.
- Our May 2020 **Distributional Impact Framework**, which will help us assess which groups of consumers may or may not benefit from particular decisions that we could take.

These are the main examples and there are likely to be more. We will aim to incorporate these, and any others, in our future assessment of consumer benefits.

# Chapter 7: Sustainability Report

## Highlights:

- Domestic air travel **dropped by 41%** from last year
- Building carbon use has **reduced by 15%** from last year
- In London our print volume is **less than 20%** of what it was before 2010

Our adoption of smarter working and upgrading our video conferencing capabilities has contributed greatly to these improvements.

We remain on track to achieving the Greening Government Targets, which include the following objectives (against a 2009-10 baseline):

- **32% reduction in overall carbon**
- **Reduce landfill to 10% of total waste**
- **Increase the proportion of waste that is recycled**
- **Reduce paper consumption by 50%**
- **Reduce water consumption**

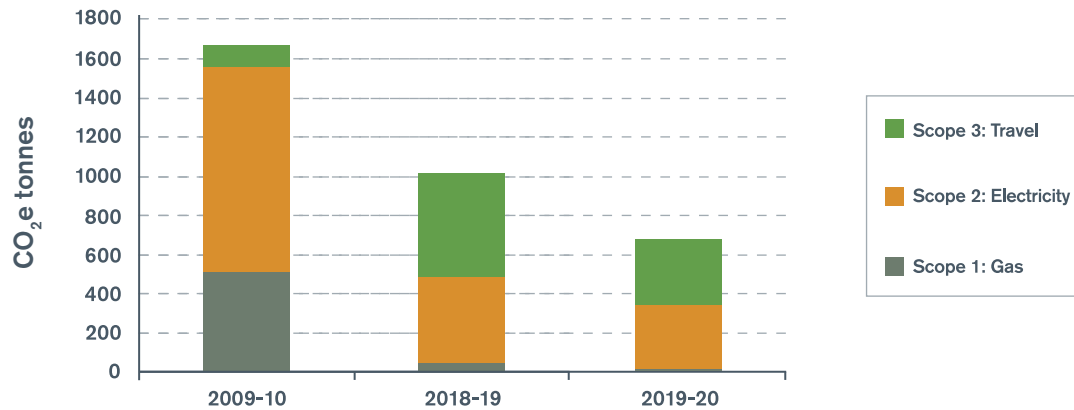
This year we have established a staff led Internal Sustainability Group (ISG). It is a collaborative network for staff interested in unleashing our potential as an organisation to demonstrate climate leadership.

The current areas of focus include:

- **Reviewing our environmental impact as an organisation and identifying areas for further improvement.**
- **Providing a mechanism for staff to contribute ideas for removing barriers to green behaviour and delivering on our decarbonisation objectives.**
- **Rolling out cultural initiatives to empower staff to contribute positively to sustainability through behaviour change, awareness raising and developing climate leaders.**

Most of the data relating to property below refers to our London office only, which is metered and apportioned to the building's tenants. The Landlord in our Glasgow office is less willing to share information and as we pay a fixed cost for our utility usage, we are unable to provide any data and therefore exclude Glasgow from our calculations where applicable.

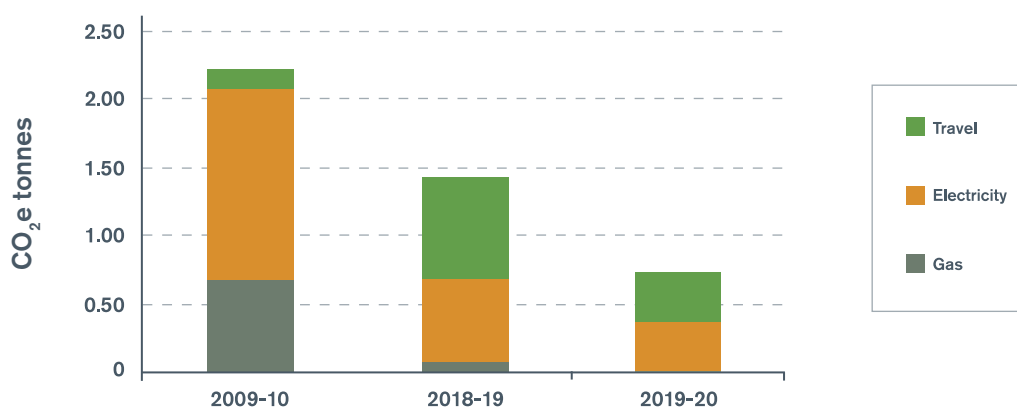
## Total Carbon



Total carbon has been **reduced by 34%** from last year. This is made up of a **15% reduction** in building carbon and a **38% reduction** in travel carbon.

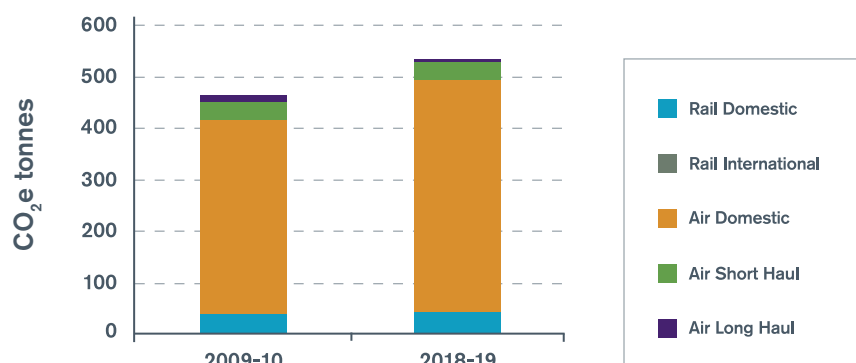
The building carbon reduction resulted from working with Management of our office in the Government Hub at Canary Wharf (10 South Colonnade, or "10SC") and the upgrade of the Building Management System. The ISG working in conjunction with 10SC Management are hoping to continue this arc of improvement.

## Carbon usage by FTE



The overall reduction in carbon means that we achieved a **35% reduction** in carbon usage per FTE compared with last year.

## Travel Carbon



There has been a **39% reduction** in total journeys this financial year compared with last year. While some of that reduction is due to Covid-19 we were only restricting travel from February onwards, so the impact of the pandemic is relatively low. The main reason that travel carbon has reduced is that **domestic air travel dropped by 41%**, partly enabled by an increase in train travel of 33%. Domestic rail travel is six times more carbon efficient than air. This has resulted in a **38% reduction** in total travel carbon.

An upgrade to our video conferencing capabilities to support a reduction in the incidence of face to face meetings contributed greatly to the reduction in travel carbon compared with 2018-19.

We are still working to make further improvements and are encouraging better use of technology and smarter working to reduce future travel.

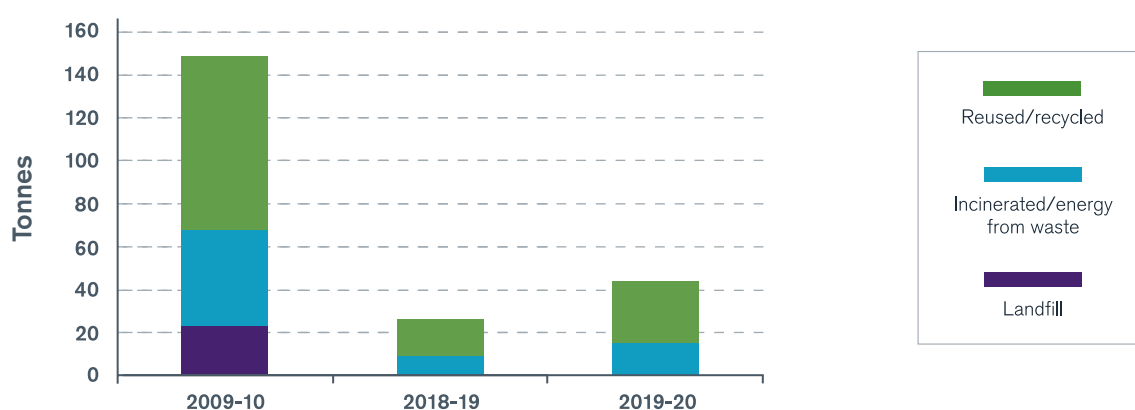
Greenhouse gas emissions		2009-10	2018-19	2019-20
Non-financial indicators (tCO <sub>2</sub> e)	Total gross emissions	1,670	1,015	671
	Per FTE	2.23	1.43	0.92
	Total net emissions	1,671	1,015	860
	Scope 1: Direct GHG emissions	511	49	7
	Scope 2: Energy indirect GHG emissions	1,045	431	330
	Scope 3: Other indirect GHG emissions	115	535	334
Related consumption data (kWh)	Electricity: Renewable (k)	1,130	1,521	1,292
	Gas (k)	1,578	269	35
Financial indicators	Expenditure on energy	£138,240	£308,870	-
	Expenditure on official business travel	N/A	£523,530	-



## Energy efficiency in our buildings

Display Energy Certificates are used to show the energy efficiency of public buildings. The Display Energy Certificate (DEC) rating for the entire 10SC building is F-143. We believe this could be improved and will be working with 10SC management to better understand where energy is being used and consider opportunities for better control measures for our building systems, in particular lighting.

## Total waste



Our waste over the past year has risen by 17 tonnes.

This increase is offset by how waste was accounted for during the previous year. We moved to 10SC in Apr 18 as the first occupants and not until late summer did the building start to fill up achieving full occupancy in October 2018. As waste is apportioned across building occupancy, last year's increase extrapolates roughly to 2018-19 levels and it is not until the next reporting year that we will be able to accurately compare.

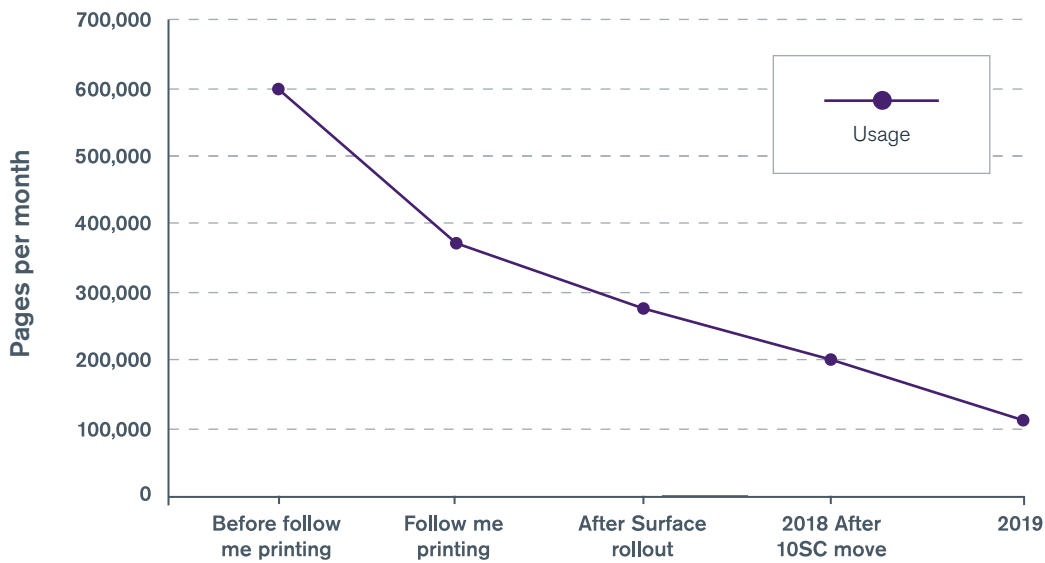
We have not sent waste to landfill since 2010, one of the Government Targets achieved and maintained since 2010.

Waste		2009-10	2018-19	2019-20	
<b>Non-financial indicators (tonnes)</b>	<b>Target</b>	-	-	-	
	Total waste	149	26	43	
	Total waste per FTE	0.2	0.04	0.05	
	Hazardous waste	1	-	-	
	Non-hazardous waste	Landfill	23	0	0
		Reused/Recycled	81	15	28
Incinerated/ energy from waste		44	11	16	
<b>Financial indicators</b>	Total disposal cost	£11,845	£9,798	-	

## Paper Consumption

The stated goal is to reduce paper consumption by 50% from the baseline year.

### Decline in monthly printing in London

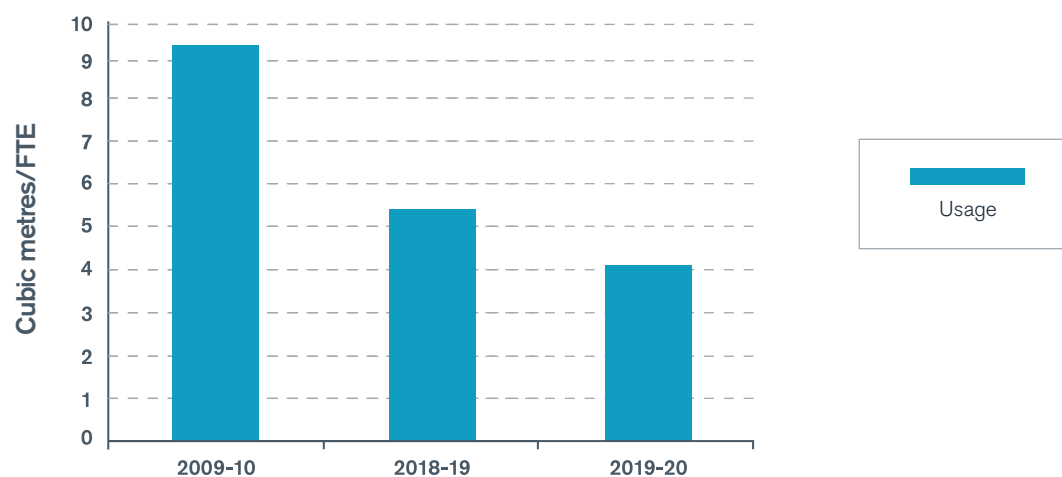


In our London office, print volume is **less than 20%** of what it was before 2010. Our Glasgow office has remained largely the same for the last three years. This is due to the need to print documents in our Glasgow office to meet statutory requirements of the environmental schemes that Ofgem oversees.

## Water

Our water use per FTE has marginally decreased from last year and is under our previously stated goal of 6m<sup>3</sup>.

### Water per FTE



Water		2009-10	2018-19	2019-20	
Non-financial indicators	Target		6.00		
	Water consumption (m <sup>3</sup> )	Supplied	7,116	3,608	3,875
		Per FTE	9.5	5.6	4.2
Financial indicators	Water supply costs	£9,026	£8,444		

**Jonathan Brearley**  
Chief Executive

15 July 2020

