

2015 Great Britain and Northern Ireland National Reports to the European Commission

**National Reports in relation to Directives 2009/72/EC
(Electricity) and 2009/73/EC (Gas)**

Ofgem 2015 National Report to the European Commission

Overview

The Directives on gas and electricity liberalisation stipulate a reporting obligation for National Regulatory Authorities (NRAs). To that end, this report covers Ofgem's annual reporting requirements to the European Commission, in accordance with Directives 2009/72/EC (Electricity Directive) and 2009/73/EC (Gas Directive). The structure of the report is agreed at the Council of European Energy Regulators (CEER).

Ofgem is the UK Office of Gas and Electricity Markets. It is governed by the Gas and Electricity Markets Authority (the Authority).¹ The terms 'the Authority', 'Ofgem', 'us' and 'we' are used interchangeably in this document. The Northern Ireland National Report is found in the second section of this UK response.

The Great Britain (GB) report covers:

- Developments in the GB energy markets in 2014 and Quarter I + II of 2015;
- The regulation and performance of the GB electricity and gas markets along the themes of Network Regulation, Promoting Competition, and Security of Supply; and
- Our compliance with the Electricity and Gas Directives on consumer protection and dispute settlement

Since GB energy markets have been fully liberalised and the regulatory structures in place for a number of years, this report is intended as an updated version of the submissions made since 2007. The structure of this report and much of the information remains unchanged, although latest data is supplied.

Finally, for further information on Ofgem's activities, please consult our Annual Reports. The 2014-15 Ofgem Annual Report is available at the link below.²

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¹ The Authority determines strategy, sets policy priorities and takes decisions on a range of matters, including price controls and enforcement. See the Ofgem website for more information.
<http://www.ofgem.gov.uk/About%20us/Pages/AboutUsPage.aspx>.

² https://www.ofgem.gov.uk/sites/default/files/docs/2015/06/annual_report_ad_accounts_2014-15.pdf

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1. Chairman's Foreword

The energy sector has been the focus of much attention over the past year and our role as an independent regulator, charged with protecting energy consumers, has been firmly in the spotlight. A General Election, a thorough review of our strategy, and an ongoing competition investigation into the energy sector are just three of the notable 2014 developments. However, as this report demonstrates, there has also been an extraordinary amount of work at both the national and European level to encourage competition, promote value for money and ensure security of supply.

We are particularly proud of the steps we have taken, through our innovative regulatory regime, to bolster the levels of electricity interconnection between ourselves and our neighbours. We have confirmed decisions for links to Belgium, Norway and France, and are reviewing further proposals for projects to Denmark, France and Ireland. Once constructed, this interconnection will strengthen our security of supply and enhance competition for decades to come.

We've also reached an important milestone in enhancing transparency with the implementation of REMIT. Our new powers to investigate market conduct and act in the event that we discover unlawful behaviour are crucial to maintaining a safe, secure and trusted wholesale energy market.

We continue to play a leading role in the work of European energy regulators, through both the Agency for the Cooperation of Energy Regulators (ACER) and the Council of European Energy Regulators (CEER), to ensure effective cooperation, play our part in making a Europe wide internal energy market a reality and to deliver the best possible outcomes for British consumers. This will continue over the next year and we look forward to working closely with the European Commission to create an Energy Union that will deliver benefits for consumers.

There is no doubt that the year ahead will be important for Ofgem. We will work with the CMA to develop and implement their final proposed remedies, where they fall within our jurisdiction, to deliver a more competitive market for customers. We will also focus on ensuring security of supply and increasingly focus on the future challenges, such as flexibility and enhanced demand side participation, facing the British market.



David Gray
Chairman

2. Main Developments in Gas and Electricity Markets

Ofgem strives to maintain and strengthen a competitive, stable and sustainable energy market that brings affordable and secure energy supplies to consumers. Transparent, integrated and liberalised European gas and electricity markets play an important role in helping us achieve these objectives. In the past year we've focused on facilitating investment in interconnection; implementing new rules to enhance transparency and trust in wholesale markets; and on promoting competition in retail markets.

Promoting efficient infrastructure investment

Creating an environment to encourage long term infrastructure investment in GB and across borders remained a top priority for Ofgem in 2014. Our 'cap and floor' regime, initially put in place for the Nemo interconnector between GB and Belgium, has been extended to future electricity interconnection projects in August 2014 and we have finished the first round of price controls using our new incentive-based regulatory framework (RIIO).

A step change in interconnection investment

Increasing certainty for developers is key to facilitating investments in projects with a long life. Our cap and floor regime provides greater revenue visibility to those planning to invest in interconnection projects, while ensuring they remain exposed to the signals faced by the market and face strong incentives to be efficient. To date, cap and floor frameworks have been granted to two electricity projects – the Nemo connection between GB and Belgium and the NSN link between GB and Norway, which will be the longest subsea interconnector in the world. There are several more interconnector projects currently being considered for the cap and floor framework, namely the FAB Link and IFA2 interconnectors to France, the Viking Link to Denmark and Greenlink to the Republic of Ireland. Greater interconnection will promote competition in British markets and beyond, as well as enhance security of supply.

Focussing network regulation on what consumers value

RIIO, our new incentive based price control framework was put in place for the electricity distribution companies earlier this year. This framework determines the outputs, allowed revenues and other elements of the regulatory frameworks for network companies over an eight year period and is one of the first to use incentives in such a prominent way. A key focus of the package is on encouraging the innovation required as the electricity system changes so fundamentally.

An integrated approach to planning and regulation

We also delivered a project to better coordinate the long term development of the electricity system. National Grid, the system operator, will be given additional responsibilities to identify the need for investment in the transmission network and coordinate new investment options. Furthermore, we will extend the use of competitive tendering to onshore transmission assets that are new, separable and high value in order to introduce competition in to more areas of the market and further drive down prices.

Creating competitive, integrated and transparent wholesale markets

Increasing transparency in the European wholesale market

Transparency is critical for stable, well-functioning wholesale markets. The implementation of REMIT legislation is paving the way towards a pan-European market that is resistant to insider trading and market manipulation. As of December 2014, all market participants must register with Ofgem in order to legally trade and earlier this year, we were granted criminal powers to prosecute any market participant found to be in breach of the rules.

Ensuring affordable and secure energy for the future

In 2014, Ofgem introduced a number of measures to improve both the functioning of our wholesale market and ensure, as our power generation mix changes, the secure supply of energy. Revisions to the way our system operator balances the electricity network have incentivised market participants to facilitate efficient balancing. As well as enhancing the flexibility of the system, these changes (such as a single cash out price) also help to simplify the process, thus facilitating the market entry of smaller players.

As well as changes to the electricity network system operation, we introduced a number of changes to the gas cash-out arrangements in an emergency, in order to ensure that the market rules provide appropriate incentives on gas shippers to balance supply and demand. With an increasing reliance on gas imports, these changes are intended to avoid or minimise an emergency and protect consumers that incur high costs when interrupted.

Additionally, in 2014 the Government introduced, as part of its electricity market reforms, a capacity market to provide incentives for investment in generation and secure energy supplies for GB consumers. After the first auction in December 2014 and feedback from a variety of stakeholders, Ofgem is now working on ways to streamline the auction process and encourage more participation from demand side response.

Facilitating market integration

Since the adoption of the Third Package, Ofgem has worked hard to develop and implement both the rules and infrastructure needed to be part of fully integrated European markets. In early 2014 we joined the North-West market coupling project, which allows energy to be traded across 17 countries in the day-ahead timeframe, and allows energy to flow to where it is most valued. Additionally, Ofgem has continued to play a central role in developing the rules for cross border trading - the European network codes - and is in the process of implementing those new laws in Britain.

Ensuring retail markets deliver for consumers

The health of our retail market is crucial for delivering benefits to consumers. After several years of concern and the release of the first 'State of the Market Report', we referred the market to the Competition Markets Authority (CMA), due to concerns over a lack of competition. We have continued to work with the CMA to aid their investigation and await their recommendations in the summer. We are also exploring the potential for flexibility to play a greater role in the market, continuing the roll out of smart meters across the country and monitoring companies' compliance with their licence conditions and relevant legislation.

Acting decisively where rules are breached

Energy companies must comply with the relevant European and national legislation, as well as the conditions in their licences. Ofgem monitors this compliance and where companies are found to be breaching the rules, we take action to ensure consumers

benefit. From Jan 2014 – May 2015, our enforcement activity led to energy companies paying a total of £82 million in compensation and payments. Our most notable investigations included:

- In April 2015 we penalised E.ON £7.75 million following an overcharging error. E.ON incorrectly charged exit fees and/or overcharged customers following price rises. The penalty fee went to Citizens advice to help vulnerable consumers.
- During March 2015 we concluded a series of cases looking at the compliance of companies with the Community Energy Saving Programme – a policy designed to improve domestic energy efficiency standards in the most deprived areas across Britain. Six companies failed to meet these deadlines. A total of £47.9 million was paid in compensation and fines as a result.
- In July 2014 we concluded our investigation into E.ON’s telephone and face-to-face activities. In order to help domestic customers make well informed decisions in response to telephone and face-to-face sales activities, we put in place a new licence condition that requires suppliers to provide complete and accurate information which is understandable, appropriate and not misleading. E.ON failed to comply with various aspects of their obligations over a three year period and as a result it was agreed they should pay £12 million to vulnerable customers.

Looking forward

2014 has seen significant developments in facilitating integration with our neighbouring gas and electricity markets. Progress with European network codes and guidelines has put us a step closer towards creating the Internal Energy market foreseen by the Third Package, REMIT has created a fair and trusted environment for pan-European trading and increasing levels of interconnection have the potential to enhance competition and security of supply.

Looking ahead, Ofgem will continue to work with our regulatory colleagues via CEER and ACER and colleagues in the European Commission in order to overcome the challenges that increasing levels of renewables in the generation mix will bring, as well as promoting the values of flexibility and demand side response. We will also continue to work with the CMA in order to determine whether any regulatory remedies are needed to deliver improved competition in the GB energy markets.

At both the European and national level we will continue to ensure that the consumer is at the forefront of the energy market.

3. The electricity market

This chapter contains details of developments within GB's electricity sector during 2014. This is broken down into sections covering network regulation, promoting competition, and security of supply in the wholesale and retail electricity markets.

3.1 Network regulation

Under this section unbundling, technical functioning, tariffs for connection and access, cross border issues and compliance are discussed. We show briefly what has previously been done to ensure compliance with legislation as well as other regulatory activities and market developments in 2014.

3.1.1 Unbundling

Articles 10, 11, 26 of the Electricity Directive and Article 3 Regulation (EC) 714/2009 outline our obligations in relation to unbundling certification of transmission system operators (TSOs). The Electricity and Gas (Internal Markets) Regulations 2011 (which entered into force on 10 November 2011) and the Gas and Electricity (Ownership Unbundling) Regulations 2014 (which entered into force on 15 January 2015) are together known as "the GB Regulations". The GB Regulations implement the Third Package into GB domestic legislation, including the ownership unbundling requirements set out in the Third Package Directives and Regulations in respect of TSOs and the unbundling requirements in respect of Distribution System Operators. The GB Regulations have amended the Electricity Act 1989 (Electricity Act) to include the requirement for the holders of electricity interconnector and electricity transmission licences to be certified as independent pursuant to one of the grounds for certification set out in the Electricity Act.

The GB Regulations have designated the Authority as the NRA for GB and have given it the responsibility for administering the certification process in GB. The Authority also has to notify the European Commission upon receipt of an application for certification where the applicant is from a third country or is controlled by a person from a third country. The Authority received no such applications in 2014.

TSOs

Under Article 10 of the Electricity Directive we have an obligation to ensure any undertaking which owns a transmission system is certified before it is approved and designated as a transmission operator.

In 2014 the Authority did not publish any new final certification decisions (pursuant to sections 10D(6)-(8) of the Electricity Act and Article 3(2) of Regulation (EC) No. 174/2009 (Electricity Regulation). Under Article 10 of the Electricity Directive we also have an obligation to monitor the continuing compliance of certified TSOs with the requirements of Article 9. We continue to monitor the certification status of the certified TSOs in GB, including through the review of annual declarations submitted by the relevant entities. In 2014 these entities were:

- Scottish Hydro Electric Transmission Limited
- Scottish Power Transmission Limited
- National Grid Electricity Transmission plc (NGET) and National Grid Interconnectors Limited (NGIL)
- BritNed Development Limited
- Moyle Interconnector Limited

The Authority also reviewed the certification status of the following certified OFTOs: Blue Transmission Walney 1 Limited, Blue Transmission Walney 2 Limited, Blue Transmission Sheringham Shoal Limited and Blue Transmission London Array Limited. The Authority concluded that the certification of each of them should be continued as the certification basis in respect of each of them continues to apply.³

Distribution System Operators (DSOs)

Under Article 26 of the Electricity Directive of the European Parliament and of the Council of 13 July 2009 we have an obligation to ensure that where the distribution system operator is part of a vertically integrated undertaking, it shall be independent at least in terms of its legal form, organisation and decision making from other activities not relating to distribution.

In relation to Article 26 of the Electricity Directive, there continue to be fourteen distribution service providers: Northern Powergrid (Northeast) Limited; Northern Powergrid (Yorkshire) plc; London Power Networks plc; South Eastern Power Networks plc; Eastern Power Networks plc; Electricity North West Ltd; Scottish Hydro Electric Power Distribution plc; Southern Electric Power Distribution plc; SP Distribution plc; SP Manweb plc; Western Power Distribution (East Midlands) plc; Western Power Distribution (West Midlands) plc; Western Power Distribution (South West) plc; and Western Power Distribution (South Wales) plc.

There are seven independent (embedded) electricity DSOs: Independent Power Networks Ltd; Energetics Electricity Ltd; The Electricity Network Company Ltd; ESP Electricity Ltd; Harlaxton Energy Networks Ltd; Utility Assets Ltd; and Peel Electricity Networks Ltd.

During the year we reviewed the information submitted by DSOs relating to business independence, financial reporting and output performance. In that context we were satisfied that Directive requirements relating to unbundling were being properly observed. We also instigated a review of participation by DSOs in VAT group arrangements. Our requirement for DSOs to have two independent directors on their boards came into effect during 2014.

³ All Final Decisions for OFTOs and Preferred Bidders can be found on our website.

3.1.2 Technical functioning

The technical functioning of the network is of great importance to ensure safe, secure and reliable electricity supply for consumers. In the following, we report on our responsibilities and activities for: electricity balancing services; maintaining security and reliability standards; developing our transmission system; monitoring time taken to connect and repair; monitoring safeguard measures and reporting on the RES regulatory framework over the course of 2014, in the transmission and distribution networks.

Balancing services

Under Article 37(6)(b) of the Electricity Directive, NRAs are responsible for fixing or approving the methodologies used to calculate or establish terms and conditions for the provision of balancing services.

NGET is the System Operator (SO) for the high voltage electricity transmission system in GB, with responsibility for making sure that electricity supply and demand stay in balance and the system remains within safe technical and operating limits. NGET's licence contains conditions regarding the Balancing and Settlement Code – the document which defines the rules and governance for the balancing mechanism and imbalance settlement – and regarding the procurement and use of balancing services. The Balancing and Settlement Code objectives are set out in NGET's licence and include the efficient, economic operation of the transmission system and compliance with relevant legally binding European Commission decisions.

The current electricity balancing arrangements are designed to provide commercial incentives for generators to physically match the amount that they notify they will deliver with what they ultimately deliver to the system. The current arrangements are also designed to provide commercial incentives for suppliers to physically match the amount they notify they will offtake, to the amount they ultimately offtake from the system. Generators' imbalances relate to the difference between the amount they physically deliver and their contracted volume. Suppliers' imbalances relate to the difference between that notified and that which is offtaken. Where there is an imbalance either the generator or supplier will incur cash-out charges – thereby providing the incentive to balance.

Ofgem has proposed improvements to these balancing and cash-out arrangements as part of our Electricity Balancing Significant Code Review which we launched in 2012. We published our Final Policy Decision in May 2014 and phased implementation of the reforms will start in November 2015. The reforms change the cash-out arrangements in order to improve incentives to balance efficiently. They also improve the signals about the need for flexible capacity, which is becoming increasingly important as we transition into an electricity system with an increasing share of intermittent generation.

NGET recovers the costs of balancing the system through Balancing Services Use of System (BSUoS) charges, derived from the BSUoS charging methodology which is set out in the Connection and Use of System Code (CUSC) and approved by Ofgem. Ofgem places financial and reputational incentives on the SO to encourage low operating costs within the safety and security bounds set out under the codes and licences. In addition, Ofgem is required to approve any change to the charging methodology. Further details of how BSUoS charges are levied can be found below in section 3.1.3 of this report.

Security and reliability standards, quality of service and supply

Transmission

Under Article 37(1)(h) of the Electricity Directive, regulators must monitor compliance with, and review past performance of, network security and reliability rules as well as set or approve standards and requirements for quality of service and supply. The National Electricity Transmission System Security and Quality of Supply Standard (NETS SQSS) is a technical standard that licencees are required to comply with. NETS SQSS contains coordinated criteria and methodologies that Transmission Licencees and the SO are required by their respective licences to use when planning and operating transmission systems. Ofgem must approve any change to the NETS SQSS. NGET's licence requires NGET, in its role as SO, to submit a report providing details of system security and quality of service and supply to Ofgem each year. The 2014 report includes information on system availability, security and quality of service of the NETS during 2014.

System Reliability

There is also a regulatory mechanism in place to incentivise onshore TSOs to maintain a reliable and secure system. For the purpose of the incentive mechanism, reliability is measured by the total volume of Energy Not Supplied (ENS) to customers due to loss of supply events. Each TSO is set an annual target ENS volume and is either rewarded or penalised each year according to its level of performance against its target. There is also a suite of network output measures that inform the safety and reliability of a TSO's network and will directly affect the funding at the start of next price control, RIIO-T2, in 2021.

OFTOs' system availability incentive targets are set out in each individual OFTO licence. The mechanism incentivises the OFTO to maintain system availability and therefore export capacity available to offshore generators. OFTOs receive financial rewards or penalties for performance above or below this target.

System development

In order to ensure our transmission system can continue to function well technically in future years, in 2014 Ofgem has continued to use its Strategic Wider Works (SWW) programme. This provides flexibility within the RIIO-T1 price control by allowing TSOs to bring forward projects when more information is available (rather than only allowing TSOs to develop projects that were agreed at the start of the price control). This helps to manage uncertainty and to ensure value for money for consumers by ensuring that network infrastructure projects are progressed at the most appropriate time. Since the start of 2014, under RIIO-T1, we have approved new transmission projects under the SWW arrangements. Both proposals were made by Scottish Hydro Electric Transmission to reduce bottlenecks on the northern Scottish transmission network.

The Beaulay-Mossford project will provide an extra 252MW of transmission capacity by the end of the third quarter of 2015-16. We allowed £53.2 million (2013/14 prices) for this project.

The Caithness-Moray project will cost £1.1 billion (2013/14 prices) and is the largest single electricity transmission reinforcement we have approved. It will increase capacity of the transmission network in northeast Scotland by around 800MW for 1.2GW of new renewable generation due to connect in 2018.

In 2014 we received three full submissions from electricity transmission licencees to the Electricity Network Innovation Competition which is also part of the RIIO-T1 price control. Funding is provided for innovative network projects which have the potential to provide

environmental benefits and financial savings for customers, at value for money. Three of the four projects were selected for funding. We awarded a combined total of £18.8m, of the available £27m. These examples show how Ofgem has continued to strive to develop the GB network, in order to protect the interests of existing and future consumers.

Distribution

In GB, licenced electricity Distribution Network Operators (DNOs) are required by a standard condition of their licences to design their networks to meet the requirements of the Engineering Recommendation standard P2/6 which sets out the normal levels of security required for distribution networks and the requirement for provision of emergency network capacity. In the event that a licensee cannot comply with this licence condition it is able to apply to us for a derogation.

In 2015 we issued the next electricity distribution price control, RIIO-ED1. This will run from 2015-2023 and sets the outputs that the 14 electricity DNOs need to deliver for their consumers. It sets the expenditure for this period on the network at £24.6 billion with expectations that companies will provide long-term reliability, minimise the number and duration of interruptions and ensure adaptation to climate change. RIIO-ED1 replaces the previous price control, Distribution Price Control Review 5 (DPCR5), which ran from April 2010 to March 2015.

The Electricity (Standards of Performance) Regulations 2010 (SI 2010/698) provide the legal framework for guaranteed standards for quality of service. They are specific minimum levels of service customers should expect from DNOs and must be met by each distribution company. In the event of a company failing to meet a guaranteed standard of performance it must make a payment to the customers affected. The standards cover areas such as restoring supply during an unplanned interruption, connections and voltage quality. In 2014 we proposed to update and tighten these standards of performance for electricity distribution operators, in line with decisions made as part of the new electricity distribution price control (RIIO-ED1), and a review following the December 2013 storms.

Ofgem monitors and enforces the guaranteed standards relating to quality of supply. All DNOs are required by their licences to provide us with data on the performance of their network. There are annual performance indicators, known as output measures, for specific service areas which are set out in the Regulatory Instructions and Guidance for reporting. Information such as the number and duration of interruptions, quality of telephone response and fault rates have been collected over the course of 2014.

There are financial incentives to encourage improved performance too. For example, the Interruptions Incentive Scheme began in the DPCR5 and continues in the RIIO-ED1 price control. It rewards and penalises depending on each DNO's performance against its targets for the number of customers interrupted and the number of customer minutes lost. This scheme incentivises DNOs to invest in and operate their networks to manage and reduce the frequency and duration of power cuts experienced by their customers. Following the December 2013 storms there was £4.7 million paid out to consumers who were affected by supply interruption, under the guaranteed standards and in goodwill payments.

Innovation will play a key part for DNOs to deliver security and reliability of supply at an efficient cost while dealing with uncertainty. In RIIO-ED1 price control we established the Network Innovation Stimulus, to help network companies understand what they need to do to provide security of supply at value for money as GB moves to a low carbon economy. Its equivalent Low Carbon Network Fund in DPCR5 sponsored four projects in

2014 by the DNOs to trial new technology or arrangements. In addition we believed that cost efficiencies delivered from rolling out smart grid solutions and wider network innovation from Low Carbon Network Fund trials can be embedded in the DNOs' business plans, and therefore reduced the DNOs' allowance by £322 million in RIIO-ED1.

Monitoring time taken to connect and repair

Regulators, under Article 37(1)(m) of the Electricity Directive, are required to monitor the time taken by transmission and distribution system operators to make connections and repairs. Here we report on how we have monitored this for transmission and distribution system operators during 2014.

Transmission

Since 2011, under the Connect and Manage regime, generators have been able to connect to the system in GB ahead of wider system reinforcements. It is the responsibility of the SO to ensure that the power flows across major system boundaries are within the capabilities of the system. The additional cost of these actions and the resulting 'Constrained Dispatch' of generation (constraint costs) are socialised, i.e. spread across all generation and demand (levied 50:50) in GB, and are recovered through BSUoS charges.

We receive biannual 'Timely Connections' reports from the TSOs. These reports provide us with information on the factors affecting the connection dates offered to generators. This enables us to assess whether any changes to the existing framework are needed. A non-confidential version of the report is published on NGET's website.

We also submit an annual report to the Secretary of State which monitors the impacts of the 'Connect and Manage' regime. The most recent report (December 2014) noted that under the regime, connection dates continue to have been brought forward by an average of five years compared with previous arrangements.

To date all OFTOs own and operate assets built by offshore generators. As such there have been no issues under the offshore transmission regime regarding the time taken to connect during 2014. OFTOs' licences require them to report, on a quarterly basis, offshore transmission system performance and whether that performance has fallen below target. All OFTOs have reported system availability at levels above the incentive target for 2014.

Distribution

For the purposes of reporting 'time to connect' we consider that it is made up of two elements: time to quote and time to connect. We consulted on these definitions with DNOs. Time to quote is defined as the difference, in working days, between the date the customer applies for a new connection and the date a quotation is issued to the customer. Time to connect is defined as the difference between the date on which the customer accepts the quote and the final connection date (when the connection has been installed, commissioned and left safe).

Historically, we have monitored the time taken by DNOs to provide connection offers and (since 2010) complete the connection. We have also established guaranteed standards for connections that provide compensation payments to customers where the DNO fails to deliver specified connection services within minimum timescales. These standards cover the provision of quotations, scheduling agreed dates for works with customers and completing works on the dates agreed with customers. Failure to meet these standards on 90 per cent of occasions in each quarter constitutes a breach of licence.

In their business plans for the new price control period, RIIO-ED1, companies have set their own targets for time taken to connect which they will report on. We have also introduced a new 'time to connect' incentive in RIIO-ED1 which will reward DNOs if they are able to issue quotes and complete connections (for smaller connection projects) quicker than the target timescales.

We also monitor the time taken to repair faults through the Interruptions Incentive Scheme. The time taken to repair has been incentivised as part of the customer minutes lost element of the Interruptions Incentive Scheme – this is dealt with more fully in the 'Security and reliability standards, quality of service and supply' sub-section.

Monitoring safeguard measures

In the event of a sudden crisis in the energy market and where the physical safety or securities of persons, apparatus or installations of system integrity are threatened, a Member State may temporarily take the necessary safeguard measures. Under Article 37(1)(t) of the Electricity Directive, regulators are required to monitor the implementation of those safeguard measures.

During a fuel crisis, the government has the power to direct the behaviour of the operators of certain power stations and transmission licencees to ensure industry obligations are fulfilled. The details of these arrangements are set out in the Fuel Security Code (standard licence condition B11) which transmission licencees must comply with. Under the Fuel Security Code, in an emergency the Energy Emergencies Executive Committee will establish the Joint Response Team to liaise between industry and government and to develop the mechanism by which the practical management of an emergency can be achieved.

The principal objective of this Fuel Security Code is to provide an administrative structure during a fuel crisis enabling appropriate measures be taken by the government with minimal interference with normal market arrangements. There were no such emergencies in 2014, hence the Joint Response Team was not established in 2014.

Regulatory framework for Renewable Energy Sources

Under Article 11 of Regulation (EC) 713/2009 NRAs are required to monitor access to the network, including access of electricity produced from renewable energy sources.

As part of RIIO-ED1 we introduced a specific incentive for large connection customers, the Incentive on Connections Engagement. This aims to drive DNOs to understand and meet the needs of major connection customers (larger metered demand, unmetered, distributed generation). If a DNO fails to do this, then it could incur a penalty. As part of the Incentive on Connections Engagement, DNOs must submit two reports, one at the start of the regulatory year outlining their commitments to improve services and another at the end of the year reporting back against the commitments made. We received these submissions on the 30th June 2014 which describe how DNOs have performed against the strategies for engagement, work plans of activities and key performance outputs they set themselves at the start of 2013-2014. At the end of 2014 we issued a consultation on the guidance for assessing these submissions.

During the DPCR5 we set out arrangements to facilitate the development of competition for contestable services in the electricity connections market. We specified segments of the market in which we believed competition was viable for the contestable part of the

connection. As part of our DCPR5 proposals, DNOs were required to demonstrate to us that there is effective competition in different segments of the market (the Competition Test). Where we believe there is effective competition, a DNO is allowed to charge an unregulated margin on contestable works.

DNOs were able to submit applications up to the end of 2013. We completed the Competition Test process in April of 2014 when we published our final round of decisions on applications. Overall we were satisfied that effective competition exists in 42 out of 126 relevant market segments. We consider that the competition test process has improved the state of competition in the market, however we have still not seen enough evidence of effective competition. In June 2014 we published a call for evidence to understand why competition was not developing in some parts of the market. After reviewing the evidence, we found that there are behavioural changes that can be made by the DNOs that could resolve the issues identified without the need for fundamental structural reform. We will issue a consultation in early 2015 on these remedial actions and publish a decision in the summer of 2015.

We will continue to report on the progress of this process and provide updates on how competition in connections is developing in the Electricity Distribution Annual Report.

3.1.3 Network tariffs for connection and access

Under Article 37(1)(a), (3)(c),(d), (6)(a), (8), (10), (12), of the Electricity Directive, NRAs are required to fix or approve transmission or distribution tariffs or their methodologies. Here we report on our activities surrounding the regulation of tariffs and network charges (for transmission and distribution) during 2014.

Transmission

Users of the electricity transmission system are subject to three types of transmission charges in GB: Connection charges, Transmission Network Use of System (TNUoS) charges and BSUoS charges.

Connection Charges

Connection charges relate to the provision and maintenance of connection assets which are solely required to connect a particular user (a generator, for example) to the main transmission system. The costs are recovered under NGET's connection charging methodology,⁴ which is approved by Ofgem. NGET defines 'connection assets' as assets solely required to connect an individual user to GB's transmission system, which are not and would not normally be used by any other connected party. The costs of these assets are recovered directly from the generator via connection charges. During 2014 Ofgem approved one modification to the connection charging methodology.

TNUoS Charges

The TNUoS charging methodology is applied by NGET in its role as SO and is approved by Ofgem. TNUoS charges recover the cost of the provision and maintenance of shared electricity transmission assets, or in other words, assets that cannot be solely attributed to a single user. TNUoS charges are recovered from all users of the GB electricity transmission system (excluding interconnectors). These charges vary by location, reflecting the costs that users impose on the transmission network to source (demand) or send (generators) their electricity.⁵

In October 2014 we approved CUSC Modification Proposal 224 which caps the maximum average transmission charges for generators in GB to ensure compliance with EU Regulation 838/2010. This restricts average generation charges in GB to between €0/MWh and €2.5/MWh.⁶

In July 2014 we approved CMP213 which will introduce transmission charges that vary based on generator type and historical annual load factor, as well as based on location and capacity. This change is scheduled to be implemented from 1 April 2016. Our decision has, however, been challenged and is currently under judicial review.

BSUoS Charges

NGET recovers the costs of balancing the system through Balancing Services Use of System (BSUoS) charges, derived from the BSUoS charging methodology which is set out in the Connection and Use of System Code (CUSC) and approved by Ofgem. For all three charges (Connection, TNUoS and BSUoS) the form of the methodologies must be approved by Ofgem, but we do not set or approve the level of individual charges. Additionally, wider

⁴ <http://www2.nationalgrid.com/uk/Industry-information/System-charges/Electricity-transmission/Transmission-Network-Use-of-System-Charges/Statement-of-Use-of-System-Charges/>.

⁵ See 2010 National Report for a more detailed description of the components of the TNUoS charge.

⁶ <https://www.ofgem.gov.uk/publications-and-updates/connection-and-use-system-code-cusc-cmp224-cap-total-tnuos-target-revenue-be-recovered-generation-users>.

industry, including generators and suppliers, can raise proposals to modify the charging methodologies which are subject to thorough review and consultation. The decision to modify the charging methodologies still rest with Ofgem, except where a proposed modification meets the self-governance criteria where the CUSC Panel can decide without reference to the Authority. Parties can appeal changes to the CUSC. During 2014 Ofgem rejected one modification to the BSUoS charging methodology.

Distribution

The electricity distribution licence requires DNOs to have in force at all times a Use of System Charging Methodology and a Connection Charging Methodology (collectively known as the Charging Methodologies). Both must be approved by Ofgem.

DNOs have developed common approaches to connections charging and distribution use-of-system (DUoS) charging. These common approaches include:

- The Common Distribution Charging Methodology for all customers connected at the lower voltages.
- The Extra High Voltage Distribution Charging Methodology for all demand and generation customers at the higher voltages.
- The Common Connections Charging Methodology, incorporated into all DNO connection methodologies.

Each DNO's connection charging methodology incorporates a company-specific section as well as the common methodology. The licence requires DNOs to comply with their Charging Methodologies and to publish Charging Statements prepared in accordance with those methodologies except where explicit consent is given by us. The Electricity Act 1989 enables us to determine certain disputes including whether a DNO has applied charges in line with their Charging Methodologies.

There are provisions for stakeholders to provide inputs to proposed changes to the methodologies or tariffs. This is done either through participation in industry working groups, or through the public consultation processes. We consider any inputs received when reaching a decision on methodologies or tariffs. Whilst we have the power to make a decision on proposed changes to the methodologies, we do not have the power to review these decisions.

Stakeholders have the right to apply for a review by judicial authorities in respect of any such decision. There has not been any application for judicial review of any decision regarding the methodologies or tariffs during 2014.

Prevention of cross-subsidies

Each NRA, under Article 37(1)(f) of the Electricity Directive, is required to ensure that there are no cross-subsidies between transmission, distribution and supply activities.

In GB, licenced electricity distribution, gas distribution and transmission network operators (including offshore licencees) are subject to licence conditions prohibiting regulated businesses from giving cross-subsidies to, or receiving cross-subsidies from, related undertakings. The regular information submissions that licencees are required to make, principally those relating to their price control arrangements, allow us to assess whether any risk or incidence of cross-subsidisation has arisen.

Electricity and gas transmission and distribution licences include a requirement for independent auditors to carry out a range of procedures, agreed with the Authority, to provide assurance that obligations to avoid discrimination and cross-subsidies are being respected. We review the auditors' reports and raise supplementary questions as appropriate.

The unbundling requirements as described in section 3.1.1 also provide for greater structural separation of transmission interests from generation, production and supply interests in order to prevent cross-subsidisation.

We are satisfied that there were no material cross-subsidisation issues during 2014. We are satisfied that guidance issued to TSOs and DSOs has been followed. A key area which we will continue to monitor is the interpretation and application of requirements for financial transactions to be completed on an arm's length basis and on normal commercial terms. This is especially relevant with respect to the terms of loans made to or by the licensee. Other key risk areas which we take into account are:

- the basis of recharging for services provided at a group level;
- the justification for any management fees charged to the licensee by related parties; and
- the interest rates charged on intra-group loans affecting the licensee.

We do not have any unresolved concerns at present, but arrangements need to be monitored in the context of refinancing, restructuring and corporate transaction events.

On 1 April 2014, our new requirement for each licensee (except for independent DSOs and OFTOs) to have at least two sufficiently independent directors came into effect. We consider that this measure will be supportive of good governance at licensee level, including compliance with licence conditions relating to the prevention of cross-subsidisation and discrimination.

3.1.4 Cross-border issues

In order to reach a fully integrated European energy market, it is vital that NRAs coordinate effectively on cross border issues. In this section we report on our interconnections (including allocation of capacity and congestion management), our investment plans (with regard to the TYNDP) and our cooperation with other NRAs during 2014.

Access rules on interconnection

The GB electricity market is interconnected with the Netherlands (BritNed), France (IFA), Northern Ireland (Moyle) and the Republic of Ireland (EWIC). A number of new interconnector projects are also at different stages of development.

The Third Package introduced new responsibilities for NRAs regarding the rules for granting access to cross-border electricity infrastructures, which in GB are reflected in the standard licence conditions of the electricity interconnector licence.⁷ These responsibilities can be summarised as follows:

- Licencees are required to submit any new or amended charging methodologies and access rules to Ofgem.
- Both Ofgem and the interconnector operator must ensure that charging methodologies and access rules, and any modifications to these, comply with the following objectives: objectivity, transparency, non-discrimination and compliance with any relevant legally binding decision of the European Commission (EC) or the Agency for the Cooperation of Energy Regulators (ACER).
- Interconnector operators are required to review and consult on their access rules at least once each calendar year and to provide us with a report, that should highlight what amendments, if any, will be made to better facilitate the above objectives. The review must take into account the consultation.
- Ofgem has the power to request licencees to review and amend the access rules.

In 2014, Ofgem continued to monitor interconnector statistics, including information on auctions, capacity, nominations and flows.

Existing interconnection

Interconnexion France-Angleterre (IFA)

The England-France Interconnector is jointly operated by NGIL and Réseau de Transport d'Électricité, the French TSO. IFA is a high voltage direct current line with a capacity of 2000MW.

Capacity is allocated explicitly in the long term, using a single coordinated capacity platform. 'Netting'⁸ and 'use-it-or-sell-it' are applied to ensure that the maximum possible capacity is made available to market participants in all timeframes. Day-ahead capacity is allocated via implicit auctions following the implementation of market coupling. For intraday trading, explicit auctions are used.

⁷ See standard conditions 10, 11 and 11A:

https://epr.ofgem.gov.uk//Content/Documents/Electricity_Interconnector_Standard%20Licence%20Conditions%20Consolidated%20-%20Current%20Version.pdf.

⁸ Netting is the superposition of hourly nominations in two opposite directions, in order to release some capacity in the more congested direction for the next allocation step.

IFA did not propose any changes to its access rules during 2014. It intends to participate in the Harmonised Allocation Rules (HAR) pilot project, which is part of the Forward Capacity Allocation European Network Code.

BritNed

The 1000MW BritNed high voltage direct current cable, between GB and the Netherlands, commenced operation in April 2011. BritNed allocates capacity on its cable through a blend of implicit and explicit auctions. It holds medium term (monthly and annual) and day-ahead implicit auctions (part of market coupling) and intraday explicit auctions.

BritNed has a 25-year exemption from rules relating to the use of interconnector revenues and charging methodologies, and certain licence conditions are not in operation in its licence.⁹ However, it must still comply with the interconnector licence condition relating to access rules, introduced as a result of the Third Package.¹⁰ In September 2014, BritNed submitted a set of modified access rules to Ofgem for approval and in December 2014 we approved them.¹¹ BritNed intends to participate in the HAR pilot project.

Moyle

The Moyle interconnector, which links Scotland to Northern Ireland, offers around 450MW of capacity to the market through explicit long-term, daily and intraday auctions. One cable on the Moyle interconnector continues to be on a forced outage reducing its available capacity to 250MW.¹² It offers a range of long-term products from one month to one year. To maximise the availability of capacity, the use-it-or-lose-it rule applies to all long-term capacity. In July 2014, Ofgem approved proposed modifications to the Moyle access rules.¹³ Moyle intends to participate in the HAR pilot project.

EirGrid East-West Interconnector (EWIC)

EWIC became operational in November 2012. It has a technical capacity of 500MW between Wales and Ireland and uses the same capacity allocation platform as Moyle. It offers capacity through explicit long-term (monthly and annual), daily and intraday auctions and applies 'use-it-or-sell-it' to long-term capacity. EWIC is not exempt from any requirements relating to access rules and charging methodologies. In July 2014, Ofgem approved the amended access rules for EWIC.¹⁴ EWIC intends to participate in the HAR pilot project.

New Interconnection

Eleclink

In September 2014 we published our final decision on the exemption request from Eleclink Limited, a proposed 1000MW interconnector project between GB and France.¹⁵ The decision included a joint opinion with CRE, the French NRA. We granted a partial exemption from use of revenues, third party access and unbundling under Article 17 of the Regulation.

⁹ Standard conditions 9 and 10 of the Electricity Interconnector Licence.

¹⁰ Standard condition 11A of the Electricity Interconnector Licence.

¹¹ <https://www.ofgem.gov.uk/publications-and-updates/approval-britned-access-rules>

¹² <http://www.eirgrid.com/media/Generation%20Capacity%20Statement%202014.pdf>.

¹³ <https://www.ofgem.gov.uk/publications-and-updates/approval-modified-access-rules-and-notice-respect-charging-methodology-moyle-interconnector>.

¹⁴ <https://www.ofgem.gov.uk/publications-and-updates/approval-modified-access-rules-and-notice-respect-charging-methodology-eirgrid-east-west-interconnector>.

¹⁵ <https://www.ofgem.gov.uk/publications-and-updates/final-decision-eleclink-limited%E2%80%99s-request-exemption-under-article-17-regulation-ec-7142009-great-britain-france-electricity-interconnector>

Cap and floor regime development

We have developed a new cap and floor regulatory regime for the Nemo project, the proposed interconnector between GB and Belgium. Following a consultation process, we published a final decision on the cap and floor regime design for Nemo in December 2014.¹⁶

In August 2014, we extended the cap and floor regime to the near-term interconnector projects.¹⁷ We received five applications from projects planning to be operational before 2021. These projects could connect GB with Norway (NSN - 1400MW), France (FAB Link - 1400MW & IFA2 - 1000MW), Denmark (Viking Link - 1000MW) and the Republic of Ireland (Greenlink - 500MW). All five of these projects were deemed eligible for assessment under the cap and floor regime. We prioritised the assessment of the NSN interconnector as the project was closest to taking a final investment decision, and made a decision to grant NSN a cap and floor regime in principle in March 2015.¹⁸ We have also issued a consultation on the other four projects and expect to make a decision on whether to grant cap and floor to these projects in principle in summer 2015.

Monitoring TSO investment plans in view of the Ten Year Network Development Plan

We set price controls for the electricity TSO. As part of this process we review the companies' investment plans. We explicitly require these plans to consider the interaction with wider European developments. We also require the companies to consider the various uncertainties across the period for which the control is set (and across a longer period). Under the price control we require the transmission companies to report on their performance against these plans on a regular basis.

The GB SO produces, on an annual basis, the Electricity Ten Year Statement.¹⁹ This publication describes the GB National Electricity Transmission System, the Transmission Operators' potential investment plans in the wider European network and details of how NGET, as SO, will manage the uncertainty of future energy scenarios in both planning and operating the system. We are in the process of implementing a new licence condition to make the production of this statement by NGET a requirement under the licence, including the requirement to consider potential development of interconnection with the rest of Europe.

The licence condition will also require an explanation of any differences between the data used in the Electricity Ten Year Statement and the EU-wide ten year network development plan.

Integrated Transmission Planning and Regulation (ITPR) project

We set up the ITPR project in 2012 to review the existing arrangements for planning and delivering onshore, offshore and cross-border electricity transmission networks in GB. In March 2015 we published our final conclusions and decided to implement a number of measures to provide for a more integrated approach to electricity transmission planning

¹⁶ <https://www.ofgem.gov.uk/publications-and-updates/decision-cap-and-floor-regime-gb-belgium-interconnector-project-nemo>

¹⁷ <https://www.ofgem.gov.uk/publications-and-updates/decision-roll-out-cap-and-floor-regime-near-term-electricity-interconnectors>

¹⁸ <https://www.ofgem.gov.uk/publications-and-updates/decision-initial-project-assessment-nsn-interconnector-norway>

¹⁹ <http://www.nationalgrid.com/uk/Electricity/ten-year-statement/current-elec-tys/>.

and delivery.²⁰ In the context of this report, we have focused on those measures related to cross-border transmission.

We will maintain a developer-led approach to interconnection, and open more cap and floor application windows in the future, as long as efficient investment continues to be brought forward under this approach. For the transmission elements of potential generation projects from outside GB that would export power directly to GB, our default position will be that their transmission connections will not receive consumer underwriting. However, we will leave open the option of consumer underwriting on a project-by-project basis, in cases where we are satisfied that the regulatory arrangements between GB and the other Member States adequately protect GB consumers. We will maintain continuity in the regulatory treatment of an existing transmission asset if it evolves into a multiple purpose project (MPP – projects that feature some combination of onshore transmission, offshore transmission or interconnection), and work with relevant parties to determine the most appropriate regulatory treatment of MPPs from the outset. Treatment of specific MPPs will need to consider the relevant EU requirements, for example unbundling and third party access.

In addition, we will enhance the SO's role so that it leads the identification of system needs and assesses options to meet these needs. The SO will be required to undertake a new network options assessment process to appraise major investment options and consider the value of potential additional interconnection to other countries. We also confirm our view that it is in consumers' interests to extend the use of competitive tendering to onshore transmission assets that are new, separable and high value. We will now develop and consult on the detailed regime for onshore competition. We plan to work with government to explore legislative change to support extending competitive tendering and the approach to new types of transmission projects, such as MPPs.

Cooperation

Article 37(1)(c) of the Electricity Directive imposes duties on us to consult and cooperate with ACER and other NRAs on cross-border issues. Changes have been made to the Electricity Act to reflect this.²¹ This includes the requirement to provide ACER and other NRAs with the information they may need to carry out their responsibilities under the Electricity Directive. The changes also place a responsibility on us to cooperate with other NRAs to promote certain objectives. These include enabling an adequate level of interconnector capacity and promoting jointly managed cross-border trade in electricity as well as the allocation of cross-border capacity.

Examples of cooperation

In 2014, we cooperated with the NRAs of adjacent Member States over a number of issues around existing and new interconnectors, and continue to. We are working closely with the Irish and Northern Irish regulators to develop and approve common trading arrangements for the Moyle and EWIC and on the Single Electricity Market European market integration project.²²

²⁰ <https://www.ofgem.gov.uk/publications-and-updates/integrated-transmission-planning-and-regulation-itpr-project-final-conclusions>

²¹ See Regulation 35 of the Electricity and Gas (Internal Market) Regulations 2011, which inserts section 3F into the Electricity Act 1989: <http://www.legislation.gov.uk/ukxi/2011/2704/regulation/35/made>

²² http://www.allislandproject.org/en/TS_Current_Consultations.aspx?article=ebc174b6-7ec5-44fa-b1fe-72a665e6966f.

Under the Electricity Directive, NRAs are required to certify TSOs, including interconnector operators, as compliant with the ownership unbundling requirements. See section 3.1.1. This has required cooperation between us and the Irish, French and Dutch NRAs during 2014.

Ofgem, together with GB TSOs and power exchanges are working with European counterparts to voluntarily implement aspects of the European Network Codes and Framework Guidelines for the European electricity market. These are commonly referred to as pilot projects. Specifically, GB is part of multi-region coupling of day-ahead cross border markets. GB TSOs participate in Project Terre which relates to sharing balancing replacement reserves. GB TSOs are working on the development of Harmonized Allocation Rules applicable in the forwards timeframe. In addition to this, we have been consulting with many other NRAs during 2014 through our role as the lead regulator for the cross-border intraday project.

We also actively contribute to ACER and CEER's work in the development of the ENCs and Guidelines for the European electricity market. We hold the chair position of the Grid Connection Workstream and the co-chair positions in the Electricity Working Group and Smart Grids Coordination Task Force. We also actively contribute to other Task Forces under the Working Groups.

3.1.5 Compliance

Ensuring that NRAs and market participants comply with mandatory obligations is essential for a well functioning energy market. Below, we report on our powers to enforce the Agency's and Commission's decisions, as well as the investigations that have concluded during 2014 relating to existing legislation.

Compliance with binding decisions of the Agency and the Commission, and with the Guidelines

Under the Third Package NRAs are required to ensure compliance with and implement binding decisions of ACER and of the European Commission. To provide the Authority with the powers to carry out these functions, the Electricity Act 1989 has been amended. There were no such relevant binding decisions for GB in 2014.

Compliance of transmission and distribution companies, system owners and electricity undertakings with relevant Community legislation, including cross border issues

Ofgem has powers to investigate compliance of distribution companies, onshore and offshore transmission companies, system owners and electricity undertakings with relevant EU legislation. If a breach is found, we have powers to impose penalties. As a condition of certification, TSOs are obliged to notify the Authority if they know (or reasonably should know) of any events or circumstances which have occurred, or are likely to occur, that may affect their eligibility for certification and must provide an annual declaration (approved by a resolution of the TSO's board of directors) in this regard. The Authority also has powers to require information to be provided by the TSO for the purpose of monitoring the TSO's certification.

Ofgem, in close cooperation with other relevant NRAs, ensures TSOs are compliant with Network Codes and Guidelines by monitoring GB TSO business rules, standard transportation agreements and all other relevant operational rules and agreements. Ofgem requires TSOs to notify the Authority if they know (or reasonably should know) of any events or circumstances which have occurred, or are likely to occur, that may affect their compliance with the Ofgem approved network code compliance regime.

Investigations Concluded:

Electricity

Inaccurate reporting

- In June 2014, we found npower breached its reporting requirements under the Electricity Act 1989 by misreporting their supply data for the Renewables Obligation and Feed in Tariff scheme. npower had underreported the amount of electricity supplied from 2010-2012 and this distorted the market for Renewables Obligation Certificates. We fined npower £125,000 for this. npower had also previously voluntarily retired ROCs valued at £896,900 to recognise the impact on the market and made a late payment of £63,000 to account for their Feed in Tariff reporting error.

Network Connections

- During routine monitoring in May 2014, Scottish and Southern Energy Power Distribution ('SSEPD') and Ofgem found that between August 2010 and September 2013 SSEPD had failed to meet the timescales within which customers must be offered connections. In recognition of these failures SSEPD paid £750,000 to the Scottish Hydro Electric Community Trust to assist customers with the cost of electricity

connections in rural areas. SSEPD was found to have previously breached licence conditions relating to the same failures in 2011. Their 2014 donation payment took into account these previous breaches and SSEPD's subsequent failure to fully rectify their systems.

Network Outages

- In July 2014, SSE and UK Power Networks donated £3.3 million in compensation following an informal investigation into the companies' performance during exceptional storms the previous winter. This was in addition to £4.7 million already paid out to consumers under the guaranteed standards and in goodwill payments. Over Christmas 2013 nearly a million homes experienced power cuts due to severe storms; 16,000 customers were left without power for more than 48 hours. The money was subsequently paid to organisations that play an important role in helping vulnerable customers during power cuts and severe weather.

Cross-cutting (electricity and gas)

Environmental Programmes

- In March 2015, we completed seven investigations into compliance with the Community Energy Saving Programme ('CESP') and Carbon Emissions Reduction Target ('CERT'). Energy companies had to achieve carbon savings by setting up schemes to promote and deliver energy saving measures to domestic energy users. By the end of the programme energy companies had achieved 99% of the overall targets for CERT and CESP. Individual CESP obligations were not met by British Gas, SSE, Scottish Power, Drax, InterGen and GDF Suez. In addition, British Gas did not meet its obligation for the CERT scheme.

We found five out of the six non-compliant CESP parties continued to install energy efficiency measures after the deadline as mitigation activity. Four parties delivered mitigation equivalent to their shortfall, whilst InterGen only partially mitigated their shortfall. Drax did not engage in any mitigation activity. British Gas mitigated its Cert shortfall in full. By mitigating and reducing the harm to consumers associated with their failure these companies received a reduced penalty. In addition to this mitigation activity, at the conclusion of our investigations we secured £49.7m in redress payments and imposed over £5m in penalties. The redress money has, in accordance with proposals developed by the companies under investigation, been distributed to charitable and non-profit organisations that support projects associated with energy efficiency and/or the alleviation of fuel poverty.

Complaints Handling

- In October 2014, we found EDF Energy was in breach of the Consumer Complaints Handling Regulations 2008 between May 2011 and January 2012. The investigation was prompted following an increase of over 30% in the levels of complaints during the mass-migration stages of introducing a new IT system. The contraventions included untimely handling of complaints and a deficient reporting of detail and steps taken to resolve a complaint. EDF Energy took actions to improve its compliance and was required to pay £3m in redress to Citizens Advice Energy Best Deal Extra and Plymouth Citizen's Advice Bureau.

Mis-Selling

- In July 2014, we found that E.ON had acted in breach of licence conditions relating to marketing and domestic contracts. E.ON provided misleading information to consumers and failed to have adequate management and training in place to prevent

such breaches. E.ON agreed to pay £12m to consumers through a fuel poverty package and, in addition, to directly compensate individual affected consumers where it was possible to identify them. This negotiated settlement brought direct compensation to affected consumers as well as broader benefits targeted at vulnerable consumers.

- In July 2014, following engagement with Ofgem, British Gas agreed to pay £1m in compensation after it became apparent they had mis-sold to customers in various retail outlets nationwide. As British Gas reported this issue to Ofgem and took immediate corrective action, we decided to accept this consumer package in lieu of opening a formal investigation. The consumer package comprised of a £434,000 payment to the British Gas Energy Trust and £566,000 worth of direct compensation to affected customers.

Tariff Rules

- In July 2014, ScottishPower agreed to make payments totalling £750,000 to Energy Best Deal, for failing to ensure the prices of different payment methods reflected the difference in costs to the supplier. Following a formal investigation we found such practices breached licence conditions relating to payment methods under domestic supply contracts. The agreed payment will aid consumers directly and ScottishPower has taken steps to ensure that it will comply in the future.

Switching Practices

- In May 2014, we imposed a financial penalty of £800,000 on British Gas and they also agreed to pay £3.2m into an Energy Efficiency Fund for failing to comply with provisions relating to non-domestic customer transfer blocking and contract renewal obligations. British Gas's breaches include erroneous objections to switching and failure to notify customers of expiring contracts. Preventing such practices is essential to a well-functioning market.
- British Gas Business agreed to pay £1.4m directly back to affected micro-businesses and a further £250,000 into an Energy Efficiency Fund following an informal investigation into standard licence conditions relating supply to Micro-Business customers.
- In April 2015, we completed our investigation into Spark Energy's compliance with its gas and electricity supply licences and the Gas and Electricity (Consumer Complaints Handling Standards) Regulations 2008. We imposed a financial penalty of £1 following our determination that the company had breached a number of requirements relating to domestic customer switching, transferring customers to other suppliers, billing practices and complaints handling. Spark also made a redress payment of £250,000 (less £1) in equal shares to Citizens Advice Scotland and Citizens Advice (covering England and Wales) to provide help and advice to energy consumers.

Ongoing

The following enforcement investigations are ongoing since 31 December 2013. All investigations prior to this have been closed:

- Investigation into Utilita's compliance with obligations on non-domestic customer transfer blocking (Standard Licence Condition 14 of the gas and electricity supply licences).
- Investigation into npower and Scottish Power's compliance with Standard Licence Conditions 25 and 27 and with the Gas and Electricity (Consumer Complaints Handling Standards) Regulations 2008.

- Investigation into Business Energy Solution's compliance with the requirements of conditions 7A, 7B, 7, 14 and 21B of their gas and electricity supply licences.
- Investigations in relation to the advanced meter roll out under requirements of Standard Licence Condition 12 for British Gas, E.ON and npower.
- Investigation into Economy Energy's compliance with the requirements of conditions 23, 24 and 25 of their gas and electricity supply licences in relation to marketing.
- Investigation into Spark Energy's compliance with its gas and electricity supply licences and the Gas and Electricity (Consumer Complaints Handling Standards) Regulations 2008.

For the avoidance of doubt, the fact that we have launched investigations should not in any way be taken as implying that any company has breached its obligations. As part of the investigation processes, the evidence will be examined before conclusions are reached.

3.2 Promoting Competition

Promoting competition is an important part of the regulator's role of protecting the interests of consumers, as greater competition helps to reduce consumers' energy bills. Here we report on the current state of the wholesale and retail markets in GB and the main changes in 2014, as well as our monitoring activities in both the wholesale and retail markets during the past year. As a large amount of Ofgem's engagement with the retail energy market does not distinguish between electricity and gas sectors, this is covered below. Where Ofgem does assess the electricity and gas retail sectors separately, this is noted and dealt with separately.

3.2.1 Wholesale markets

The following section provides an overview of our monitoring under article 37(1)(i),(j),(k),(l),(u) and Article 40(3), and the main developments in the wholesale electricity market in GB during 2014. Detailed information can be found in the following sections, a summary of which is presented below:

- Monthly averaged over the counter (OTC) day ahead baseload and peakload electricity prices for 2014 were down on 2013.
- Lower gas prices fed through to power via generation. Gas prices fell as high temperature in winter 2013/14 left large amounts of gas in storage. This improved the near-term supply outlook and reduced demand for summer storage injections.
- Annual churn rates for total traded volumes also increased between 2013 and 2014.
- We made a Market Investigation Reference (MIR) to the Competition and Markets Authority in (CMA) June 2014 following a public consultation. This followed the publication of the first annual State of the Market report in March 2014, in collaboration with the Office of Fair Trading (OFT) and the CMA.
- The total traded volume of wholesale electricity increased in 2014 by 14% to 1,071.7 TWh. This was driven by increases in OTC trading, but total exchange trades fell.
- Net imports along GB's interconnectors increased by almost 50% between 2013 and 2014 to 19.4 TWh. The majority of this was accounted for by increased volumes along IFA and BritNed.
- EDF again contributed the largest proportion of power generation in GB. Centrica, Drax, E.ON, RWE, Scottish Power and SSE all produced more than 5% of total GB generation.

Policy developments in several areas of GB's wholesale electricity market have continued throughout 2014. Some notable policy areas include:

- Implementing our Electricity Balancing Significant Code Review.
- Launch of registration for market participants under REMIT.
- The first auction process in the capacity market.
- Development and implementation of European Network Codes and Guidelines.

3.2.1.1 Monitoring the level of prices, the level of transparency, the level and effectiveness of market opening and competition

Prices

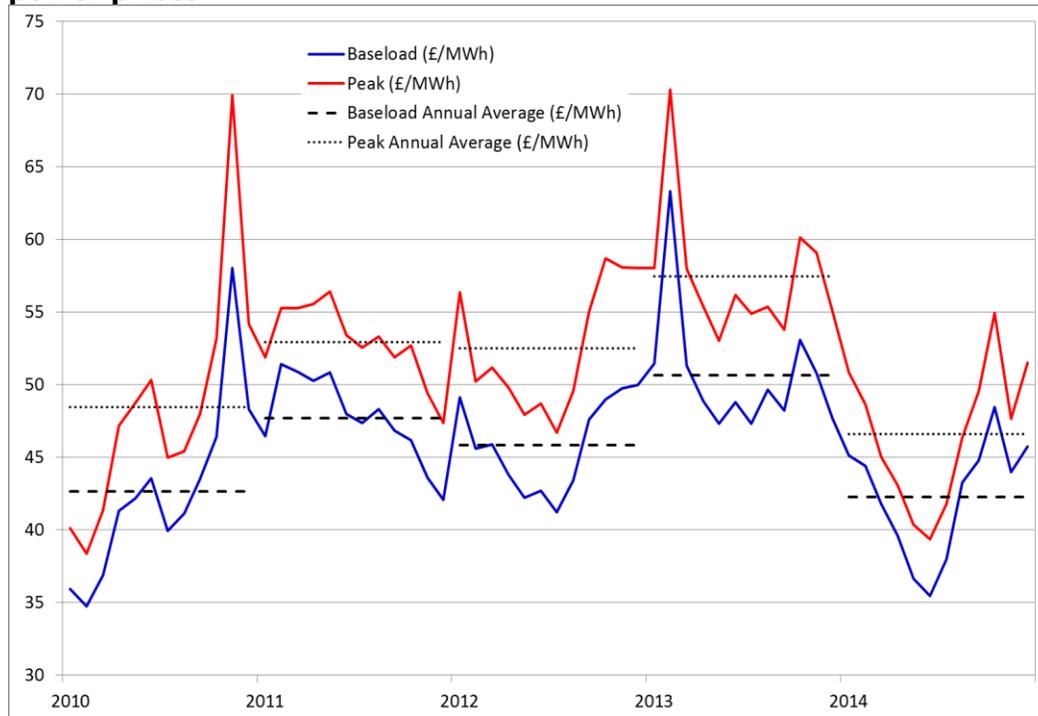
In GB wholesale prices are compiled and made available to market participants by a number of independent pricing agencies, energy market brokers, and exchanges.

Argus Media, ICIS Energy and Platts provide pricing based on reported OTC trades, and are made available to the market via subscription services. Data providers produce pricing data for a wide variety of peak and baseload contracts up to three years ahead of delivery. Real time energy broker pricing based on OTC trades is also provided via financial data providers.

Following a call for evidence, we announced in July 2014 that we would consider the outcome of two sets of proposals from the European Commission and The International Organisation of Securities Commissions (IOSCO) on financial benchmarks before deciding on our next steps. In the interim, we strongly support extending the scope of the IOSCO Oil PRA principles to price assessments for gas and electricity markets on a voluntary basis. In addition to a wide range of OTC pricing data, the three power exchanges in the GB electricity market²³ all provide pricing data to the market.

Figure 1 shows monthly averaged OTC day ahead baseload and peakload electricity prices in GB since the beginning of 2010. Average baseload and peakload prices broadly fell in 2014, and are the lowest average prices in the series. This was a result of lower gas prices feeding through to power generation as gas-fired generation continued to operate as the marginal fuel for large parts of 2014. Temperatures were above seasonal normal levels in winter 2013/14. This reduced demand for heating and left large amounts of gas in storage. This improved supply outlook coupled with reduced demand for storage injections weighed gas prices, and power prices in turn. Please see section 4.2.1 for more information on the trends in the GB gas market 2014.

²³ The APX Group, N2EX (a Nord pool Spot and Nasdaq OMX commodities joint venture) and the Intercontinental Exchange (ICE)

Figure 1: GB monthly and annual averaged Day Ahead baseload and peakload power prices

Source: ICIS Energy

Liquidity

On March 31 2014, new regulatory requirements to promote liquidity in the wholesale electricity market came into effect. We introduced these reforms, known as 'Secure and Promote', because we were concerned (as were industry participants) that low levels of liquidity were posing a barrier to effective competition. The new regulations aim to help independent suppliers to access the wholesale market and ensure that the market provides the products and price signals that all companies need to compete effectively.

The regulations include reforms to meet three objectives:

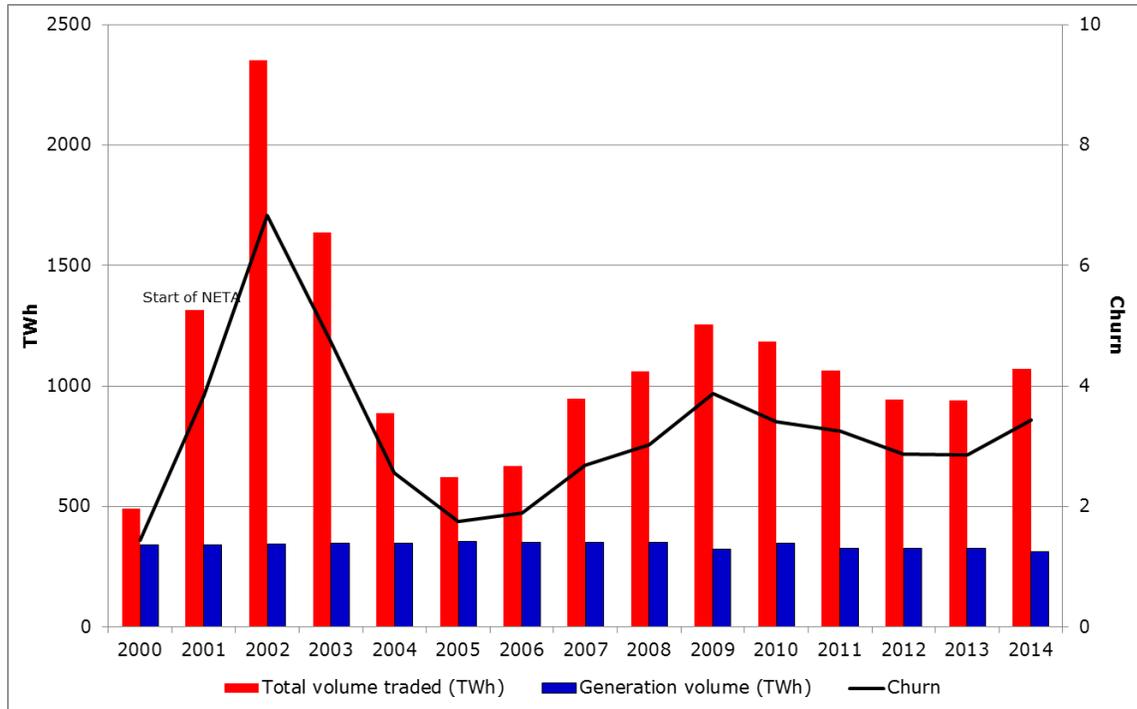
1. **A market making obligation**, which obliges firms to post prices at which they would be prepared to buy and sell electricity. The market making obligation creates more transparency in the wholesale market as participants can see prices for delivery of electricity up to two years out. This is important for building trust and confidence.
2. **Supplier Market Access rules** to improve access to the wholesale market for small suppliers. These rules ensure that the largest eight generators cannot treat requests to trade by independents as a low priority. The rules also set deadlines for them to respond to these requests.
3. **A reporting requirement** of day ahead trading of the six largest vertically integrated companies and the two largest independent generators.

We are now monitoring the effects of the reforms both to assess their impact and to make sure the obligated parties comply with them.

The results show that there has been an improvement in liquidity in the wholesale market over the period the new arrangements have been in place. Independent suppliers have

also told us that they are finding it easier to access the products they need. However, we recognise that there are other factors that could have contributed to this. Many factors can impact liquidity and it is difficult to isolate the effect of our reforms. In addition, liquidity follows seasonal trends. While there are positive signs so far, it is too early to draw more meaningful conclusions. At least a full year of data is needed. We published an Interim Report in December 2014²⁴ and will publish our first annual report by the end of summer 2015.

Figure 2: GB total traded volume, generated volume and churn ratios from 2000 to 2014



Source: ICIS Energy, APX, ICE, N2EX, DECC DUKES.

Transparency

REMIT

EU Regulation on Wholesale Energy Market Integrity and Transparency (REMIT) is a key tool in ensuring the transparency of prices within the wholesale energy market. It came into force in December 2011 and prohibits insider trading and attempted or actual market manipulation in wholesale energy markets across the EU.

In July 2014 we published an open letter on our findings of the inside information review on market participant notifications and provided some general areas which market participants might want to consider.

In August 2014, the UK government consulted on legislation to introduce criminal sanctions for the main REMIT prohibitions of market manipulation and insider trading.

In December 2014 the European Commission approved the REMIT Implementing Acts which came into force in January 2015. It sets the date for the start of transaction

²⁴ <https://www.ofgem.gov.uk/publications-and-updates/wholesale-power-market-liquidity-interim-report>.

reporting obligations of 7 October 2015 for transactions on organised market places and 7 April for off-organised market place transactions.

On 1 December 2014, we opened up REMIT registration for GB market participants. Since then, we have continued to provide support for market participants registering in GB. The registration process needs to be completed before transaction reporting begins. Also, in December 2014 we consulted on our REMIT Procedural Guidelines and Penalties Statement. This invited stakeholders to comment on proposed changes to two documents that describe how we monitor, investigate and enforce the requirements of REMIT.

We regularly discuss REMIT issues with ACER, other NRAs and financial authorities, including how best to co-operate. This will help us deal effectively with any cases that have a negative impact on wholesale energy markets in more than one EU country or which affect financial markets.

Market Opening and Competition

Market investigation referral to the CMA

In March 2014 we published our first annual State of the Market report, in collaboration with the OFT and the CMA.²⁵ On 26 June 2014, we made a MIR to the CMA after a public consultation process.²⁶ The CMA's investigation is currently in progress. The publication of provisional findings is expected in June/July and the final decision is due by the end of 2015. Please see section 3.2.2 for more details.

Wholesale Market Trading

A total of 1,071.7 TWh of wholesale electricity was traded in GB during 2014. This represents a 14% increase from 939.7 TWh of total trades in 2013.

OTC trading²⁷

Total OTC trading in 2014 rose by 137.9 TWh to 906.2 TWh, from 768.3 TWh in 2013. The proportion of the total electricity volumes which were OTC traded was broadly stable year-on-year. Around 85% of all power traded in GB was OTC traded, marginally up from 82% in 2013.²⁸

Exchange trading

Volumes traded on the exchanges decreased in 2014 to 165.5 TWh, from 171.7 TWh in 2013. A key driver of this was a fall in volumes traded on N2EX. This meant the proportion of exchange traded volumes fell to 15%.

Volumes on the APX Power UK exchange, which is usually associated with intra-day trading, rose to around 26.2 TWh 2014. This is an increase of around 15% (or 3.5 TWh) on the calendar year for 2013.²⁹

The N2EX exchange, which mainly sees day ahead and future trading, saw some broad declines in traded volumes. Volumes in its day ahead auction fell to 135.2 TWh, down 3% from 138.9 TWh in 2013. Its near-term continuous market saw larger declines as traded

²⁵ <https://www.ofgem.gov.uk/ofgempublications/86804/assessmentdocumentpublished.pdf>.

²⁶ <https://www.ofgem.gov.uk/publications-and-updates/consultation-proposal-make-market-investigation-reference-respect-supply-and-acquisition-energy-great-britain>

²⁷ Bilateral trading between two market participants or where an intermediary (the broker) brings together a buyer and seller.

²⁸ Please note, the values for 2013 have been revised compared to those published in the 2014 National Report.

²⁹ Includes both APX Continuous and Day Ahead auctions Data available from: <http://www.apxgroup.com/>

volumes fell by over 95% in 2014, from 3.5 TWh to 0.1 TWh.³⁰ This was a result of the markets being suspended by Nord Pool Spot on 1 April 2014 pending the launch of a new intra-day market on the platform.³¹

UK power futures exchange traded contracts are also available on the Intercontinental Exchange (ICE). Traded volumes on the ICE fell in 2014 to 4.0 TWh, from 6.6 TWh in 2013.

Market integration

For background information on GB interconnection, interconnection policy and market coupling please refer to section 3.1.4 of this report.

The GB market is broadly integrated with neighbouring markets with almost 4 GW³² of interconnection with three other markets. Prices for trades along these are established using market based methods. GB typically imports from France (IFA) and the Netherlands (BritNed), and exports to Northern Ireland (Moyle) and the Republic of Ireland (East-West). The Moyle interconnector continued to operate at half capacity (250 MW).³³ In 2014 we also decided to roll out the cap and floor regulatory regime to new near-term electricity interconnectors.¹⁷

IFA (2 GW) and BritNed (1 GW) are participants in the NWE Day Ahead market coupling pilot project that was launched in February 2014. Market Coupling should make sure power is produced where it is most efficient and transported to areas of consumption where it is most valued. This should lower prices for consumers and support secure and sustainable supply. Market coupling has seen an improvement in the efficiency of GB interconnector flows according to price differentials. Looking at 200 days before and after market coupling went live³⁴, the efficiency of the volume of flows along IFA increased from 92% to 99%. While BritNed efficiencies increased also from 95% to 97%. The Moyle (0.45 GW)³⁵ and East-West (0.5 GW) interconnectors will not be included as part of the market coupling pilot project.

Net imports of power along GB's four interconnectors increased between 2013 and 2014 to 19.4 TWh, an increase of almost 50% (6.4 TWh). The majority of this was accounted for by increases in net imports across IFA and BritNed, which were up by 4.6 TWh and 1.5 TWh, respectively. This could have been driven by the increasing carbon price floor in the GB market, as well as the introduction of day ahead market coupling. An increase in gross flows (both imports and exports) was also observed in 2014. These increased to 26.8 TWh in 2014 from 21.8 TWh the previous year.

In periods of high electricity demand in both GB and France during winter, IFA often exports from GB to France. But the number of occasions, or settlement periods, in 2014 which saw exports along IFA fell once again. Exports from GB to France fell from around 0.5 TWh in 2013 to close to zero in 2014, meaning almost 100% of the flows along IFA in

³⁰ Includes Prompt and Day Ahead auctions. Data available from: <https://www.n2ex.com/>

³¹ <http://www.icis.com/resources/news/2014/03/05/9759907/business-as-usual-for-uk-s-n2ex-auction-as-prompt-and-intraday-markets-set-for-revamp/>

³² This figure does not account for the fault with Moyle.

³³ Mutual Energy have announced that the cable should be back to full capacity by 2016.

³⁴ Before market coupling: 19/07/2013 - 03/02/2014. After market coupling: 04/02/2014 - 22/08/2014.

³⁵ This figure relates to export capacity. Import capacity is 0.08 GW. Note these figures do not take into account the current outage. See National Grid's Electricity Ten Year Statement for more details: <http://www2.nationalgrid.com/UK/Industry-information/Future-of-Energy/Electricity-ten-year-statement/Current-statement/>

2014 were imports. Combined exports along Moyle and East-West also fell by around 0.2 TWh to 3.5 TWh in 2014.

Market concentration

Figure 3 below shows that seven generation companies once again had market shares exceeding 5%. The largest three companies generated almost half of the electricity supplied to the GB market 2014.³⁶

Metered generation and interconnector volumes in 2014 indicate that EDF again contributed the largest proportion of power supply in GB. Based on this data, EDF's share fell year-on-year to 25% in 2014. EDF is the majority owner of most of GB's nuclear fleet which operates as baseload generation capacity. The decline could be related to the reduced output from the Hartlepool and Heysham 1 plants at the end of 2014. Centrica, Drax, E.ON, RWE, Scottish Power and SSE all produced more than 5% of total GB generation. The market share of generators outside of the largest eight also rose from around 16% last year to 20% in 2014.

Figure 3: 2014 wholesale electricity market share in GB based on metered volume

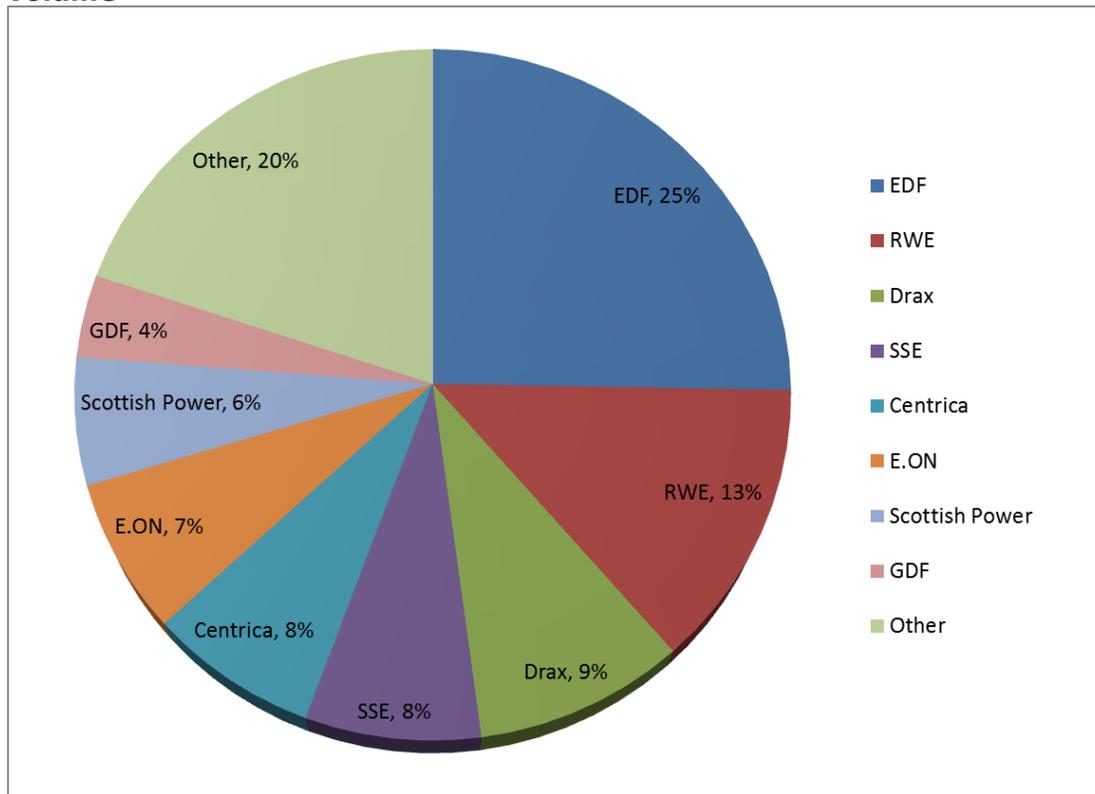


Table 1 provides the Herfindahl-Hirschman Index (HHI) analysis based on the same data as the market shares. The HHI is an indicator for the level of competition in a specific market. The largest individual HHI by capacity is EDF (HHI of 639), which is lower than 2013. The total HHI decreased to 1,144 in 2014.

³⁶ Based on metered generation volume and interconnector imports. Generation shares are based on proprietary data. Station demand has been excluded. Interconnectors were not included in the 2013 analysis.

Table 1: HHI based upon 2014 metered volume

Company	HHI
EDF	639
RWE	178
Drax	86
SSE	59
Centrica	56
E.ON	51
Scottish Power	35
GDF	15
Other	23
Total	1,144

Market power concerns in the electricity wholesale sector

The Transmission Constraint Licence Condition (TCLC) came into force on 29th October 2012. It is complementary to powers under competition law to tackle abuse of dominance. We published guidance on our intended approach to the interpretation and enforcement of the TCLC on the same date.

The TCLC prohibits generators from obtaining an excessive benefit for electricity generation in relation to periods of transmission constraints. This may occur either where a generator creates or exacerbates a transmission constraint by taking uneconomic action, or where the generator obtains an excessive financial benefit for the SO in return for reducing their generation. These behaviours can significantly increase the costs of balancing the electricity system during periods of transmission constraint.

Throughout 2014, we continued to monitor the bids and offers submitted in the balancing mechanism and generator's compliance with the TCLC. In 2014, the average price paid to onshore wind farms to reduce generation was £82/MWh compared to £88/MWh in the previous year.

The TCLC will cease to have effect 5 years after Section 18 of the Energy Act 2010 came into force on 16 July 2012. There is the possibility of a 2 year extension which would be granted by the Secretary of State.

3.2.2 Retail market

Gas and Electricity retail market overview

A large amount of Ofgem's engagement with the retail energy market does not distinguish between the electricity and gas sectors – rather, the market is considered as a whole. This is reflected below. Where Ofgem does assess the electricity and gas retail sectors separately, the information has been documented in this section and 4.2.2 respectively. The following section describes our monitoring activities of the retail market in 2014. To this purpose we look separately at the domestic and non-domestic markets and also distinguish between small and medium enterprises and large industrial consumers.

3.2.2.1 Monitoring the level of prices, the level of transparency, the level and effectiveness of market opening and competition

Monitoring the level of prices

All final consumer prices in the GB retail energy markets are determined by market forces. There are elements of the final price which are attributable to the regulated aspects of the market, in particular distribution and transmission charges, which are price controlled. Ofgem actively monitors domestic suppliers' electricity prices across GB. We receive price change notifications from suppliers but also contract with Energylinx, an independent data provider and one of the comparison sites accredited by the Confidence Code run by Ofgem. Ofgem uses this information to calculate the implications for domestic customers' retail bills based on characteristics such as their consumption level, payment type, and region fell by 1% (£6) over the year.

Figure 4 shows the change in typical domestic electricity bills in GB's electricity market for direct debit, prepayment and standard credit customers between December 2013 and December 2014. Overall, average electricity bills fell by 1% (£6) over the year.

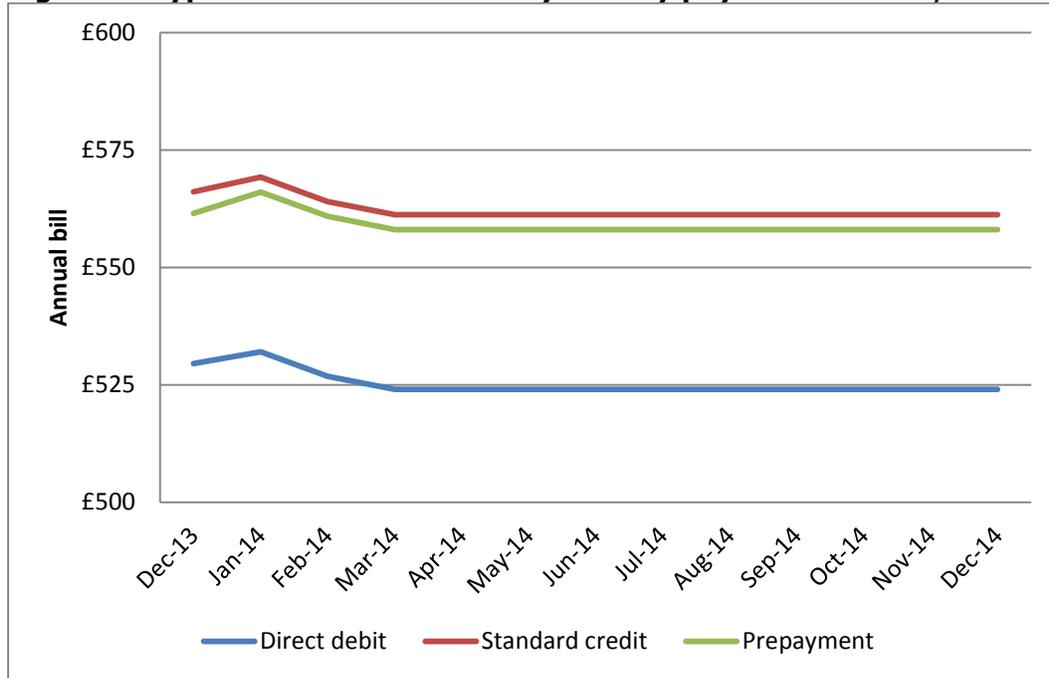
Figure 5 shows the change in typical domestic dual fuel bills in GB's dual fuel market for direct debit, prepayment and standard credit customers between December 2013 and December 2014. Overall, average dual fuel bills fell by 1.6% (£20) over the period.³⁷

During 2014, we observed an increase in the number of fixed-price tariffs that domestic energy suppliers offer, with most fixed deals being priced at a discount relative to variable tariffs. The cheapest fixed deals were generally offered by smaller suppliers. As well as monitoring domestic electricity bill levels, we also assess the extent to which particular costs have an impact on these bills. Suppliers face a range of costs that influence how they set retail electricity prices. These costs can vary within and between years, and include wholesale energy costs, the costs of UK government environmental and social policies such as the Renewable Obligation and the Warm Home Discount, and transmission and distribution costs. We use the Supply Market Indicator (SMI) (see below) to explore the relationship between retail bills and these costs.³⁸

³⁷ Change for the three payment methods was: direct debit, -0.9% (£11); prepayment, -1.8% (£23); standard credit, -2% (£26).

³⁸ <https://www.ofgem.gov.uk/gas/retail-market/monitoring-data-and-statistics/understanding-energy-prices-great-britain/supply-market-indicator>

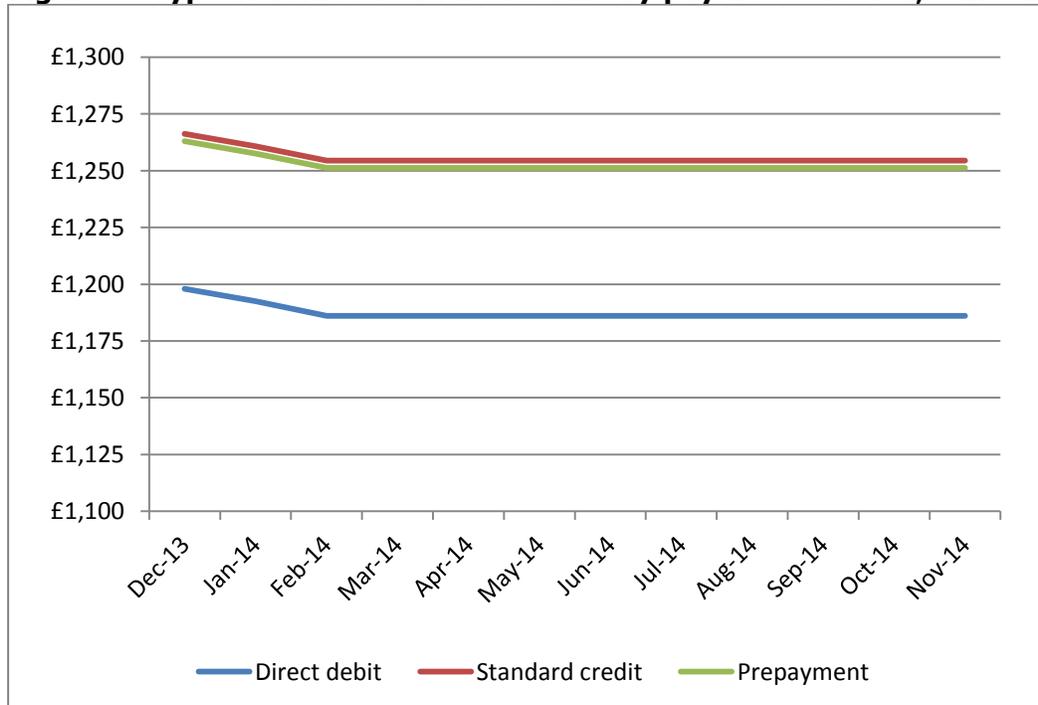
Figure 4: Typical domestic electricity bills by payment method, Jan – Dec 2014



Source: Ofgem analysis of Energylinx data

Notes: 1) Average of Big six's standard tariffs, 2) Revised consumption level: 3,200 kWh per year

Figure 5: Typical domestic dual fuel bills by payment method, Jan – Dec 2014



Source: Ofgem analysis of Energylinx data

Notes: 1) Average of Big six's standard tariffs, 2) Revised consumption level: 3,200 kWh per year

Monitoring Transparency

Under Article 37(1)(i) Ofgem is committed to ensuring the energy market is transparent to the benefit of consumers. In this section, we explain the rules in place regarding the transparency of suppliers' activities and how we have monitored compliance in 2014.

Financial transparency

Over the last five years, we have taken measures that have significantly improved the transparency of revenues, costs and profits. Since 2009 we have required large, vertically-integrated suppliers to publish annual Consolidated Segmental Statements (CSS) on their websites. These Statements provide a breakdown of suppliers' revenues, costs and profits and are reconcilable to audited accounts. Ofgem produces an annual summary of the Statements, the archive of which can be found on our website.³⁹

Since 2014, we have made a number of improvements to the reporting requirements for the Statements. We now require companies to audit their statements, to publish them sooner, to provide greater cost breakdown, and to provide greater insight into their trading activities. We also commissioned an in-depth review of the large companies' transfer pricing policies in 2014 which concluded that they were appropriate and in line with global accounting standards.

To complement the backward-looking CSS, since 2009 we have published a 12-month forward look at cost trends through our SMI on a regular basis (currently every month). It looks at the average annual bills for consumers and estimates the annual cost per customer faced by a typical large supplier to deliver gas and electricity for the following 12 months. This helps make trends in costs and bills clearer to consumers. We keep the methodology under continuous review and update our assumptions as circumstances change.

Transparency for domestic consumers

As part of the measures to increase transparency set out in our Retail Market Review (RMR) reforms, we required suppliers to inform their customers about their cheapest tariff in their bills and other communications. We are now proposing that suppliers inform their customers of the cheapest tariff, whether under a white label brand or the licenced supplier's brand.⁴⁰ Suppliers will have to inform customers on their own brand tariffs if a white label branded tariff is cheaper, and correspondingly, customers on a white label-branded tariff will have to be informed if a tariff of the licenced supplier is cheaper.

In December 2013, we introduced tariff simplification rules under the RMR. The rules were aimed at making the market simpler and facilitating consumers' ability to compare deals in order to choose the best energy tariffs for their needs and in 2014 we have closely monitored compliance with these rules. In addition, we actively monitor supplier compliance with our 'Clearer Information' reforms introduced in March 2014, to ensure that consumers are being provided with information to engage with their supplier and the energy market.

In GB, consumers can compare suppliers' gas and electricity prices using a wide range of online energy price comparison websites. Ofgem currently administers a code of practice,

³⁹ <https://www.ofgem.gov.uk/electricity/retail-market/monitoring-data-and-statistics/understanding-profits-big-energy-suppliers>

⁴⁰ A white label provider is an organisation that does not hold a supply licence and instead partners with a licenced supplier. Under the arrangement, the licenced supplier offers gas and/or electricity using the brand of the white label provider.

the 'Confidence Code'.⁴¹ This ensures that consumers can use a site they trust to provide accurate and reliable pricing information. In 2015 we made changes to the Confidence Code which will further strengthen requirements on accredited price comparison services to provide accurate and reliable price comparisons.

As part of changes to embed the principle of transparency within the Confidence Code, accredited sites must show all tariffs available in the market unless the consumer actively chooses a bespoke view by filtering by a particular tariff or aspect of service, for example. Accredited comparison services must also be transparent about how they operate, for instance explaining whether they have any commission arrangements with suppliers.

In addition, we consider that effective information exchange between suppliers and Third Party Intermediaries (TPIs) is important in ensuring that consumers have a positive experience when engaging in the energy market. In 2015 we released an open letter⁴² which clarifies existing licence conditions related to supplier provision of tariff data to TPIs. This will help TPIs to support consumers in more confidently engaging in the market.

Transparency for non-domestic consumers

Our research has shown that some businesses experienced a lack of transparency and clarity in the information provided on bills by their supplier. Since 31 March 2014, suppliers have to make sure all their bills and statements clearly show the contract end date and the deadline for giving notice. We've also stopped suppliers setting narrow periods for allowing customers to end contracts. Micro-businesses can now give notice at any time. Additionally, we reviewed the rules on automatic rollovers which apply when a micro-business reaches the end of a fixed-term contract and is moved to a new tariff. We concluded that auto rollovers can continue but have introduced new rules to simplify the contract renewal process for micro-business consumers. From 30 April 2015 suppliers must:

- allow micro-businesses to give no more than 30 days' notice to end a contract
- include current prices and annual consumption on renewal letters for fixed-term contracts, and
- acknowledge termination notice within five working days of receipt

We are also working on how best to increase the transparency of non-domestic TPIs' activities. TPIs act as brokers between non-domestic customers and suppliers, assisting customers in finding the most appropriate energy deal for their needs. However, our 2014 consultation⁴³ found continued evidence that TPIs are not always delivering the best outcomes for consumers, for example companies pressurising customers into accepting unnecessary long-term contracts. To enhance safeguards for these consumers, we've developed a draft code of practice for non-domestic TPIs and are considering the detailed requirements of the code. We propose to prevent suppliers from providing tariff information to any TPI that doesn't comply with this code. We published an open letter⁴⁴ on ways forward for the TPI sector in August 2014.

⁴¹ <https://www.ofgem.gov.uk/information-consumers/domestic-consumers/switching-your-energy-supplier/confidence-code>

⁴² <https://www.ofgem.gov.uk/publications-and-updates/information-flows-between-suppliers-and-third-party-intermediaries-tpis>

⁴³ [Proposals for regulation non-domestic TPIs](#)

⁴⁴ <https://www.ofgem.gov.uk/ofgem-publications/89218/non-domestic-tpi-copopenletterpublish.pdf>

Monitoring the effectiveness of market opening and competition

Ofgem monitors the effectiveness of market opening and competition in retail markets, through regular data collection of market participants. We publish our analysis in monitoring reports and also commission consumer research to inform our view of the market. Here we report on our monitoring activities during 2014 on the following: complaints, disconnections, maintenance services, market shares, switching rates, contractual practices and data exchange.

During 2011-2012 we carried out the RMR, in which we set out our finding that a large proportion of consumers were disengaged from the energy market, potentially weakening competitive pressure on suppliers. A main cause of disengagement was the complexity of tariffs and lack of trust in the market. Thus, in 2013 we implemented retail market reforms⁴⁵ that are aimed at making the market simpler, clearer and fairer for consumers. The majority of these policies entered into force between 31 December 2013 and 31 March 2014. The final set of measures requiring suppliers to move consumers off expensive 'dead' tariffs came into effect on 30 June 2014, which was the deadline for suppliers to move consumers off expensive dead tariffs.⁴⁶

In March 2014 we published our first annual State of the Market report, in collaboration with the OFT and the CMA.⁴⁷ On 26 June 2014, we made a market investigation reference (MIR) to the CMA after a public consultation process.⁴⁸ The purpose of a MIR is for the CMA to investigate whether there is any feature, or combination of features, of a market in the United Kingdom for goods or services prevents, restricts, or distorts competition.

The decision was made on the basis that we had reasonable grounds to suspect that there were features of a market which were harming competition. This was due to the findings of our assessment that demonstrated that competition is not working as well as it should for consumers. It showed increasing distrust of energy suppliers, uncertainty about the relationship between the supply businesses and the generation arms of the six largest suppliers, and rising profits with no clear evidence of suppliers reducing their own costs or becoming better at meeting customer expectations.

The CMA's investigation is currently in progress. The publication of provisional findings is expected in June/July 2015 and the final decision is due by the end of 2015.

Complaints by household consumers

Ofgem does not directly investigate domestic customer complaints. If a consumer wishes to make a complaint about an energy supplier or network operator, they should contact the relevant company in the first instance. Suppliers are required to meet complaints handling standards set by Ofgem for dealing with and processing customer complaints.⁴⁹ Information about how to make a complaint is on the back of the energy supplier's bill and on energy company websites. If the energy company cannot resolve a complaint by the end of the day after it was received, it must tell the consumer that it has a complaints procedure, where it is on the website, and offer to send a copy. The complaints procedure must provide for an internal review of the complaint and the remedies available including compensation.

⁴⁵ <https://www.ofgem.gov.uk/electricity/retail-market/market-review-and-reform/retail-market-review>

⁴⁶ This is defined as a tariff in respect of an Evergreen Supply Contract which is not a Live Evergreen Tariff.

⁴⁷ <https://www.ofgem.gov.uk/ofgempublications/86804/assessmentdocumentpublished.pdf>

⁴⁸ <https://www.ofgem.gov.uk/ofgempublications/86807/consultationpublish.pdf>

⁴⁹ The complaint standards are prescribed by 'The Gas and Electricity (Consumer Complaints Handling Standards) Regulations 2008' which came into force on 1 October 2008.

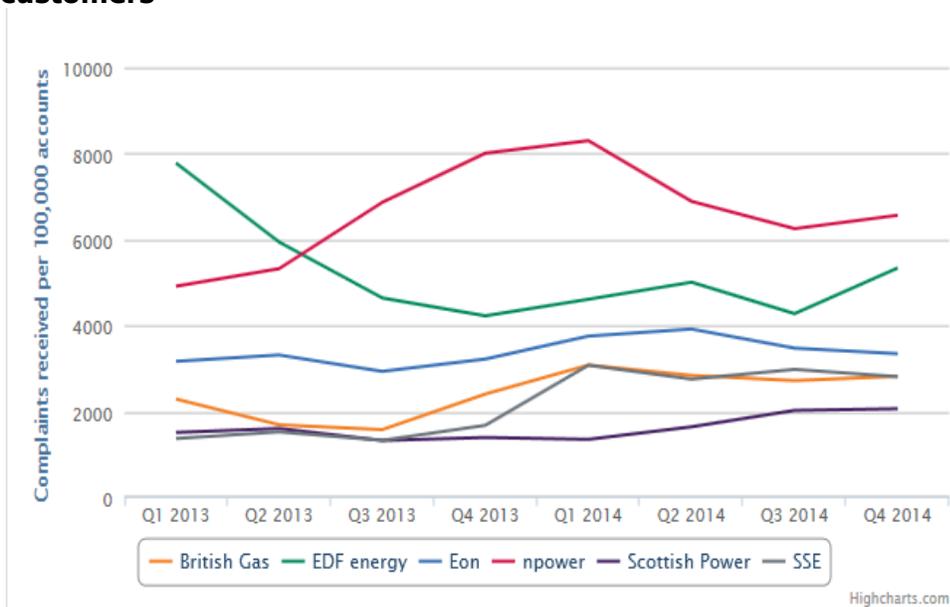
If a vulnerable consumer needs help with their complaint or a consumer has been disconnected or has been threatened with disconnection, they can go to Citizen’s Advice Extra Help Unit. Citizens Advice also provides telephone and online assistance for all consumers. Contact details for Citizens Advice are on the back of energy suppliers’ bills and on energy company websites.

All domestic energy suppliers are required to be members of the statutory redress scheme approved by Ofgem. If a complaint is not resolved to the consumer’s satisfaction and either eight weeks have passed since the complaint was made or it has reached a point of deadlock (where the energy company says it can do no more to resolve the complaint), it must write to the consumer to tell them they can seek redress through the Ombudsman (independent dispute resolution service). Information about the Ombudsman is also on the back of energy suppliers’ bills and on energy company websites. The Ombudsman is independent of the energy companies and free of charge to the consumer. Its decisions are binding on the energy company but not the customer and the Ombudsman has the power to make a financial award to the customer of up to £10,000.

The Ombudsman received over 52,000 complaints in 2014 compared with 17,000 in 2013. The Ombudsman will publish complaints data by individual energy companies later this year.

All domestic suppliers publish their complaints data in a common format agreed with Ofgem on their websites. Figure 6 below shows that complaints per 100,000 customers have increased for the former incumbent suppliers over 2014, and that RWE npower remains the most complained about company on this measure. Complaints per 100,000 customers received by the largest independent suppliers are generally lower than for the former incumbents.

Figure 6: Largest suppliers: Complaints received by company per 100,000 customers



We have published our latest research into customers' satisfaction with suppliers' complaints handling. Following the disappointing results, we required the former incumbent suppliers to detail on their websites their plans for improving complaints handling and to audit their processes for the closure of complaints. We will be monitoring the progress of their plans for improvement, and repeating the research in 2016.

Disconnections for debt

We require suppliers to provide us with information about disconnections for debt as part of their Social Obligations Reporting. Monitoring supplier performance in this area allows us to identify issues of concern with supplier performance and take action.

Charges for and the execution of maintenance services

To assess performance, the electricity and gas distribution networks are required to submit regulatory returns on an annual basis providing relevant cost, volume and output information to Ofgem. A component of the DUoS charges that all customers pay as part of their energy bills reflect the costs associated with the volume of maintenance work undertaken.

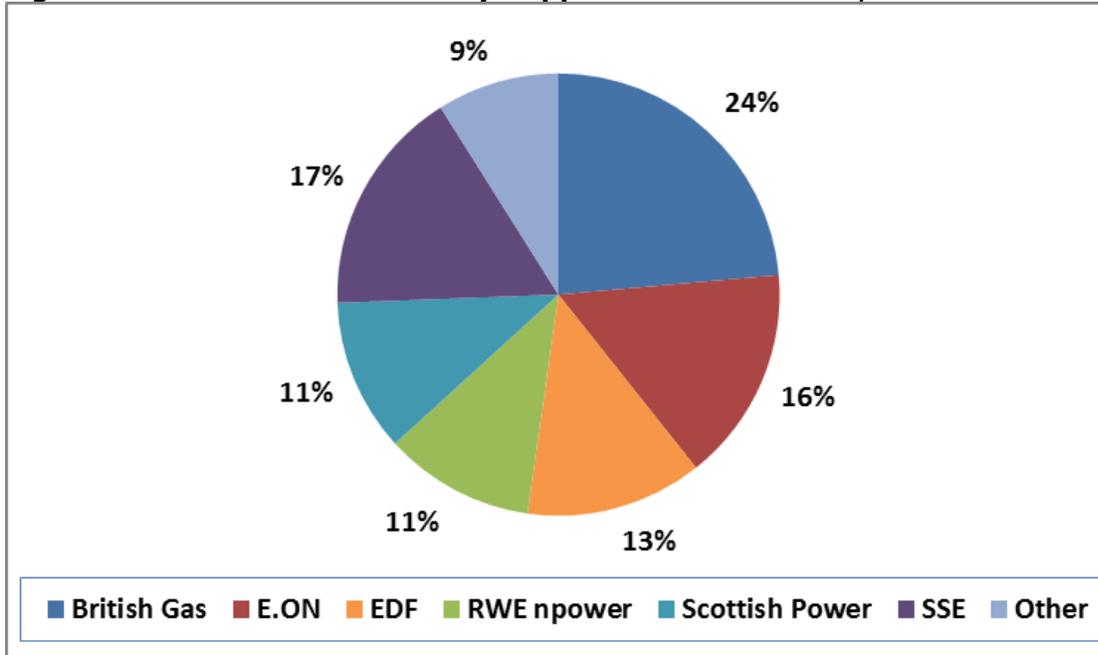
Domestic market shares

In December 2014 there were 27.6m domestic electricity consumers in GB. As Figure 7 shows, the largest six suppliers (British Gas, SSE, E.ON, EDF and RWE Npower) supplied 91 per cent of these customers.

The 18 smaller suppliers active in the domestic segment had a combined market share of 9 per cent in December 2014. These are: Axis Telecom; Co-Operative Energy; Economy Energy; Ecotricity; E(Gas & Electricity); Extra Energy; First Utility; Flow Energy; Ganymede Energy Supply (LoCO2); Gnergy; Good Energy; Green Energy; Green Star Energy; iSupply Energy; OVO Energy; Spark Energy; Utilita and Utility Warehouse. The recent growth of smaller suppliers is an encouraging development.

As a group, their market shares increased by four percentage points between December 2013 and December 2014. More stable conditions in wholesale markets and the exemption from some environmental charges for smaller suppliers are among the main drivers for the observed growth.

The figures relating to the national market shares do not reveal regional characteristics of the electricity market, which are a legacy of the regional monopolies that existed in the electricity sector prior to market liberalisation. The former electricity incumbents retain, on average, a market share of 30 per cent in their home regions.

Figure 7: GB Domestic Electricity Suppliers' Market Share, December 2014

Source: Ofgem analysis of DNOs' data

Non-domestic market shares

We also regularly monitor non-domestic suppliers' market shares.⁵⁰ The six largest suppliers of the domestic market have a lower presence in the non-domestic market, which has seen a significant entry of independent suppliers since 2008. In the segment of non-domestic sites with non-half hourly meters, which mostly correspond to small businesses, the aggregate market share of the largest six suppliers was 87%, down from 92% in 2013. In the segment of the larger non-domestic sites, those with half hourly meters, the joint market share of the largest six suppliers was 77%, down from 78% in 2013.

In 2014 independent suppliers supplied 13 per cent of non-half hourly sites and 22 per cent of half hourly sites.

⁵⁰ The data presented in this report are based on number of supply points. However, it should be noted that market shares by volume may show a different story as some suppliers may have a low number of supply points which have however very high volumes of energy supplied.

Table 2: Electricity suppliers' non-domestic market share in December 2014

Electricity supplier	Non-Domestic Sites		
	Non-half hourly	Half hourly	All Non-Domestic
British Gas	19.3%	5.5%	18.5%
E.ON	17.4%	12.9%	17.1%
SSE	16.5%	13.5%	16.3%
RWE npower	13.1%	21.1%	13.5%
EDF	12.8%	20.0%	13.2%
Scottish Power	7.9%	4.4%	7.7%
Opus	7.0%	2.2%	6.7%
Haven Power	1.3%	5.6%	1.5%
Total Gas and Power	1.2%	3.2%	1.3%
BES Commercial Electricity	1.1%	0.0%	1.0%
Utility Warehouse	0.8%	0.0%	0.7%
Extra Energy	0.4%	0.0%	0.4%
Dual Energy	0.4%	0.0%	0.4%
Ecotricity	0.3%	0.2%	0.3%
Gazprom	0.1%	1.4%	0.2%
Good Energy	0.1%	0.8%	0.2%
Green Energy	0.1%	0.1%	0.1%
Green Star Energy	0.1%	1.0%	0.1%
GDF Suez	0.1%	3.7%	0.3%
Smartest Energy	0.0%	3.1%	0.2%
LoCO2	0.0%	0.2%	0.0%
Power4All	0.0%	0.5%	0.0%
Others	0.2%	0.5%	0.3%
Total	100.0%	100.0%	100.0%

Source: Ofgem analysis of DNOs data

HHIs

HHIs⁵¹ are often used to gauge market concentration. Though HHIs do not provide conclusive evidence on the level of competition, they offer pointers as to whether there are potential risks to the market not delivering competitive outcomes. The relevant HHIs for electricity in December 2014 were as follows (2013 figures in brackets):

- domestic: 1,574 (1,636)
- non-domestic, non-half hourly metered sites: 1,395 (1,660)
- non-domestic, half hourly metered sites: 1,322 (1,273)

In comparison with 2013, the HHIs for the domestic and non-domestic non-half hourly metered sites have fallen, while the HHI for the non-domestic half-hourly metered sites has increased slightly. All three electricity markets are judged to be 'concentrated' according to the threshold HHI levels (1,000) used by the CMA.

⁵¹ HHI is commonly used to assess market concentration, ranging from 10,000 for a monopoly to just above zero for perfect competition. The Competition Markets Authority in the UK categorize a market as 'concentrated' if its HHI exceeds 1,000 and 'highly concentrated' if its HHI exceeds 1,800.

Domestic switching rates

Consumers' ability to switch their energy supplier is important for a well-functioning, competitive energy market, although it must not be considered in isolation. Ofgem monitors switching rates together with pricing and market structure data on an ongoing basis.

In 2014, 3.1m domestic consumers switched their electricity supplier, equivalent to an average of approximately 251,000 per month. This represents an annual switching rate of 11.1 per cent, 0.7 per cent lower than observed in 2013. We also saw an increase in switching away from the six largest suppliers, an average of 47.5 per cent of customers that switched during 2014 moving to smaller suppliers.

We also noted an increase in customers switching internally to different tariffs, payment methods and type of account management with their existing supplier. The rate of total internal switching was approximately four times higher than external switches for Q4 2014. Internal switches representing an active tariff choice (rather than automatic tariff switching at the end of a contract) were approximately double the rate of external tariff switching.

The speed and reliability of switching is also important (see chapter 5.1 for our change of supplier project within our smarter markets programme of reforms). In December 2014, the system average time⁵² to complete a switch was down to 16 days in electricity (from 18 days in June and September).

Our consumer surveys provide an additional source of information on the consumer switching experience. The Ipsos Mori Tracking Survey 2014⁵³ found that 61 per cent of electricity customers could not recall ever having switched supplier, down from 65 per cent in 2012.

Consumer survey data also shows that 13 per cent customers reported having switched electricity supplier in the last year, a slight increase from the previous year. From those who did not switch suppliers in the last year, 10 per cent changed tariffs, and 3 per cent changed payment methods within their own supplier. Most of the switchers did so to save money.

Our consumer surveys show that most of those who switched did so to save money. In the TNS survey⁵⁴ we find that 46 per cent of consumers feel that it's hard to work out whether they will save or not by switching, 45 per cent believe there are no real differences in prices across suppliers, and 47 per cent believe that switching is a hassle that they do not have time for. Moreover, many consumers continue to distrust energy suppliers to treat them fairly.

Non-domestic switching rates

In March 2015 we published our quantitative survey on micro and small business consumer engagement.⁵⁵ It showed that around one in four smaller business customers

⁵² This is the average number of calendar days from the day when the supplier notifies the switching request to the network operator system until the day the switch is executed.

⁵³ <https://www.ofgem.gov.uk/ofgem-publications/88375/customerengagementwiththeenergymarket-trackingsurvey2014finalpublished2662014.pdf>.

⁵⁴ <https://www.ofgem.gov.uk/publications-and-updates/domestic-retail-market-review-%E2%80%93-evaluation-framework-and-baseline-results>.

⁵⁵ [Micro and Small Business engagement in the Energy Market 2015. Quantitative Research Report.](#)

(23 per cent) reported having switched suppliers in the last year, rising to nearly three in five (60 per cent) over the last five years.

Businesses appear to be making informed switching decisions. Respondents who had switched over the last five years reported that, on average, they had contacted more than three suppliers directly or via energy brokers.

Non-domestic switching is primarily price-driven and cost saving was by far the most likely reason for switching (78% of those who had switched in the last 5 years found or were offered a lower price contract or tariff the last time they switched). Receiving a renewal notice from an existing supplier was a significant trigger for switching (47% citing this as a reason), as was the recommendation from a broker (31%). This research also showed that two in five smaller businesses have never considered switching.

Among businesses that have not switched in the last 5 years, satisfaction with the current supplier was a key reason for not switching (60% of non-switchers). Being tied to an existing contract was also significant (41%). A minority of around one in five cited the perceived complexity and the time it takes to switch (19%) and scepticism of the savings that could be made from switching (19%) as reasons for not switching.

Consumers and suppliers have also expressed concerns that transfer blocking ('Objections') rules set out in licences and industry codes are not adhered to in some circumstances. The impact of objections can be significant for consumers.

Ofgem has proposed to lead the industry towards reliable next day switching by 2019. We want to take a fresh look at whether objections should be part of a redesigned switching process or whether suppliers should develop other ways of managing risk. This work has commenced with a recent call for evidence.

Contractual practices

Under article 37(1), paragraphs (k) and (l), Ofgem is required to monitor restrictive contractual practices and ensure contractual freedom. We have dedicated Retail Markets and Enforcement teams that engage with a variety of stakeholders, ensuring that we are both proactively monitoring the market, and that we are open to any issues that may be brought to our attention. Additionally, the suppliers' licences contain conditions relating to the provision of clear contractual information to household and small business consumers.

Household customers are also protected by the general national rules which transpose Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts. These rules are set out in the Unfair Terms in Consumer Contracts Regulations 1999 (UTCCRs) and UCTA (Unfair Contract Terms Act 1977) and Ofgem is one of the public bodies with enforcement powers. The new Consumer Rights Bill, which is likely to enter into force in October 2015, will make changes to the law regarding unfair terms by consolidating the UTCCRs and UCTA into one new Act and provide some additional consumer protection via new provisions. In addition, in respect of special types of contract that are deemed by national law to exist between a supplier and customer, there are bespoke rules in place which protect both household and business customers from unduly onerous terms.

Compatibility of data exchange processes

Under Article 37(1)(u), Ofgem is required to contribute to the compatibility of data exchange processes for the most important market processes. All licenced suppliers and

network operators must comply with industry codes (changes to which must be approved by Ofgem) in order to operate in the gas and electricity markets.

As described in more detail in Chapter 5.1, access to consumption data from smart meters is managed centrally, through the Data and Communications Company (DCC), monitored by Ofgem.

3.2.2.2 Recommendations on supply prices, investigations and measures to promote effective competition

Supply prices

All final consumer prices in the GB retail energy markets are determined by market forces. All price controls on final consumer prices were lifted by April 2002. Retail prices can be affected by numerous costs, including wholesale energy prices, costs associated with environmental and social programmes such as Renewable Obligation Certificates⁵⁶ and the Warm Home Discount,⁵⁷ and transmission and distribution costs.

As a result electricity prices in the supply market are not within Ofgem's direct control and we do not make annual recommendations on supply prices nor provide these to the competition authorities. Ofgem's primary role is to protect the interests of present and future consumers. By fulfilling this role we aim to ensure the electricity and gas markets deliver the best outcomes for consumers. Through our licence conditions, our market monitoring activities and our regular market reviews, as described above, we aim to ensure supply prices comply with the relevant paragraphs in Article 3 of the Electricity and Gas Directives.

Investigations

The Authority has concurrent competition and consumer protection powers with the CMA. We will work with the CMA going forward, including as members of the United Kingdom Competition Network which aims to promote best practice and co-ordination between the sectoral regulators in the use of their concurrent competition powers.

Measures to promote effective competition/ monitoring distortions or restrictions of competition

The previous sections have outlined both our State of the Market Assessment and our regular ongoing monitoring activities in respect of assessing distortions and/or restrictions of competition. These work streams are helping us to identify where further intervention in the market is needed to promote effective competition and improve outcomes for consumers. section 3.1.5 shows our cross-cutting (gas and electricity) enforcement cases.

⁵⁶ <http://www.ofgem.gov.uk/Sustainability/Environment/RenewablObl/Pages/RenewablObl.aspx>.

⁵⁷ <http://www.ofgem.gov.uk/Sustainability/Environment/WHDS/Pages/WHDS.aspx>.

3.3 Security of supply

Under Article 4 of the Electricity Directive, Member States have to ensure the monitoring of security of supply issues.

No single body is responsible for ensuring security of supply in GB as we rely on the market to provide us with this. However the Government sets overall energy policy on energy security. Ofgem is responsible for regulating the market and National Grid, as operator of GB electricity system has responsibility for ensuring that supply meets demand on a minute-by-minute basis each day.

The Third Package does however put an obligation on NRAs to monitor investment in generation capacities in relation to security of supply. We therefore review NGET's annual Electricity Ten Year Statement⁵⁸ and UK Future Energy Scenarios documents,⁵⁹ which outline detailed electricity demand and generation (closure and investment) projections, and other relevant publications by NGET. We have also published in 2014 an annual Statutory Security of Supply Report⁶⁰ jointly with DECC, which analyses the availability of electricity and gas for meeting the reasonable demands for energy of consumers in GB.

Here we report on our monitoring activities with regard to generation capacity (and investment in it) and the balance of supply and demand during 2014.

Generation capacity

Total installed transmission capacity on the GB system for 2014/15 was expected to fall to 76.3 GW, down 3.0 GW from 2013/14. The fall was mainly driven by drops of 2.3 GW and 1.9 GW in coal and gas-fired generation, respectively. These plants were expected to close due to a mixture of environmental legislation, unfavourable generation economics and fuel-type conversions. This expected capacity decline could partly be offset by increases in biomass (0.6 GW), offshore wind (0.5 GW) and onshore wind (0.1 GW).

Expectations for 2014/15 were more positive when considering generation not connected to the transmission network, or 'embedded' generation.⁶¹ Total capacity was expected to increase year-on-year to reach 13.3 GW by 2014/15. This is an increase of 1.2 GW, which is mainly driven by solar. Falling installation and unit costs have created this growth despite falling subsidies. However, distributed and micro generation capacity typically has lower availability rates and has an intermittent output. Due to the way it is connected to the networks, generation from these plants is seen as a reduction in transmission connected demand. These characteristics can create new challenges for the SO.

The expected decline in thermal generation capacity connected to the transmission network led to a deterioration in the supply-side outlook for winter 2014/15. For more information on this, please see the *Capacity Assessment* section below.

Demand

Peak power demand on the transmission network was lower in 2014 than 2013. Actual maximum demand for 2014 (including station load, pumped storage and

⁵⁸ <http://www.nationalgrid.com/uk/Electricity/ten-year-statement/current-elec-tys/>.

⁵⁹ <http://www2.nationalgrid.com/uk/industry-information/future-of-energy/future-energy-scenarios/>.

⁶⁰ http://www.decc.gov.uk/en/content/cms/meeting_energy/en_security/sec_supply_rep/sec_supply_rep.aspx#.

⁶¹ This is distributed and micro generation in the Gone Green scenario in National Grid's 2014 UK Future Energy Scenarios.

interconnectors)⁶² fell by 4.3 GW to 52.2 GW. This trend is also seen in peak demand excluding station load, pumped storage and interconnectors,⁶³ which fell by 4.5 GW to 50.9 GW in 2014. These values are not weather corrected meaning they don't necessarily represent structural changes in demand. In this case, increased temperatures between winters were key drivers of the fall. Temperatures in winter 2012/13 averaged 3.3°C, but rose sharply to average 5.2°C for winter 2013/14.⁶⁴ Increased embedded generation⁶⁵ and energy efficiency measures could have also contributed.

There have also been falls in minimum transmission demand, which can create challenges for the SO. When station load, pumped storage and interconnectors are included, demand fell by 1.6 GW to 19.3 GW. A smaller fall of 0.5 GW to 18.1 GW was observed when station load, pumped storage and interconnectors were excluded.

Statutory Security of Supply Report

In October 2014 we published our joint Statutory Security of Supply Report (SSSR)⁶⁶ alongside DECC. This is part of an obligation on us and government to report annually to Parliament on the availability of electricity and gas for meeting the reasonable demands of consumers in GB. The report noted that GB's electricity system has delivered secure supplies to date, while facing significant challenges of decarbonisation and replacing ageing and polluting plants. The report also noted that developments over the last twelve months have significantly decreased the risk of customer disconnections.

The SSSR also focused on our Capacity Assessment report and the Capacity Market. Details on both are below.

Capacity Assessment

The Energy Act 2011 amended the Electricity Act 1989 (by inserting a new section (47ZA) into it) and introduced an obligation on Ofgem to provide the Secretary of State with a report assessing plausible electricity capacity margins and the risk to security of supply associated with each alternative. But after the publication of our 2014 Capacity Assessment this obligation was removed.

After the 2013 capacity assessment report, two measures were introduced to reduce the risk to customer disconnections:

- We have approved new balancing services (Supplemental Balancing Reserve and Demand Side Balancing Reserve) that National Grid can use to help balance the system when margins are tight.
- The Government has also introduced the Capacity Market to reduce risks to security of supply in the medium term and beyond. In addition, the Government has set the level of resource adequacy to determine how much to procure, the Reliability Standard.⁶⁷

⁶² Total Gross System Demand (TGSD).

⁶³ Initial Demand Outturn (INDO), based on National Grid operational generation metering.

⁶⁴ This is based on Met Office winter assessments which cover December, January and February.

⁶⁵ Embedded generation can meet local supply needs, therefore reducing transmission demand and less power is required from this network.

⁶⁶ <https://www.gov.uk/government/publications/statutory-security-of-supply-report-2014>

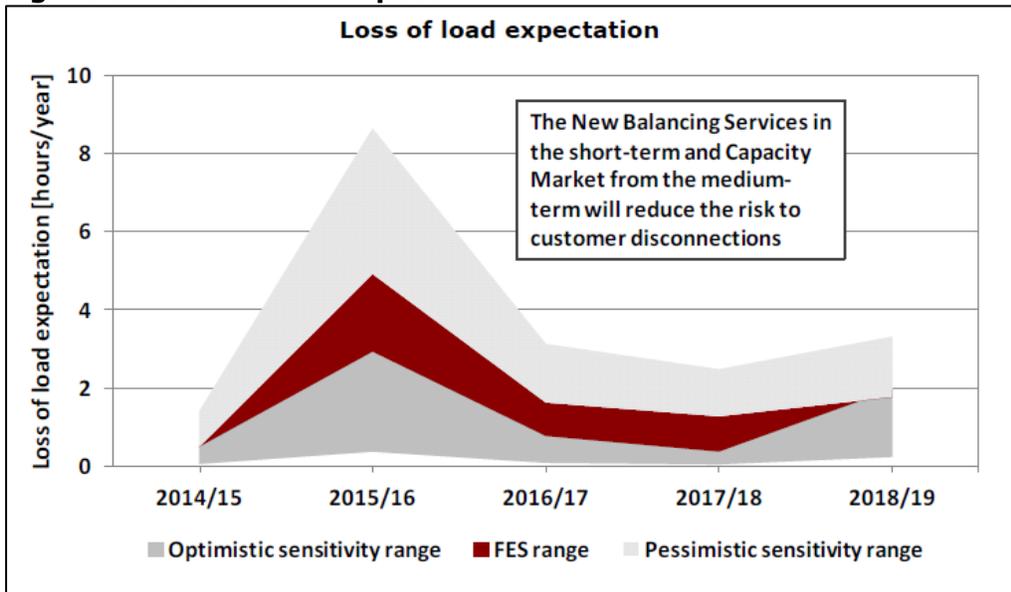
⁶⁷ The Reliability Standard is set at 3 hours loss of load expectation per year.

Our 2014 Capacity Assessment report assessed the risks to the security of GB's electricity supply over the winters 2014/15 to 2018/19. The main purpose of this report is to illustrate the levels of security that could be delivered by the market alone, and inform Ofgem's and the government's decisions on security of supply. We also analysed the potential impact of the New Balancing Services on the risk to customer disconnections.

The report showed, in the absence of the measures taken by National Grid, Ofgem and the Government, the outlook for security of supply over the next five winters is largely similar to the one we presented in our 2013 report.⁶⁸ We expect a reduction in de-rated margins⁶⁹ over the next two winters, with de-rated margins dropping to their lowest level in 2015/16, driven by a reduction of electricity supplies from conventional generation. De-rated margins are then expected to improve as new conventional plants comes online and some mothballed plants return to the market.

Figure 8 depicts the Loss of Load Expectation (LOLE) over the next years. The LOLE is the average expected number of hours per year in which supply is expected to be lower than demand under normal operation of the system. As de-rated margins drop in the mid-decade, the LOLE is projected to increase to a maximum of around 9 hours in 2015/16, before it drops to a maximum of around 3 hours for the last three winters of the analysis. For the optimistic range the LOLE remains at approximately zero levels for the entire period.

Figure 8: Loss of Load Expectation



Source: Electricity Capacity Assessment Report 2014

We also estimate the risk of customer disconnections. The likelihood of controlled disconnections without the new balancing services would vary between about 1 in 8 to 1 in 4 years in 2015/16 for National Grid's future energy scenarios. However, if National Grid procured the maximum volume of new balancing services it has indicated for 2015/16, the

⁶⁸ <https://www.ofgem.gov.uk/publications-and-updates/electricity-capacity-assessment-report-2013?docid=5&refer=Markets/WhIMkts/monitoring-energy-security/elec-capacity-assessment>.

⁶⁹ is the average excess of available generation over peak demand. These could vary between around 2% and 8% in 2015/16. We then expect them to increase to a minimum of around 3% for the pessimistic range and above approximately 8% for the optimistic range, for the rest of the analysis period.

additional measures would reduce the risk of disconnections to up to around 1 in 73 to 1 in 31 years for the future energy scenarios.

Electricity Market Reform

Electricity Market Reform is a government policy to incentivise investment in secure, low-carbon electricity, improve the security of GB's electricity supply, and improve affordability for consumers. The key elements of this reform are being delivered through four key mechanisms:

- The Capacity Market (CM), to ensure that security of electricity supply is secured at least cost to the consumer. Ofgem own and manage the rules of this mechanism. Ofgem provides a dispute resolution function regarding certain NGET decisions.
- Contracts for Difference (CfD) to support new investment in all forms of low-carbon generation. Ofgem provides a dispute resolution function regarding certain NGET decisions.
- Introduction of a carbon price floor to reduce uncertainty, put a fair price on carbon and provide a stronger incentive to invest in low-carbon generation now.
- An Emissions Performance Standard to provide a clear regulatory signal on the amount of carbon new fossil-fuel power stations can emit.

Ofgem sets and monitors performance outputs, incentives and funding for the Delivery Body, NGET plc. Ofgem also enforces the Rules and Regulations, the Competition Act 1998, and REMIT, and monitors NGET's compliance.

In 2014 the Electricity Market Reform programme has progressed from the design process to implementation and normal operations. The secondary legislation governing the Electricity Market Reform, including the Capacity Market Rules, Electricity Capacity Regulations and CfD Regulations, came into force on 1 August 2014. The Capacity Market prequalification process began from this date leading into the first T-4 capacity market auction which ran from 16-18 December 2014. Ofgem received a total of 20 appeals in relation to the CM prequalification process and in all cases the initial decision made by NGET plc to not qualify the Appellant was upheld.

The final budget notice for CfD was announced in early October 2014 ahead of the start of the first CfD allocation round on 16 October. The qualification results were sent to participants in mid-November and, since the volume of qualified participants exceeded the budget allowance, a competitive auction was announced in January 2015 and run in early February 2015 following the submission of sealed bids.

Following the auction 15 contracts were awarded valued at £315m accounting for a total of 2.13 GW of capacity from five different technologies. The CfD auction is 'pay as clear', and so the value of the contracts for all participants is determined by the clearing price, which is set by the marginal strike price bid as determined using the allocation budget and ranked set of bids. The majority of contracts went to wind generation technologies (55% offshore and 35% onshore). All of the technologies bid below their technology specific strike prices as set by Government, with Solar PV bidding almost 58% below their administrative strike price. Solar PV technology won 3% of the budget on offer, however, since the auction these contracts have failed to be countersigned meaning the relevant companies will be ineligible to bid for CfDs for a period of 13 months, and their contract value will be reallocated. All of the other CfD contracts awarded as per the February auction were signed by 27 March 2015. The majority of projects are set to be commissioned in 2017/18 and 2018/19. Ofgem received 3 appeals in relation to the CM

prequalification process and in all cases the initial decision made by NGET plc to not qualify the Appellant was upheld.

Summary of 2014 T-4 auction results:

398 Capacity Market Units (CMUs) qualified and confirmed their entry for the 2014 T-4 auction.⁷⁰ 26 CMUs opted-out of the CM. Most of these opt-out decisions were anticipated due to planned closures before the first delivery year for capacity market participants (2018/19).

A total of the 64.6 GW of capacity entered the auction,⁷¹ far above the procurement target of 48.6 GW. The auction procured 49.3 GW of capacity for the 2018/19 delivery year at a clearing price of £19.40,⁷² at a cost of £955.6m. Accounting for the capacity procured for post-2018/19 due to agreements longer than one year in length, the total capacity procured in this 2014 auction was 89.4 GW out to 2032/33 at a total cost of ~ £1.7bn. Below is a breakdown of the full auction results:⁷³

Table 3: Breakdown of awarded capacity by CMU classification

	Capacity (MW)	Capacity (%)	Number of CMUs	Number of CMUs (%)
Existing Generating CMU	31,447	63.84	170	55.56
Refurbishing CMU	7,049	14.31	17	5.56
Pre-Refurbishment CMU	7,968	16.18	27	8.82
New Build Generating CMU	2,621	5.32	77	25.16
Unproven DSR CMU	166	0.34	13	4.25
Proven DSR CMU	8	0.02	2	0.65
Total	49,259	100	306	100

Source: Final Auction Results - T-4 Capacity Market Auction 2014, National Grid.

Table 4: Breakdown of awarded capacity by CMU technology type

	Capacity (MW)	Capacity (%)	Number of CMUs	Number of CMUs (%)
CCGT	22,259	45.19	47	15.36
CHP & autogeneration	4,235	8.60	36	11.76
Coal/Biomass	9,232	18.74	29	9.48
DSR	174	0.35	15	4.9
Hydro	682	1.38	29	9.48
Nuclear	7,876	15.99	16	5.23
OCGT and Reciprocating Engines	2,101	4.27	121	39.54
Storage	2,699	5.48	13	4.25
Total	49,259	100	306	100

Source: Source: Final Auction Results - T-4 Capacity Market Auction 2014, National Grid.

New Balancing Services

In 2014, the SO procured for the first time the new balancing services (Supplemental Balancing Reserve and Demand Side Balancing Reserve) it introduced in 2013.⁷⁴ The SO conducted a pilot tender of the new Demand Side Balancing Reserve during the summer. Over 500 individual sites with over 300 MW of reserves tendered for this service. The SO

⁷⁰ A further 169 CMUs opted in to participate in the CM but failed to prequalify for the auction.

⁷¹ A total of 66.97 GW came forward to participate in the auction.

⁷² Capacity auctions are 'pay-as-clear', therefore the same clearing price is paid to every participant that clears the auction for every kW of capacity they have been contracted to provide.

⁷³ <https://www.emrdeliverybody.com/Capacity%20Markets%20Document%20Library/T-4%202014%20Final%20Auction%20Results%20Report.pdf>.

⁷⁴ These services are Demand Side Balancing Reserve and Supplemental Balancing Reserve. These services assist NGET to balance the system and provide consumers with an extra layer of protection from potential disruptions to supply.

offered contracts to the majority of tender participants. In addition, due to uncertainty ahead of winter 2014-15, the SO launched a tender for the Supplemental Balancing Reserve in September 2014. The SO received tenders from over 26 units and contracted with three power stations. In total, the SO procured 1.1 GW of these reserves for winter 2014-15.

4. The Gas Market

This chapter contains details of developments within GB's gas sector during 2014. This is broken down into sections covering network regulation, promoting competition, and security of supply in the wholesale and retail electricity markets.

4.1 Network regulation

Under this section unbundling, technical functioning, tariffs for connection and access, cross border issues and compliance are discussed. We show briefly what has previously been done to ensure compliance with legislation as well as other regulatory activities and market developments in 2014.

4.1.1 Unbundling

Articles 10, 11, 26 of the Gas Directive and Article 3 Regulation (EC) 715/2009 outline our obligations in relation to unbundling certification of TSOs. The Electricity and Gas (Internal Markets) Regulations 2011 (which entered into force on 10 November 2011) and the Gas and Electricity (Ownership Unbundling) Regulations 2014 (which entered into force on 15 January 2015) are together known as "the GB Regulations".

The GB Regulations implement the Third Package into the GB domestic regulatory regime including legislation, licences and industry codes. Ownership unbundling requirements are included alongside Regulations in respect of TSOs, storage and Liquefied Natural Gas (LNG) system operators, and the unbundling requirements for DSOs. The GB Regulations have amended the Gas Act 1986 ('Gas Act') to include the requirement for the holders of gas transporter and gas interconnector licences to be certified as independent from generation and supply interests pursuant to one of the grounds for certification set out in the Gas Act.

The GB Regulations have amended the Utilities Act 2000 to designate the Authority as the NRA for GB and have given it (through amendments to the Gas Act and the Electricity Act) the responsibility for administering the certification process in GB. The Authority is also required to notify the European Commission upon receipt of an application for certification where the applicant is from a third country or is controlled by a person from a third country. The Authority received no such applications in 2014.

TSOs

Under Article 10 of the Gas Directive we have an obligation to ensure any undertaking which owns a transmission system is certified as independent from generation and supply interests before it is designated as a TSO.

We continue to monitor the certification status of the four certified gas TSOs in GB, including through the review of annual declarations submitted by the relevant entities. Having reviewed these annual declarations in Q3 14, we remained satisfied that the grounds for their certifications remain valid:

- Balgzand Bacton Leiding Company (BBL): second package exemption still valid
- Interconnector (UK) Limited (IUK)

- Premier Transmission Limited (equivalent to Moyle Interconnector in the electricity section)
- National Grid Gas (NGG) plc

We are also reviewing another application for full ownership unbundling from another TSO.

DSOs

There was a change to the number of gas DSOs in GB during 2014 from 22 to 23. We continue to have eight gas DSOs (no change this year): four network areas for NGG plc, Northern Gas Networks Ltd, Scotland Gas Networks plc, Southern Gas Networks plc and Wales and West Utilities Ltd.

There are now fifteen, previously fourteen, independent (embedded) gas distribution system operators: Energetics Gas Ltd, ES Pipelines Ltd, ESP Connections Ltd, ESP Networks Ltd, ESP Pipelines Ltd, Fulcrum Pipelines Ltd, GTC Pipelines Ltd, Independent Pipelines Ltd, Quadrant Pipelines Ltd, Indigo Pipelines Ltd, Severn Gas Transportation Ltd, Greenpark Energy Transportation Ltd, SP Gas Transportation Cockenzie Ltd, SP Gas Transportation Hatfield Limited and Energy Asset Pipelines Ltd. Each independent DSO owns and operates a number of relatively small networks at various geographical locations.

During the year we have also monitored and reviewed two changes in business ownership: the sale of Indigo Pipelines Ltd (formerly SSE Pipelines Ltd) out of a vertically integrated group (SSE), and the acquisition of Bord Gáis Energy (a vertically integrated state owned Irish energy company) by Brookfield Renewable Energy (which has a link to Brookfield Infrastructure Partners that owns several independent network operators in GB). In both cases we are satisfied that Directive requirements relating to unbundling were properly observed.

We reviewed the returns submitted by DSOs relating to business independence, financial reporting and output performance. In that context we were satisfied that the Gas Directive requirements relating to unbundling were being properly observed. We also instigated a review of participation by DSOs in VAT group arrangements and a consultation on the accounts and cross subsidy audit requirements applicable to independent gas distribution system operators. Our requirement for DSOs to have two independent directors on their boards came into effect during 2014.

Storage and LNG System Operators

The Second and Third Energy Packages established a number of unbundling requirements for storage operators as part of the mandatory third party access arrangements.

In GB, the default access regime for a gas storage facility is negotiated third party access (nTPA). Under nTPA, storage system operators cannot produce gas, except as an unintended consequence of storage activities. They also cannot supply, ship, or sell gas except for the efficient operation of the storage facility or of another storage facility. Legal and functional separation is required from any parent or associated undertakings involved in these activities. These provisions, contained in Articles 15-16⁷⁵ of the Gas Directive,

⁷⁵ A system storage operator shall be independent at least in terms of their legal form, organisation and decision making from other activities not relating to transmission, distribution and storage.

were transposed in the Gas Act Section 8(R). Ofgem published guidance on compliance with nTPA requirements in December 2011.⁷⁶

In GB, two storage facilities are subject to nTPA: Rough and Hornsea. Rough is owned and operated by Centrica Storage Limited. Hornsea is owned and operated by SSE Hornsea Limited. They must operate their respective storage facilities independently of the interests of affiliates carrying out any of the above restricted activities. This includes establishing an independence programme to ensure non-discrimination against other parties, and the appropriate disclosure or use of information. In addition, the storage system operator must publish an annual report setting out compliance with the independence programme.

All other storage facilities (eight operational) in GB have been granted Minor Facilities Exemptions (MFEs) from nTPA. MFEs are granted on the basis that the facility is not economically and/or technically necessary for providing efficient access to the system for the operation of an efficient gas market. The nTPA unbundling requirements set out above do not apply to facilities with an MFE.

For LNG facilities, the default access regime under the Third Energy Package is regulated Third Party Access (rTPA). Under rTPA, LNG system operators must keep their (financial) accounts separate from any other business. These provisions, contained in Article 31 of the Gas Directive, were transposed in the Gas Act Section 19E(2)-(4). Ofgem published guidance on rTPA in April 2012.⁷⁷ All three LNG facilities in GB have been granted an exemption from rTPA requirements under the Gas Act Section 19(C).

⁷⁶<http://www.ofgem.gov.uk/Markets/WhlMkts/CompanEff/Documents1/Guidance%20on%20the%20regulatory%20regime%20for%20gas%20storage%20facilities%20in%20GB.pdf>.

⁷⁷<https://www.ofgem.gov.uk/ofgem-publications/40393/guidance-regulated-third-party-access-regime-liquefied-natural-gas-facilities-gb.pdf>.

4.1.2 Technical functioning

The technical functioning of the network is of great importance to ensure safe, secure and reliable gas supply for consumers. In the following we report on our responsibilities and activities for: gas balancing services, maintaining security and reliability standards, developing our transmission system, monitoring time taken to connect and repair, monitoring safeguard measures and reporting on the RES regulatory framework over the course of 2014, in the transmission and distribution networks.

Balancing services

Under Article 41(6)(b) of the Gas Directive, regulators must fix or approve the methodologies used to calculate or establish the terms and conditions for the provision of balancing services. These balancing services must be performed efficiently and incentivise network users to balance their inputs and off-takes.

In GB, the primary responsibility for balancing lies with gas shippers. The current arrangements are designed to provide shippers with commercial incentives to balance their inputs to, and off-takes from, the GB high-pressure National Gas Transmission System (NTS) over the course of each daily balancing period, which corresponds to a gas day. As such, parties who are not in balance incur charges that reflect the costs incurred by the SO in addressing the imbalance. These charges are known as cash out prices.

In 2014, we decided to sharpen these incentives through our gas security of supply significant code review by facilitating demand side response during situations of system stress and pricing emergency consumer interruptions into cash-out prices.

NGG, in its role as SO for the NTS, has a role as residual balancer and, as such, it can buy and sell gas to correct residual imbalances and thus ensure that the system remains in balance at all times. The primary tool that NGG uses to balance the system is the on-the-day commodity market (OCM). Ofgem has oversight through licensing arrangements over the types of balancing tools that NGG can use and their tendering processes. In addition, the Gas Directive requires regulators to ensure that TSOs are given appropriate incentives to increase efficiencies, foster market integration and security of supply. Within GB, financial incentives provide information to the market allowing it to better self-balance in each gas day, hence reducing the need for NGG to act in its role as residual balancer. These incentives help ensure security of supply by ensuring that shippers are motivated to contract for enough gas to meet their demand.

A price measure incentivises NGG to trade at a price close to the market price, thereby minimising the impact of NGG's balancing actions in the market on a daily basis. The linepack measure incentivises NGG to ensure that the linepack at the end of each gas day is similar to that at the start of the same day, so that the costs of resolving imbalances are accurately targeted on those shippers who caused them. Ofgem also financially incentivises NGG to provide the market with accurate demand forecasts up to five days ahead.

Our incentive period is set for 8 years (from 2013), in alignment with the first gas transmission price control (RIIO-T1) to use the RIIO model (Revenue = Incentives+Innovation+Outputs). As such, with the exception of a few incentives that expire earlier (2015 and 2016), NGG is incentivised under this scheme until March 2021.

Security and reliability standards, quality of service and supply

Under Article 41(1)(h) we are required to monitor the compliance with, and review the past performance of network security and reliability rules for both the transmission and distribution networks. We also have an obligation to set and/or approve standards and requirements for quality of service and supply.

Gas quality is regulated through both the Gas Safety (Management) Regulations 1996 (SI 1996/551) and the Gas (Calculation of Thermal Energy) Regulations 1996 (SI 1996/493). These regulations set rules relating to the gas composition, calorific value and measurement standards to ensure the safety and quality of the gas supply.

Transmission

The long term reliability standards to which the NTS has to be planned and operated are provided for by the gas transporter licence and are enforceable by Ofgem.

We enforce quality of service by:

- Requiring National Grid NTS to comply with standard special condition A9 of the gas transporter licence.
- Monitoring the quality of service and supply to individual users as the standards are set out in the Uniform Network Code (UNC).

Distribution

Standard special licence condition D10 of the gas transporter licence for the distribution networks sets timescales within which Gas Distribution Network companies (GDNs) must provide connection services, attend/respond to gas emergencies and respond to telephone calls to its emergency services and enquiry service obligations telephone line. GDNs must provide services within these timescales at least 90 or 97 per cent of the time (dependent on the obligation) in order to comply with their licence obligations. The guaranteed standards of performance also require GDNs to meet expected levels of service or pay customers compensation if they fail.

We monitor quality of service by:

- Requiring GDNs to comply with and monitoring performance against standard special licence condition D10 – quality of service standards of the gas distribution licence.
- Monitoring GDN performance against guaranteed standards of performance which are contained in the Gas (Standards of Performance) Regulations 2005 (SI 2005/1135), and standard special licence condition D10.

In March 2014 the GDN performance from 2008 to 2013 was reported in the end of period review of the first Gas Distribution Price Control.⁷⁸

In April 2013 the first gas distribution price control (RIIO-GD1) to use the RIIO model of network regulation was established. This set a financial regulatory framework for delivering key outputs for the GDNs. These included customer satisfaction and ensuring a reliable network. The performance for 2013 to 2014 against the RIIO-GD1 set-outputs is monitored and reported.⁷⁹

⁷⁸ <https://www.ofgem.gov.uk/ofgem-publications/86749/gdpcr1closeoutreportfinalv2.pdf>.

⁷⁹ <https://www.ofgem.gov.uk/network-regulation-%E2%80%93-riio-model/network-performance-under-riio/riio-gd1-performance-data>.

Monitoring time taken to connect and repair

Article 41(1)(m) of the Gas Directive requires GDNs to report information on the time taken to make connections and repairs. In the following we report how we have monitored this for transmission and distribution system operators during 2014.

Transmission

Connections to the NTS are governed by the UNC. Connections to the NTS are infrequent and for major pipeline developments they can take many years. The UNC requires National Grid Gas Transmission (NGGT) to provide quarterly data on connections agreements. NGGT has published this data for their 2013 quarterly reporting periods under 'Connection Offer Performance Reports'.⁸⁰

Distribution

We have proposed the same definitions for time to quote and time to connect as for electricity distribution (see section 3.1.2). We are currently discussing these proposed definitions with GDNs.

Historically, we have adopted a proactive approach to monitoring connections services and repairs by setting a minimum level of service that we expect GDNs to deliver through connections guaranteed standards. Those standards require GDNs to restore and/or repair customers' supplies within prescribed periods. They also cover the provision of connection quotations, scheduling agreed dates for connection works with customers and completing works on the dates agreed with customers.

In 2011 we amended standard licence condition 24.1 of the gas transporter licence to facilitate the performance of the Authority's functions in accordance with the Gas Directive as well as domestic legislation. We are in the process of developing the associated instructions to ensure that the GDNs report this data on a consistent basis. We expect these instructions to be in place and effective by 2016.

Monitoring access to storage, linepack and other ancillary services

Under Article 41(1)(n) of the Gas Directive regulators are required to monitor and review the access conditions to storage, linepack and other ancillary services. In the GB gas market, the default regime is for all storage facilities to offer nTPA unless the facility has been granted an exemption. Key requirements for storage facilities are:

- To be legally unbundled from related undertakings
- To offer access to third-parties on non-discriminatory terms.

Ofgem published a guidance document in December 2011 in respect of the new regulatory regime.⁸¹

National Grid is required by its licence to procure Operating Margins on an annual basis as an ancillary service. The Operating Margins service is used to maintain system pressures in the period before other system management services become effective (e.g. national or locational balancing actions). Ofgem assesses the tender process and carries out a test to ensure the tender is competitive. In 2014 we were satisfied that competition was effective for the provision of Orderly Rundown and Non Locational requirements.

⁸⁰ <http://www2.nationalgrid.com/uk/services/gas-transmission-connections/connect/performance-reports/>.

⁸¹ <http://www.ofgem.gov.uk/Markets/WhlMkts/CompandEff/Documents1/Guidance%20on%20the%20regulatory%20regime%20for%20gas%20storage%20facilities%20in%20GB.pdf>.

Monitoring correct application of criteria that determine model of access to storage

Under the Article 41(1)(s) of the Gas Directive, regulators must monitor the correct application of the criteria that determine whether a storage facility falls under negotiated or regulated access. As noted above, the GB default regime for all storage facilities is to offer nTPA unless the facility has been granted an exemption.

Ofgem grants a MFE where we are satisfied that access to the storage facility by other persons is not technically or economically necessary for the operation of an efficient gas market. The owner of a storage facility may apply to Ofgem for such an exemption, and Ofgem may revoke an exemption if the criteria are no longer met. More details of our approach are set out in an open letter.⁸²

Ofgem has granted a new MFE in 2014, see chapter 4.1.3 under 'regulated and negotiated access to storage'.

Monitoring safeguard measures

Under Article 41(1)(t) of the Gas Directive we are also required to monitor the implementation of safeguard measures. These will be used in the event of a sudden crisis in the energy market as referred to in Article 46 of the Gas Directive. Article 46 is taken forward by and further specified in Articles 10 (6) and (7) of the EU Gas Security of Supply Regulation (Regulation (EU) No. 994/2010). As such, under Article 10 of the Gas Security of Supply Regulation, the competent authority is required to prepare an emergency plan that outlines the action that it intends to take in an emergency.

In 2014, DECC published the National Preventive Action Plan: Gas,⁸³ which describes the arrangements established between the gas industry, DECC, and the European Commission for the safe and effective management of gas supply emergencies. Ofgem provided comments to DECC on the National Preventive Action Plan throughout the drafting process and as such we are comfortable that the appropriate safeguard measures have been implemented.

⁸² http://www.ofgem.gov.uk/Markets/WhIMkts/ComandEff/TPAccess/Documents1/Storage%20Exemptions%20Open%20Letter%2009%20For%20publication_.pdf.

⁸³ <https://www.gov.uk/government/publications/national-preventive-action-plan-gas>.

4.1.3 Network and LNG tariffs for connection and access

Under Article 41(1)(a), 41(6)(a), 41(8), 41(10) and 41(12) of the Gas Directive, NRAs are required to fix or approve transmission or distribution tariffs or their methodologies. Here we report on our activities surrounding the regulation of tariffs and network charges (for transmission and distribution) during 2014.

NGGT is the sole owner and operator of the GB gas NTS. There are eight GB GDNs. The revenues that both NGGT and the GDNs can collect from users of the NTS and GDN via network charges are determined by us at the price control review. The current gas transmission and distribution price controls are based on the RIIO model (RIIO-T1⁸⁴ and RIIO-GD1⁸⁵) and began on 1 April 2013, running until 31 March 2021.

Following an assessment, we establish cost allowances and performance targets which form the basis of the price control and incentive framework. Included in these arrangements is an incentive which allows allowed revenue to increase in response to user signals for new capacity. Together, these elements determine the total amount of revenue (the 'allowed revenue') that NGGT and the GDNs may earn in each year. All are required by the regulatory regime to set charges for use of their networks to comply with the limits on allowed revenue that have been set. Should more or less than the permitted revenue be earned in any formula year, then a compensating adjustment is made in the following year.

Transmission

Users of the gas NTS are subject to three main elements of transmission charges:

- Transmission Owner (TO) entry charges
- Transmission Owner (TO) exit charges
- SO charges.

TO charges are for the provision and maintenance of transmission network assets. NGGT has in the past recovered all of its TO allowed revenue on the basis of TO entry and exit capacity charges, but subsequently TO entry and exit commodity charges (charges based on actual gas flows) have been levied where NGGT has forecast a shortfall in collected revenue versus target revenue. NGGT collects its SO allowed revenue via SO commodity charges which are levied on the basis of gas flows at entry and exit. SO charges are costs incurred by the SO in its day to day operation of the NTS.

Connection charges are levied on new connections to the NTS and reflect the costs incurred by NGGT in providing any assets required to connect a user to the NTS. These connection costs are not determined by the price control review.

Under its licence, NGGT is obliged to develop and maintain a methodology which sets out how NTS charges are determined and must comply with the following objectives: that the methodology results in charges that are reflective of the costs incurred by NGGT in its transportation business; that it facilitates effective competition between gas shippers and between gas suppliers; that it takes account of developments in the gas transportation business; and that it is in compliance with the Gas Regulation (Regulation 715/2009) and legally binding decisions of the European Commission and/or ACER.

⁸⁴ <https://www.ofgem.gov.uk/network-regulation-%E2%80%93-riio-model/riio-t1-price-control>.

⁸⁵ <https://www.ofgem.gov.uk/network-regulation-%E2%80%93-riio-model/riio-gd1-price-control>.

We have approved NGGT's charging methodology. Following its implementation, the charging methodology has been incorporated into the contractual framework between GB gas network users and operators, the UNC.⁸⁶ This means that modification proposals to the charging methodology are subject to the governance procedures of the UNC. Consequently, modification proposals can be raised by any UNC party. Implementation of charging methodology modification proposals are subject to approval by us, and our assessment of the extent to which the proposed methodology changes better meet the relevant licence objectives described above. Self-governance provisions exist within the UNC governance procedures to allow low-impact modifications to be implemented without approval by us. A proposal must meet certain criteria, set out in the licence, in order to be classified as self-governance.

We do not approve the network charges levied, only the charging methodology used to determine them. NGGT is obliged to provide a 150 day indicative notice of proposed changes to the level of charges, and a 60 day final notice of actual changes. Subject to the methodology, TO entry and exit capacity charges are levied on all network users, including storage sites, LNG terminals, and beach terminals, in a non-discriminatory way. TO and SO commodity charges are not levied on gas storage users as it is not considered cost reflective to do so. NGGT is also required to submit a report each year to us which notes developments in the gas transmission charging methodology in the previous formula year and what further changes may be necessary to improve compliance with the relevant objectives.⁸⁷ In 2014, no significant changes were made to the gas transmission charging methodology.

In June 2013 we launched the Gas Transmission Charging Review.⁸⁸ The current charging regime has served consumers well by promoting the effective use of the network and facilitating effective competition. However, significant and ongoing structural changes to the GB gas market since the system was designed, and emerging EU legislation to harmonise transmission charges across Member States (EU Network Code on Tariffs), have prompted us to conduct a review. We wanted to consider what changes to the charging regime, if any, might further the interests of current and future consumers.

Following this review, in December 2014 we published our policy position on GB's gas transmission entry charging regime,⁸⁹ proposing two key changes:

1. introducing 'fully-floating' capacity charges for long-term capacity products; and
2. changing the charging arrangements for short-term capacity products.

Publishing our policy position marked the beginning of our consultation on these changes. The consultation closed on 27 March 2015. If there are any changes, we will seek to co-ordinate the implementation of these with the wider process of implementing the EU Network Code on Tariffs.

⁸⁶ Published on the [Joint Office of Gas Transporters](http://www2.nationalgrid.com/uk/Industry-information/System-charges/Gas-transmission/Forecasts/) website.

⁸⁷ <http://www2.nationalgrid.com/uk/Industry-information/System-charges/Gas-transmission/Forecasts/>.

⁸⁸ <https://www.ofgem.gov.uk/gas/transmission-networks/gas-transmission-charging-review>.

⁸⁹ <https://www.ofgem.gov.uk/publications-and-updates/gas-transmission-charging-review-our-policy-position-future-charging-arrangements>.

Distribution

The GDNs recover their allowed revenues via a combination of Local Distribution Zones (LDZ) capacity and commodity charges and an LDZ customer charge. The GDNs are obliged to provide a 150 day indicative notice of proposed changes to the level of these charges and 60 days final notice for actual changes.

In common with NGGT, under the licence the GDNs are obliged to develop and maintain a methodology which sets out how LDZ charges are determined and which complies with the same NTS charging methodology objectives listed above. There is an additional objective that the licensee shall not show any undue preference towards, or undue discrimination against, any person who operates or proposes to operate, a pipeline system in relation to the connection of that system to the pipeline system to which the licence relates. These objectives also apply to the GDNs' connection charging methodology which the GDNs are also obliged to maintain under the licence.

We do not approve the LDZ charges levied, but only the charging methodology used to determine them. The GDN charging methodologies have also been incorporated into the UNC and as such, any modification proposals to the charging methodologies are subject to the UNC governance procedures. The UNC contains provisions for stakeholders to input into the process too. This is done either through participation in various industry working groups, or through the more formalised public consultation processes. We consider any inputs received in reaching a decision on methodologies or tariffs. Stakeholders have the right to request a judicial review of any such decision.

There were no requests for judicial review on any decision regarding the methodologies or tariffs during 2014.

LNG facilities

The three⁹⁰ LNG facilities currently operating in GB have an exemption⁹¹ from third party access and therefore the provisions of Articles 41(10) and 41(6) of the Gas Directive do not apply to them.

Any exempted LNG facility is required to operate under the terms and conditions of its exemption. Commercial terms and conditions are agreed between the facility operator and its primary capacity holders. However, in the event that we believe terms and conditions published⁹² by LNG operators are discriminatory we are able take actions under the enforcement provisions contained in the Gas Act 1986 - in particular section 28. No investment under this route took place in 2014.⁹³

Prevention of cross-subsidies

Each NRA, under Article 41(1)(f) of the Gas Directive, is required to ensure that there are no cross-subsidies between transmission, distribution and supply activities.

In GB, licenced gas transmission operators and DNOs are subject to licence conditions prohibiting regulated businesses from giving cross-subsidies to, or receiving cross-

⁹⁰ Isle of Grain, South Hook and Dragon LNG.

⁹¹ Ofgem published its final decision to grant an exemption to the Isle of Grain LNG terminal for an expansion ('phase 4') of approximately 8.4 billion cubic meter/year (bcm/y) of capacity on 8 March 2013. The European Commission approved this decision on 4 June 2013.

⁹² Under section 19D Gas Act 1986.

⁹³ <https://www.ofgem.gov.uk/gas/wholesale-market/market-efficiency-review-and-reform/third-party-access-exemptions>.

subsidies from, related undertakings. The regular information submissions that licencees are required to make, principally those relating to their price control arrangements, allow us to assess whether any risk or incidence of cross-subsidisation has arisen.⁹⁴

Gas distribution licences include a requirement for independent auditors to carry out a range of procedures, agreed with us, to provide assurance that obligations to avoid discrimination and cross-subsidy are being respected. We review the auditors' reports and raise supplementary questions as appropriate.

A key area which we will continue to monitor is the interpretation and application of requirements for financial transactions to be completed on an arm's length basis and on normal commercial terms. This is especially relevant with respect to the terms of loans made to or by the relevant licencee. For gas distribution licencees, we also monitor the risk of licencee owned freehold sites being sold to related parties at insufficient value. This particularly relates to gas holder sites in major cities, where land value for development is especially high at present.

Other key risk areas we take into account are:

- the basis of recharging for services provided at a group level;
- the justification for any management fees charged to the licencee by related parties; and
- the interest rates charged on intra-group loans affecting the licencee.

On 1 April 2014, our new requirement for each licencee (except for independent DSOs and OFTOs) to have at least two sufficiently independent directors came into effect. We consider that this measure will be supportive of good governance at licencee level.

Regulated and negotiated access to storage

Under article 41(1)(s) of the Gas Directive, regulators must monitor the correct application of the criteria that determine whether a storage facility falls under negotiated or regulated access. In the GB gas market, the default regime is for all storage facilities to offer nTPA unless the facility has been granted an exemption. Key requirements for storage facilities are:

- to be legally unbundled from related undertakings if the related undertaking does certain other activities eg, supplies, sells or ships gas (more information on unbundling can be found in chapter 4.1.1) and,
- to offer access to third-parties on non-discriminatory terms.

Ofgem grants a MFE where we are satisfied that access to the storage facility by other persons is not technically or economically necessary for the operation of an efficient gas market. The owner of a storage facility may apply to Ofgem for such an exemption and Ofgem may revoke an exemption if the criteria are no longer met. More details of our approach are set out in an open letter.⁹⁵

⁹⁴ The prohibition on cross subsidies is prescribed by: Internal Markets Electricity Directive (IMED) 2009/72/EC at Article 31(3); the Internal Markets in Natural Gas Directive 2009/73/EC at Article 31(3); Standard Licence Condition 4 of the Electricity Distribution Licence; Standard Special Condition A35 of the Gas Transporter Licence (Standard Condition 41 for independent gas transporters); and Standard Condition B5 of the Electricity Transmission Licence (Standard Condition E6 for offshore transmission network operators).

⁹⁵ <https://www.ofgem.gov.uk/ofgem-publications/41204/storage-exemptions-open-letter-09-publication.pdf>.

Ofgem granted a MFE for Stublach gas storage phase 2 in May 2014. It will provide an additional 200 mcm of capacity with 16 mcm/d peak deliverability and injectability at the facility when fully operational. This work is expected to be completed by winter 2018.

4.1.4 Cross-border issues

In order to reach a fully integrated European energy market, it is vital that NRAs coordinate effectively on cross border issues. In this section we report on our access to cross-border infrastructure, LNG terminals and storage facilities, our investment plans and cooperation with other NRAs during 2014.

Access to cross-border infrastructure including allocation and congestion management

Under Article 41(6)(c), 41(8) and 41(9) of the Gas Directive, NRAs are responsible for: approving methodologies and tariffs used for access to cross-border infrastructures, ensuring transmission and distribution system operators are granted appropriate incentives, monitoring congestion management of national gas transmission networks and the implementation of congestion management rules and capacity allocation mechanisms.

The British gas system is interconnected with Belgium, the Netherlands, Northern Ireland and the Republic of Ireland. These interconnections play an important role in gas security of supply by allowing for gas to flow to where it is valued most and allowing for a more integrated European gas market.

The paragraphs below give an overview of the arrangements on each of the interconnectors. Each interconnector is licenced by Ofgem and must submit their access rules to us for approval.

IUK

The interconnector with Belgium, Interconnector UK (IUK) became operational in 1998. IUK can physically flow gas in both directions and has an import capacity of 25.5bcm/year and an export capacity of 20bcm/year.

To secure financing for the interconnector, original IUK customers agreed to book and pay for primary capacity on a 20 year term. Subsequent capacity expansions have also been funded on the basis of primary capacity charges. Primary capacity gives holders ('IUK Shippers') the right to flow a certain volume of gas in forward flow and/or reverse flow.

Primary interruptible capacity is also available to IUK Shippers to account for the fact that the physical capacity of IUK may vary depending on operating conditions. Secondary capacity can be made available to non-IUK Shippers through subletting or capacity transfers. IUK has sold all of its capacity in long-term contracts until 2018.

These long-term contracts pre-date the 2nd and 3rd Package requirements relating to third party access and are exempt.

BBL

BBL was established in July 2004 to design, construct and operate an interconnector to transport gas from the Netherlands (Balgzand) to the UK (Bacton). Transportation of gas started in December 2006, with a total capacity of ~15bcm/year. In April 2011, a fourth compressor was installed, increasing capacity by ~3bcm/year to 18bcm/year.

BBL offers forward flow capacity, on a first come first served basis, to any shipper that signs an agreement to become a BBL Shipper. The first of the existing long term contracts with BBL expire in 2016, with further capacity becoming available in 2022. As not all capacity offered in the open season in 2007 has been contracted, a limited amount of firm

capacity is available for sale. An unlimited amount of interruptible forward flow capacity is also available. Interruptible reverse flow capacity, from the UK to the Netherlands, is sold through daily, monthly and quarterly auctions at a zero reserve price. BBL has an exemption from the 2nd Package requirements and has certain licence conditions switched off relating to third party access and approval of charging methodologies for 80 per cent of its forward capacity.⁹⁶

Moffat

The Moffat interconnector with the Republic of Ireland became operational in 1993 and is a physically uni-directional interconnector. The capacity available to exit the NTS at Moffat is 32.8 mcm/day. In December 2011, a virtual reverse flow service was introduced. This allows shippers to nominate flows from Ireland to GB on an interruptible basis. The maximum entry capacity at Moffat is 31.1 mcm/day.

From 1996 a branch-off from the Moffat pipeline at Twynholm in Scotland became operational to flow gas from GB to Northern Ireland. This is also known as the Scotland to Northern Ireland Pipeline. In February 2013, a virtual reverse flow service was introduced to nominate flows from Northern Ireland to GB.

Until 30 September 2012 existing exit capacity was released on a first come first served basis. Since October 2012 users have been able to purchase long-term exit capacity (from GB to Ireland) at the Moffat interconnection point in an annual window. Short-term exit capacity and interruptible entry capacity (for virtual reverse flow) on the GB side is also available through daily auctions with a zero reserve price.

In addition, incremental exit capacity can be allocated if the interconnector capacity is sold out via the long-term booking process. National Grid can also apply oversubscription and long term use-it-or-lose-it mechanisms to ensure the maximum amount of capacity is available.

Access to LNG Terminals and Storage Facilities

In GB, we do not have a separate licensing regime for LNG system operators and they are regulated through requirements set out in the Gas Act. All LNG system operators currently have an exemption from third party access and therefore Article 41(10) does not apply to them.⁹⁷ However, in the event we believe that the terms and conditions published by owners of LNG import or export facilities are discriminatory, we are able to take action under the enforcement provisions contained in the Gas Act - in particular section 28.

Storage is also a non-licenced activity in GB and is regulated pursuant to the Gas Act provisions under a nTPA regime, which itself derives from the Gas Directive, part of the Third Package. Under the nTPA regime, we do not have the responsibility to approve tariffs or charging methodologies for storage facilities. Instead, it is up to the Storage System Operators to ensure that their tariffs meet the requirements of the Gas Regulation. We have the power to proactively monitor Storage System Operators' compliance with the Gas Regulation and can take enforcement action if we believe any conditions relating to a grant of storage rights published⁹⁸ by owners of a gas storage facility are discriminatory.

The Gas Directive gives the right to any party affected to submit a complaint for review by the NRA regarding a decision on methodologies used or concerning the proposed tariffs or

⁹⁶ Standard conditions 10,11 and 11A of the Gas Interconnector Licence.

⁹⁷ See Article 41(10) of the Gas Directive 2009/73/EC.

⁹⁸ See section 19B of the Gas Act 1986.

methodologies. Changes have been made to the Gas Act to extend the scope of the dispute resolution mechanism in order to cover disputes arising out of complaints to the Authority against owners of gas storage facilities and owners of LNG import or export facilities.⁹⁹ We did not receive any complaints in 2014.

Implementation of the Third Package

The Third Package introduced new responsibilities for regulatory authorities regarding the rules for granting access to cross-border gas infrastructures.¹⁰⁰ In GB, changes have been made to the standard conditions of the Gas Interconnectors Licence¹⁰¹ to take full account of these new responsibilities.

In August 2012, the European Commission adopted the Congestion Management Procedures (CMP) Guidelines¹⁰², which set a deadline of 1 October 2013 for the implementation of three procedures, and 1 July 2016 for the implementation of a fourth.

The main requirements of the CMP Guidelines are incentives for TSOs to offer capacity in addition to their technical levels and to allow users to surrender their unused capacity for resale. Further to the work completed in 2013, we approved a UNC modification in August 2014 that introduced the long term use-it-or-lose-it mechanism.

Both BBL's and IUK's implementation of CMP was put on hold in late 2013 pending agreement with neighbouring NRAs on the interpretation and application of the CMP Guidelines. IUK's proposal was submitted and approved in late 2014. BBL is currently preparing detailed proposals.

In October 2013, the European Commission adopted the Capacity Allocation Mechanism (CAM) Regulation, which applies from 1 November 2015.¹⁰³ The main requirement of the CAM Regulation is for capacity at interconnection points to be auctioned as a bundled product with standard durations.

We have adopted a two-stage process with relevant TSOs and NRAs of GB, Belgium and the Netherlands to implement the auction of bundled products. During the first stage, the relevant TSOs jointly consulted with stakeholders on proposals to implement bundled capacity auctions and sought an opinion from relevant NRAs on these proposals. In April 2014 IUK consulted on its proposal for implementing the CAM Regulation and provided stakeholders with an update in September on the changes made.¹⁰⁴ IUK is expected to submit its proposal for approval in 2015. In the second phase, the TSOs make the necessary changes to their industry documents and contracts.

We published a statutory consultation in December 2014 on changes to NGG's licence needed to facilitate implementation of CAM in GB.¹⁰⁵ These changes took effect from April 2015. NGG also raised two UNC code modifications to:

1. Implement the standardised products and auctions required by CAM.

⁹⁹ Regulation 28 amends sections 27B-27D of the Gas Act

¹⁰⁰ See Articles 41(6)(c), 41(8), 41(9) and 41(10) of the Gas Directive 2009/73/EC

¹⁰¹ See standard conditions 10, 11 and 11A of the Gas Interconnector Licence.

¹⁰² <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:231:0016:0020:EN:PDF>.

¹⁰³ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:273:0005:0017:EN:PDF>.

¹⁰⁴ <http://www.interconnector.com/about-us/what-we-have-to-say/consultations/>.

¹⁰⁵ <https://www.ofgem.gov.uk/publications-and-updates/statutory-consultation-proposed-licence-modifications-facilitate-implementation-capacity-allocation-mechanisms-network-code-great-britain>.

2. Manage existing bookings at Interconnector Points purchased before CAM was foreseen. Three alternative proposals of how to manage existing bookings were also raised. We are currently assessing these proposals before reaching a decision on which (if any) to approve.

Cooperation

Article 41 (1)(c) of the Gas Directive requires us to consult and cooperate with ACER and other NRAs over cross-border gas issues and to promote certain objectives. These include the integration of national gas markets, jointly managed cross border trade in gas and the allocation of cross-border capacity. Changes have been made to the Gas Act 1986 to reflect this.¹⁰⁶

Examples of cooperation

In 2014, we cooperated and continue to cooperate with neighbouring NRAs over a number of issues concerning interconnectors and full implementation of the European Network Codes. For example, Ofgem has been working with the Northern Ireland, Republic of Ireland, Dutch and Belgian regulators to facilitate the implementation of the Guidelines/ENCs on congestion management policy, capacity allocation, gas balancing and transmission tariffs.

Moreover, we also co-chaired, alongside two other regulators, ACER's incremental capacity work stream to introduce a transparent, market-based process to trigger new cross-border gas transmission capacity where needed. Furthermore, we have contributed to the development of the Harmonised Tariff Structures Framework Guidelines.

Ofgem has also been very actively involved at CEER working with regulators across Europe to develop a vision for gas storage regulation, as well as to develop the revised Gas Target Model. We co-chair the Gas Storage Task Force and continue to contribute to CEER's projects around sharing experiences on regulatory matters, including on storage and LNG issues.

Monitoring investment plans and assessment of consistency with Community wide network development plan

We set price controls for the gas TSO (NGG) and as part of this process we review the company's business plans. We explicitly require the business plans to consider the interaction with wider European developments as part of the context of the plan. We also require the company to consider the various uncertainties across both the period for which the control is set and beyond.

In practice, major changes to the gas transmission network including those related to community-wide network developments will arise through the commercial incremental entry and exit arrangements for which we will be aware and involved at major stages of development e.g. setting revenue drivers to make sure that National Grid receives an appropriate revenue adjustment. We will therefore have sufficient information to inform our duty under Article 41(1)(g).

Currently, we are establishing a monitoring approach to review ongoing performance against the outputs determined in the price control. We are involved in work comparing the domestic investment plans with the EU-wide plan.

¹⁰⁶ See Regulation 34 of the Electricity and Gas (Internal Market) Regulations 2011, which inserts section 4D into the Gas Act 1986.

4.1.5 Compliance

Ensuring that NRAs and market participants comply with mandatory obligations is essential for a well functioning energy market. Below, we report on our powers to enforce the Agency's and Commission's decisions, as well as the investigations that have concluded during 2014 relating to existing legislation.

Compliance of regulatory authorities with binding decisions of the Agency and the Commission and with the Guidelines (Article 43)

Under the Third Package we are required to ensure compliance with and implement binding decisions of ACER and of the European Commission and with the Guidelines. In order to enable Ofgem to do this, our principal objective under the Gas Act has been amended so as to provide that the Authority has to carry out its functions under Part I of that Act in the manner that it considers is best calculated to implement or ensure compliance with any binding decision of ACER or of the European Commission.

Compliance of transmission and distribution companies, system owners and natural gas undertakings with relevant Community legislation, including crossborder issues

We have powers to investigate compliance of transmission and distribution companies, system owners and natural gas undertakings with relevant Community legislation. If a breach is found, we have powers to impose penalties. As a condition of certification, TSOs are obliged to notify the Authority if they know (or reasonably should know) of an event or circumstances which have occurred, or are likely to occur, that may affect their eligibility for certification and must provide an annual declaration (approved by a resolution of the TSO's board of directors) in this regard. The Authority also has powers to require information to be provided by the TSO for the purpose of monitoring the TSO's certification.

IUK and BBL are obliged to give quarterly reports to the Authority on progress in complying with conditions set out in the Authority's final certification decisions.

Ofgem, in close cooperation with other relevant NRAs, ensures TSOs are compliant with Network Codes and Guidelines (as required by GB TSO licences) by monitoring GB TSO business rules, standard transportation agreements and any other relevant operational rules and agreements. As with certification, we require TSOs to notify the Authority if they know (or reasonably should know) of an event or circumstances which have occurred, or are likely to occur, that may affect their compliance with the Ofgem approved network code compliance regime.

Update on Ofgem's enforcement investigations

We have not had any investigations in 2014 relating solely to gas provisions. Please refer to section 3.1.5 to view investigations relating to cross cutting (electricity and gas) undertakings.

4.2 Promoting Competition

In the following chapter we report on the current state of the wholesale and retail markets in GB and the main changes in 2014, as well as our monitoring activities in both the wholesale and retail markets during the past year. As a large amount of Ofgem's engagement with the retail energy market does not distinguish between electricity and gas sectors, this is covered below. Where Ofgem does assess the electricity and gas retail sectors separately, this is noted and dealt with separately.

4.2.1 Wholesale markets

The following section provides an overview of our monitoring under Article 37(1)(i),(j),(k),(l),(u) and Article 40(3), and the main developments in the wholesale gas market in GB during 2014. Detailed information can be found in the following sections, a summary of which is presented below:

- A healthy supply and demand picture placed downward pressure on gas prices throughout most of the year.
- As a result of these trends, average day-ahead gas prices in 2014 were down 26% year-on-year.
- A combination of near term fundamentals, falls in the oil price and a loosening of the global LNG market contributed to falls across the gas forward curve over the year.
- Traded volumes increased by 27% in 2014 to 1,888 bcm, with annual churn rising from 20 to 29.
- Futures volumes increased 76% in the year, to account for 46% of total annual traded volume.
- LNG imports to GB were up 20% year-on-year, to 11.3 bcm.
- Net imports from the Continent were down 88% year-on-year to 842 mcm. IUK switched from being a net importer in 2013 to net exporting 4 bcm in 2014.
- We made a MIR to the in June 2014 following a public consultation. This followed the publication of our first annual State of the Market report in March 2014, in collaboration with the OFT and the CMA.

Policy developments in several areas of GB's wholesale gas market have continued throughout 2014. Some notable policy areas include:

- Implementing cash-out reform under the Gas Significant Code Review.
- Approval of a MFE for Stublach gas storage facility.
- Development and implementation of European Network Codes and Guidelines.

4.2.1.1 Monitoring the level of prices, the level of transparency, the level and effectiveness of market opening and competition

Prices

Wholesale gas prices in GB are compiled and made available to market participants by a number of independent pricing agencies, energy market brokers and via exchanges. Argus Media, ICIS Heren and Platts provide pricing based on reported OTC trades, made available to the market via a subscription service. In addition, financial data providers (such as Bloomberg PROFESSIONAL service) provide close to real time energy broker pricing based on OTC trades.

In addition to a wide range of OTC pricing data, the Intercontinental (ICE) exchange also provides pricing data to the market, both through the OCM and through the ICE Futures market.

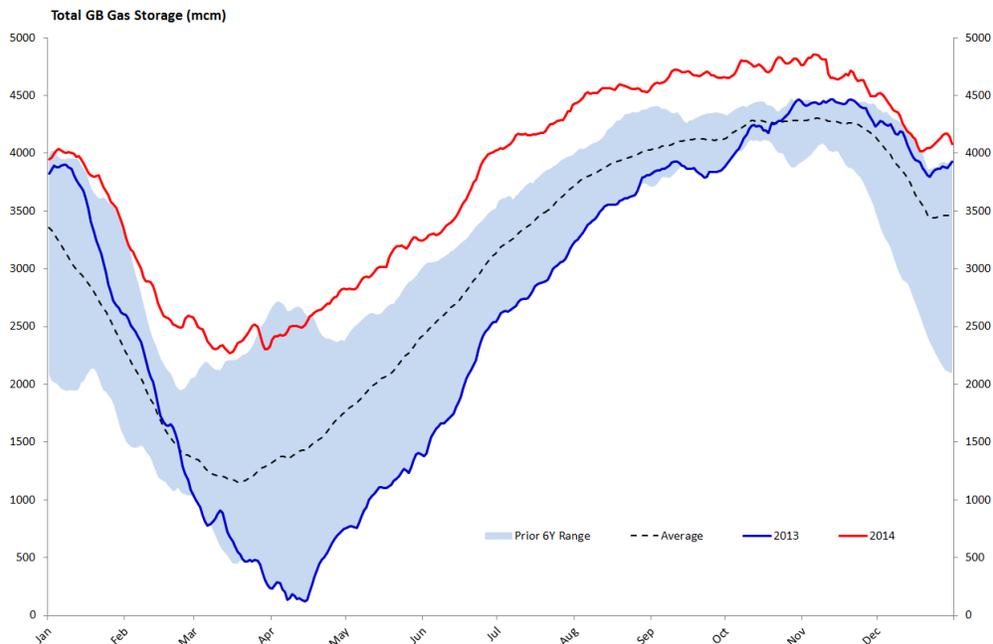
Fundamentals

A healthy supply and demand picture placed downward pressure on gas prices through most of the year.

GB storage stocks reached record highs in 2014 (see Figure 9) following the mild winter of 2013/14, reducing demand for summer storage injections and improving the supply outlook for winter 2014/15.

Figure 9: Total GB gas in storage during 2014 (red line), compared with 2013 (blue line), 6Y average (dotted) and prior 6 year range (blue bands)

Source: National Grid/Bloomberg/Ofgem.



LNG flows also contributed to the strong supply picture in 2014. In total, LNG imports to GB were up 20% year-on-year, to 11.3 bcm.¹⁰⁷ This was largely a result of price trends in the global LNG market, with both market fundamentals and oil-gas links putting downward pressure on global prices. These effects became particularly pronounced in the second half of the year, when GB imports of LNG were up around 58% compared with the second half of 2013.

Total GB gas demand was down in 2014, falling 7.1 bcm year-on-year to 70.5 bcm/year. Of this decrease, 5.2 bcm was due to a fall in domestic consumption, with mild temperatures weighing on heating demand. Total annual gas demand for electricity consumption was unchanged in 2014, outturning lower year-on-year in the first quarter due to mild temperatures but finding some support in Q2-Q4, as coal and nuclear outages

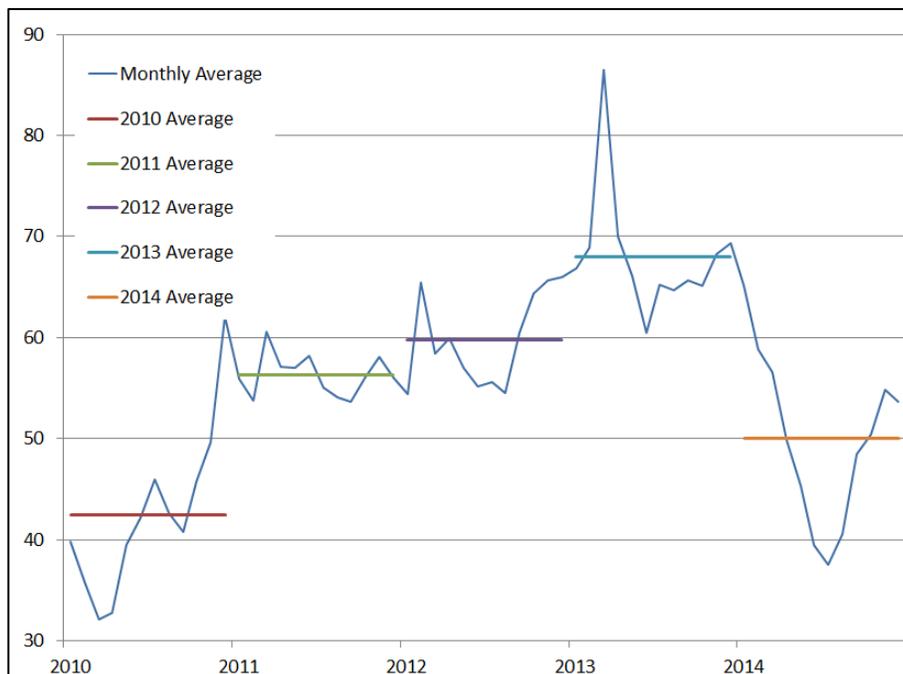
¹⁰⁷ <https://www.gov.uk/government/statistics/gas-section-4-energy-trends>.

combined with low gas prices to incentivise increased Combined Cycle Gas Turbines generation.

Price developments

GB wholesale gas prices both for near-term and forward delivery generally fell throughout 2014, driven by a combination of healthy fundamentals and a feed through of oil price drops. The average day ahead gas price in 2014 was the lowest since 2010 at 50p/therm,¹⁰⁸ compared with 68p/therm in 2013 (see graph below). Similarly, the forward contract for delivery of gas in winter 2015/16 finished the year 16p/therm (23%) lower than at the end of 2013.

Figure 10: Monthly average day ahead NBP price (p/therm, light blue) and yearly average day ahead prices since 2010



Liquidity

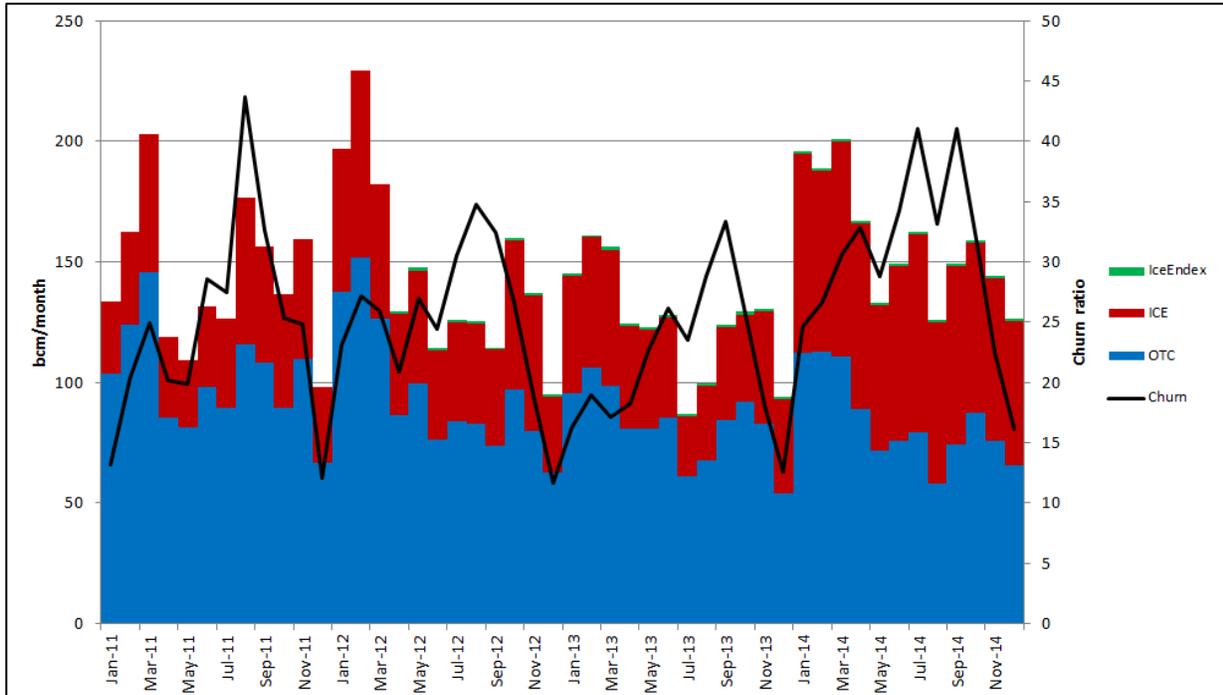
GB saw an increase in both traded volumes and churn in 2014,¹⁰⁹ compared with 2013. Traded volumes increased by 27% year-on-year to 1,888 bcm, with annual churn rising from 20 to 29.

¹⁰⁸ Price data from ICIS Energy.

¹⁰⁹ Based on data from London Energy Brokers' Association, ICE and National Grid.

Much of the growth in liquidity was in futures trading on the exchange (ICE Futures Europe). ICE's share of total traded volume of GB gas rose from 34% in 2013 to 46% in 2014, with volumes on ICE increasing 76% year-on-year.

Figure 11: NBP trading volumes and churn, 2011 to 2014



Transparency

REMIT

The REMIT legislation is a key tool in ensuring the transparency of prices within the wholesale energy market. For further information, please refer to the Electricity section (3.2.1).

Market opening and competition

Market investigation referral to the CMA

In March 2014 we published our first annual State of the Market report, in collaboration with the OFT and the CMA. On 26 June 2014, we made a MIR to the CMA after a public consultation process. The CMA's investigation is currently in progress. The publication of provisional findings is expected in May/June and the final decision is due by the end of 2015. Please see section 3.2.2 for more details.

Market integration

The GB gas market is well-integrated with both European and global gas markets. IUK interconnector connects GB with Belgium, while BBL connects GB with the Netherlands. GB is connected to the LNG market through the Isle of Grain, South Hook and Dragon LNG terminals and the Teeside GasPort facility for energy bridge regasification vessels.

For IUK, each shipper has a share of the Forward Flow and Reverse Flow Standard Capacity. Historical analysis¹¹⁰ indicates that IUK is price responsive to a relatively high level of efficiency. In the case of BBL, experience suggests that flows to GB remain broadly steady and are less responsive to price signals under normal operating conditions.

In 2014, net imports from the Continent were down 88% year-on-year to 842 mcm¹¹¹ (from 6,824 mcm in 2013), as GB remained well supplied throughout the year. The drop was most notable for IUK, over which GB switched from being a net importer in 2013 to net exporting 4 bcm in 2014.

Market concentration

The GB market receives its gas supplies from a variety of different sources comprising indigenous supplies from the UK continental shelf, imports from Norway (via the Vesterled, Langeled and Tampen Link pipelines), imports from Continental Europe (via IUK and BBL) and from the LNG market (via the above terminals). With this diversity of supply also comes a diversity of shippers on the wholesale market.

For the interconnectors, originally nine shippers acquired Capacity Rights in IUK for a period of 20 years from 1 October 1998 through to 30 September 2018. Currently, 13 Shippers hold primary capacity rights.¹¹² On BBL, there are currently 14 shippers, three of which have primary capacity rights.¹¹³

For LNG, there are six shippers (BP, Centrica, GDF Suez, E.ON, Iberdrola and Sonatrach) who import gas through the Isle of Grain. The South Hook Terminal is owned by a UK joint venture of Qatar Petroleum (67.5 per cent), ExxonMobil (24.15 per cent) and Total (8.35 per cent). Dragon LNG is equally owned by two shareholders, BG Group and Petronas.

Rough remains the largest GB storage facility, with no change to this status projected in the near term. There are approximately 20 capacity holders at Rough.

¹¹⁰ <https://www.ofgem.gov.uk/ofgem-publications/75776/interconnector-flows-further-analysis-next-steps-final.pdf>.

¹¹¹ <https://www.gov.uk/government/statistics/gas-section-4-energy-trends>.

¹¹² Information correct as at Q1 2015. Shippers are listed on IUK's website: <http://www.interconnector.com/access-services/the-service/current-shippers/>.

¹¹³ Shippers are listed on BBL's website: <http://www.bblcompany.com/commerce/shippers-list>.

4.2.2 Retail market

A large amount of Ofgem's engagement with the retail energy market does not distinguish between the electricity and gas sectors – rather, the market is considered as a whole. This engagement is covered in section 3.2.2. Where Ofgem does assess the electricity and gas retail markets separately, the information has been documented in 3.2.2 and 4.2.2 respectively.

4.2.2.1 Monitoring the level of prices, the level of transparency, the level and effectiveness of market opening and competition

Before the full introduction of competition in 1999, British Gas had a monopoly to supply all domestic gas consumers in GB. In the subsequent years, competition developed, especially from the former Public Electricity Suppliers. As a result, the majority of the domestic gas supply market is now accounted for by British Gas and by the 5 large vertically integrated electricity suppliers (which evolved from the Public Electricity Suppliers through mergers and acquisitions). There were also 19 small domestic gas suppliers in December 2014. We have seen growth in small supplier numbers during 2014, with 3 new companies entering the market.

Within the non-domestic market, there were 38 active suppliers at the end of 2014, 3 more than the total number of active suppliers at the end of 2013.

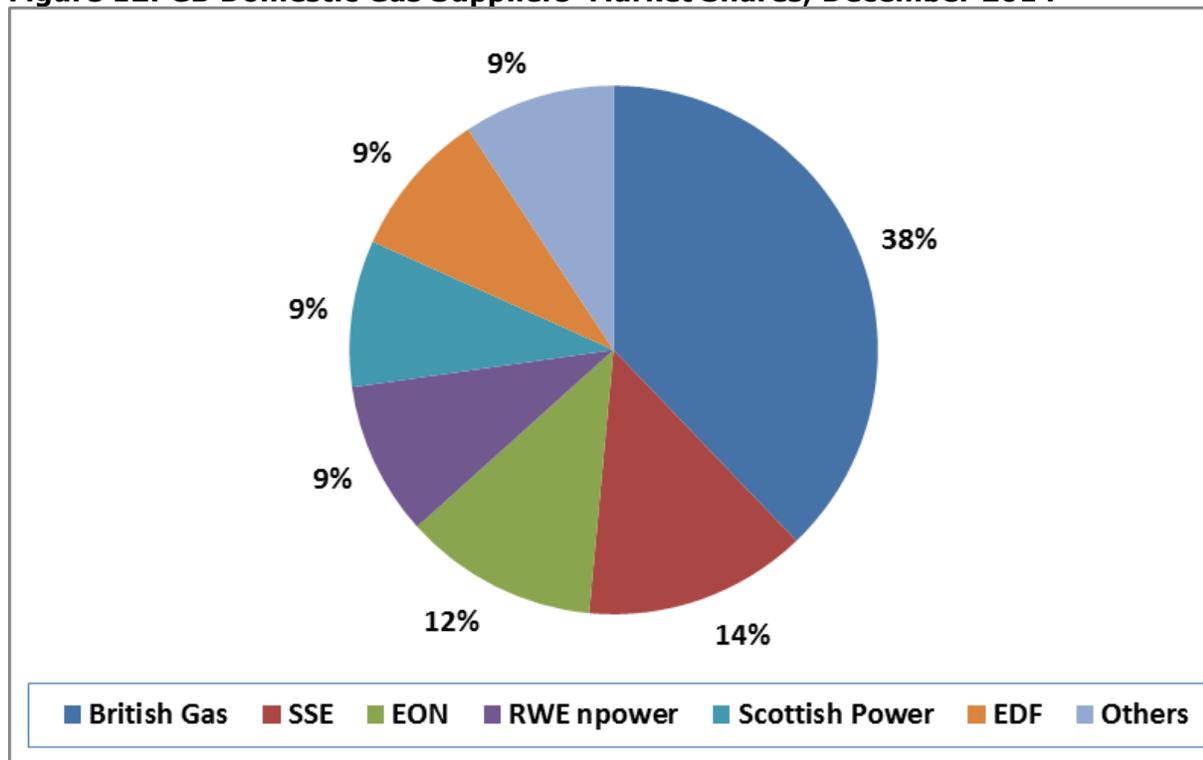
Monitoring the effectiveness of market opening and competition

Domestic market shares

In December 2014 there were 21m domestic gas consumers in GB. As Figure 12 shows, the former incumbent suppliers accounted for 91 per cent of gas supply to these customers, down from 95 per cent in 2013.

The 19 independent gas suppliers active in the domestic market had a combined market share of 9 per cent in December 2014. Independent suppliers operating in the market are Axis Telecom; Better Energy; Co-Operative Energy; Dali Gas; Economy Energy; ecotricity; E (Gas & Electricity); Extra Energy; First Utility; Flow Energy; Gnergy; Good Energy; Green Energy; Green Star Energy; OVO Energy; Spark Energy; Utility Warehouse; Utilita; Zog Energy.

As a group, independent suppliers' market share increased by four percentage points in the period December 2013-2014.

Figure 12: GB Domestic Gas Suppliers' Market Shares, December 2014

Source: Ofgem analysis of Xoserve gas meter point data

Non-domestic market shares¹¹⁴

The non-domestic gas market is characterised by a larger number of independent suppliers compared to the domestic gas market. In addition to the former incumbent suppliers, there are 32 independent suppliers, with varying focus and market share across two main segments: one for meter points with annual average consumption below 732,000 kWh (Small Annual Quantity, proxy for small business customers), and the other for meter points with annual average consumption above 732,000 kWh (Large Annual Quantity, proxy for large business customers).

As Table 5 shows, in the segment of small business customers British Gas is the leading supplier, as in the non-domestic market as a whole. Its market share is eroding over time and has gone down by 2 per cent relative to 2013. Independent suppliers Opus and Contract Natural Gas have increased their market shares approximately by 1 per cent each, while other suppliers' shares have remained relatively unchanged.

International producers have a strong presence in the segment of large business customers, the leading one being Total Gas and Power, which has increased its market share by 1% compared to 2013. SSE has registered the largest increase, of around 3%. The largest loss, of 3%, was recorded by EON, while GdF, Corona, Gazprom and British Gas all registered small losses, below 1%.

¹¹⁴ The data presented in this report is based on number of supply points. However, it should be noted that market shares by volume may show a different story as some suppliers may have a low number of supply points which have however very high volumes of energy supplied.

Table 5: Gas Suppliers' non-domestic market shares December 2014

Gas Supplier	Non Domestic Sites		
	<732 MWh Annual Quantity	>732 MWh Annual Quantity	All Non Domestic
British Gas	36.3%	7.9%	33.4%
EON	15.7%	8.0%	14.7%
Total Gas and Power	10.6%	26.9%	11.5%
RWE npower	7.3%	2.8%	6.8%
Contract Natural Gas Ltd	5.7%	0.7%	5.2%
Corona	5.0%	18.4%	7.3%
SSE	4.4%	7.5%	4.3%
Gazprom	4.3%	14.4%	5.2%
Opus	4.1%	0.1%	3.8%
Dong	0.8%	4.8%	0.9%
GDF Suez	0.5%	4.7%	0.6%
Regent Gas	0.4%	1.8%	0.5%
Business Energy Solutions	0.3%	0.1%	1.4%
Crown Energy	0.3%	0.8%	0.4%
Economy Gas	0.1%	0.0%	0.1%
ENI Trading and Shipping	0.0%	0.7%	0.0%
Others	4.0%	0.5%	3.7%
Total	100.0%	100.0%	100.0%

Source: Ofgem analysis of Xoserve meter point data

HHIs

HHIs¹¹⁵ indicators are often used to gauge market concentration. Though HHIs do not provide conclusive evidence on the level of competition, they offer pointers as to whether there are potential risks to the market not delivering competitive outcomes. The relevant HHIs for gas in December 2014 were as follows (2013 figures in brackets):

- domestic – 2,094 (2,190)
- non-domestic, small businesses – 1,861 (2,063)
- non-domestic, large businesses – 1,510 (1,514)

Both gas domestic and non-domestic small business segments are 'highly concentrated' according to the threshold HHI levels (1,800) used by the Competition Markets Authority. In both segments the HHI has fallen in 2014 relative to 2013. The gas non-domestic large business segment is judged to be 'concentrated', being above the 1,000 threshold. It has remained almost unchanged relative to 2013.

Prices for household consumers including prepayment systems

All final consumer prices in the GB retail energy markets are determined by market forces as all price controls on final consumer prices were lifted by April 2002. However, there are elements of the final price which are attributable to the regulated aspects of the market, in

¹¹⁵ HHI is commonly used to assess market concentration, ranging from 10,000 for a monopoly to just above zero for perfect competition. The Competition Markets Authority in the UK categorise a market as 'concentrated' if its HHI exceeds 1,000 and 'highly concentrated' if its HHI exceeds 1,800.

particular distribution, metering and transmission charges, which continue to be price controlled. There are also a number of other costs that influence how suppliers set retail gas prices including wholesale energy costs, and the costs of the UK Government's environmental and social policies such as the Renewable Obligation and the Warm Home Discount which can vary over time.

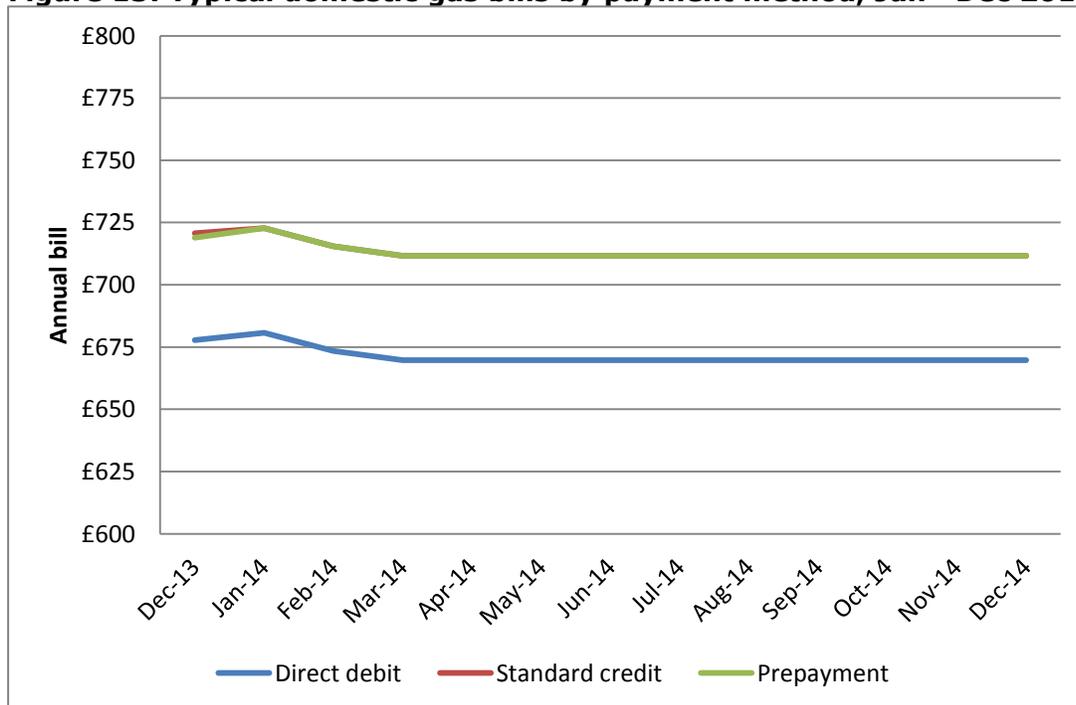
We use the SMI (see section 3.2.2) to explore the relationship between retail bills and these costs.¹¹⁶

Ofgem actively monitors domestic suppliers' gas prices across GB. We receive price change notifications from suppliers but also contract with Energylinx, an independent data provider and one of the comparison sites accredited by the Confidence Code run by Ofgem. Ofgem uses this information to calculate the implications for domestic customers' retail bills based on characteristics such as their consumption level, payment type, and region.

Over the last year, we have observed an increase in the number of fixed-price tariffs that domestic energy suppliers offer, with most fixed deals being priced at a discount relative to variable tariffs. The cheapest fixed deals were generally offered by smaller suppliers.

Figure 13 shows the change in average domestic gas bills in GB's gas market between January and December 2014. Overall, average gas bills decreased by 1 per cent (£8) over the year. The standard credit and prepayment prices were the same from January 2014 to December 2014.

Figure 13: Typical domestic gas bills by payment method, Jan– Dec 2014



Source: Ofgem analysis of Energylinx data

Notes: 1) Average of Big six's standard variable tariffs, 2) Revised consumption level: 13,500 kWh per year

¹¹⁶ <https://www.ofgem.gov.uk/gas/retail-market/monitoring-data-and-statistics/understanding-energy-prices-great-britain/supply-market-indicator>.

Domestic switching rates

Consumers' ability to switch their energy supplier is important for a well-functioning, competitive energy market, although it must not be considered in isolation. Ofgem monitors switching rates together with pricing and market structure data on an ongoing basis.

In 2014, approximately 2.3m domestic consumers switched their gas supplier, equivalent to 190,000 per month. This is a switching rate of 10.8 per cent, almost unchanged relative to 2013. We also saw an increase in switching away from the six largest suppliers, on average 47 per cent of customers that switched during 2014 moving to smaller suppliers and a slight increase in December 2014.

On the other hand, we noted an increase in customers switching internally to different tariffs, payment methods and type of account management with their existing supplier. The total internal switching rate has been approximately four times higher than the switching rate between suppliers for the final quarter of 2014, while internal switching only reflecting an active tariff choice has been approximately twice as high.

The speed and reliability of switching is also important (see chapter 5.1 for our change of supplier project within our smarter markets programme of reforms). In December 2014, the system average time¹¹⁷ to complete a switch was down to 19 days in gas (from 24 days in June and 23 in September).

Our consumer surveys provide an additional source of information on the consumer switching experience. The Ipsos Mori Tracking Survey 2014¹¹⁸ found that 58 per cent of gas customers could not recall ever having switched supplier, down from the 63 per cent in 2012.

Consumer survey data also shows that 13 per cent customers reported having switched gas supplier in the last year. From those who did not switch suppliers in the last year, 12 per cent changed tariffs, and 4 per cent changed payment methods within their own supplier.

Non-domestic switching activities

In 2014, 115,000 non-domestic consumers switched their gas supplier, equivalent to an average of approximately 9,600 per month. This represents an annual switching rate of 15%, above the domestic switching rate of 10.8%.

In March 2015 we published our quantitative survey on micro and small business consumer engagement,¹¹⁹ covering both gas and electricity markets. It showed that around one in four smaller business customers (23 per cent) reported having switched suppliers in the last year, rising to nearly three in five (60 per cent) over the last five years.

Businesses appear to be making informed switching decisions. Respondents who had switched over the last five years reported that, on average, they had contacted more than three suppliers directly or via energy brokers.

¹¹⁷ This is the average number of calendar days from the day when the supplier notifies the switching request to the network operator system until the day the switch is executed.

¹¹⁸ <https://www.ofgem.gov.uk/ofgem-publications/88375/customerengagementwiththeenergymarket-trackingssurvey2014finalpublished2662014.pdf>.

¹¹⁹ [Micro and Small Business engagement in the Energy Market 2015. Quantitative Research Report.](#)

Non-domestic switching is primarily price-driven and cost saving was by far the most likely reason for switching (78% of those who had switched in the last 5 years found or were offered a lower price contract or tariff the last time they switched). Receiving a renewal notice from an existing supplier was a significant trigger for switching (47% citing this as a reason), as was the recommendation from a broker (31%).

On the other hand, this research also showed that two in five smaller businesses have never considered switching.

Among businesses that have not switched in the last 5 years, satisfaction with the current supplier was a key reason for not switching (60% of non-switchers). Being tied to an existing contract was also significant (41%). A minority of around one in five cited the perceived complexity and the time it takes to switch (19%) and scepticism of the savings that could be made from switching (19%) as reasons for not switching.

Consumers and suppliers have also expressed concerns that transfer blocking ('Objections') rules set out in licences and industry codes are not adhered to in some circumstances. The impact of objections can be significant for consumers.

Ofgem has proposed to lead the industry towards reliable next day switching by 2019. We want to take a fresh look at whether objections should be part of a redesigned switching process or whether suppliers should develop other ways of managing risk. This work has commenced with a recent call for evidence.

4.2.2.2 Recommendations on supply prices, investigations and measures to promote effective competition

Ofgem's work in accordance with the above heading is cross-cutting, i.e. it applies to both the electricity and gas markets. As a result, it has been covered in the retail market overview in section 3.2.2.

4.3 Security of supply

Under Article 5 of the Gas Directive, Member States have to ensure the monitoring of security of supply issues.

No single body is responsible for ensuring security of supply as we rely on the market to provide us with this. However, the Government sets the overall energy policy on energy security. Ofgem is responsible for regulating the market and National Grid, as operator of GB gas system, has responsibility for ensuring that supply meets demand on a minute-by-minute basis each day.

In October 2014 we published our joint Statutory Security of Supply Report (SSSR)¹²⁰ alongside DECC. This is part of an obligation¹²¹ on us and the Government to report annually to Parliament on the availability of electricity and gas for meeting the reasonable demands of consumers in GB. The report concluded that GB's gas market continues to function well with sufficient capacity and the ability to deliver to meet demand.

The report also noted that the market itself is best placed to allocate risk and weigh up the 'correct' level of capacity redundancy which delivers the best value for consumers. In the past three years, GB has experienced periods of relatively high demand – particularly in March/April 2013 – and periods of low demand – for instance during summer 2014. In all scenarios, the market has responded and the gas system has met demand without issues. GB has never suffered a gas deficit emergency and the likelihood of having an emergency remains low.

Ofgem's reform of the gas cash-out mechanism and the Gas Significant Code Review, will sharpen the incentives on gas market participants to invest in measures to enhance security of supply.

¹²⁰ <https://www.gov.uk/government/publications/statutory-security-of-supply-report-2014>.

¹²¹ Under section 172 of the Energy Act 2004 as amended by section 80 of the Energy Act 2011.

5. Consumer protection and dispute settlement in electricity and gas

The following chapter contains details of our consumer protection and dispute settlement work in both the GB gas and electricity sectors during 2014. This includes developments in the domestic and non-domestic sectors and further information on smart metering and smarter markets, our consumer vulnerability strategy and protecting consumers.

5.1 Consumer protection

According to articles 37(1)(n) of the Electricity Directive and 41(1)(o) of the Gas Directive, Ofgem must help to ensure that consumer protection measures are effective and enforced, especially as new technology enters the market. Here we report on the following aspects of current and future consumer protection during 2014: smart metering; the smarter markets programme; access to consumption data, consumer vulnerability strategy and how we protect vulnerable consumers.

Smart metering

The Government has decided to implement the smart meter rollout through regulation and the rollout will be led by energy suppliers. Licence conditions require suppliers to take 'all reasonable steps' to ensure that smart metering systems which comply with the Smart Meter Equipment Technical Specifications are installed in domestic and smaller non-domestic premises by the end of 2020.

Ofgem continued throughout 2014 to provide independent advice and expertise for the Government's Smart Meter Implementation Programme. We now play a key role in monitoring and, where appropriate, enforcing compliance with the new regulatory obligations relating to smart meters to ensure that the interests of consumers remain protected during the transition to smart metering.

Regulating energy suppliers

The deadline for rollout of advanced gas and electricity meters to larger non-domestic was April 2014. By that time, only 75% of electricity meters and 86% of gas meters had been upgraded to 'advanced meters'. This outcome was disappointing and suppliers are continuing to install the advanced meters.¹²² Ofgem opened investigations against three suppliers regarding their rollout performance¹²³ and we are monitoring the progress of all suppliers in improving their April 2014 completion rate.

In October 2014, we published our decision that during the domestic smart meter rollout, suppliers must provide us with their plans for the rollout, set annual milestones and meet the commitments previously set.

Regulating the Data and Communications Company (DCC)

The Smart Communication licences were awarded by the Secretary of State to Smart DCC Ltd¹²⁴ on 23 September 2013 (referred to as 'DCC') under the Gas Act and under the

¹²² <https://www.ofgem.gov.uk/ofgem-publications/89289/amropenlttrfinal.pdf>.

¹²³ <https://www.ofgem.gov.uk/publications-and-updates/ofgem-opens-investigation-british-gas-e.-and-npower-over-advanced-meter-roll-out-performance>.

¹²⁴ Smart DCC is a subsidiary of the Capita Group.

Electricity Act. The DCC has an important role in providing secure communications between energy suppliers, network operators and authorised third parties.

A key objective of the DCC is to secure the interoperability of the operation of smart meters when a customer switches supplier. Industry is working closely with government on the establishment of technical standards that will enable smart meters to be operated by the DCC and for suppliers to be able to communicate with the DCC.

The DCC is governed by its licences which set out its core obligations, restrictions and entitlements. It is also bound by the industry's Smart Energy Code, which outlines the DCC's contractual relationship with its users and allows them to gain access to DCC services. Ofgem has monitored the DCC during 2014 to ensure it abided by its licence conditions.

Our monitoring included annual ex post price control arrangements and the approval of DCC's charging statements. During 2014, we assessed DCC's costs, revenues and activities during its first six months of operations, and published our first price control decision in February 2015.

Suppliers are currently installing the first generation of meters that comply with the government's Smart Meter Technical Equipment Standard. Meter manufacturers are currently finalising the development of the second generation of equipment that will be operated by the DCC. A programme of development and testing is planned before the main installation phase is expected to begin in late 2016.

Smarter Markets Programme

The roll-out of smart metering has the potential to make retail energy markets work better for consumers. However, this will require reforms to the arrangements that govern how market participants interact with each other and consumers. We are continuing to progress work to deliver necessary reforms through the Smarter Markets Programme. Our work covers the change of supplier process, the electricity settlement process and consumer empowerment and protection. Key achievements in 2014 were as follows:

Change of supplier:

To increase switching reliability we have made changes to suppliers' licences, including new obligations on suppliers not to erroneously transfer consumers. We have also worked with the industry to halve switching timescales to 17-days (including, where applicable, the 14-day cooling off period for domestic consumers). In June 2014, we published a consultation on moving to reliable next-day switching. We proposed to do this by bringing together the existing separate gas and electricity switching arrangements into a single centralised service run by the DCC.

Electricity settlement:

This process is central to working out how much energy suppliers need to buy and the charges they pay to transport it to consumers. Improving the accuracy of settlement by using half-hourly consumption data will help to create the right environment for demand-side response. In 2014, we worked with the industry to develop and shortlist options for using half-hourly consumption data from smart meters in the settlement process for domestic and smaller business consumers. We also approved a change during 2014 to settlement that will require larger business consumers to be settled using their half-hourly consumption data.

Consumer empowerment and protection.

In early 2014, we consulted on a programme of work to ensure that the regulatory arrangements empower and protect consumers in a market with widespread deployment of smart metering and the transition to it. In September, we published the updated work programme taking into account the consultation responses. This programme should help consumers to make the most of smart meter benefits.

Ensuring access to consumption data

Suppliers are required to provide gas and electricity consumption data to their customers, if requested by the customer. Following the introduction of the data access and privacy licence conditions, Ofgem has monitored these in 2014 and will continue to do so, enforcing breaches as required.

The Government also introduced licence obligations as part of the implementation of the Energy Efficiency Directive, which require suppliers to give domestic consumers easy access to certain consumption data on their smart meters. Ofgem monitor and, where appropriate, enforce any licence obligations on suppliers.

Domestic consumers

Unreturned closed account credit balances

When a consumer closes their account with a supplier (if they are switching or changing tenancy) it is possible that they are owed money. This may be because the latest bill was estimated, or because fixed direct debit calculations resulted in a positive overall credit balance. Ofgem found unacceptably large amounts of money held by suppliers in closed account balances and called on suppliers to return this money and improve their policies and practices. In 2014, suppliers publically committed to steps to return this money and developed minimum common actions to improve their practices in the futures.

Monitoring suppliers' social obligations

In 2014, we continued to collect social obligations reporting from domestic suppliers. This data helps us to:

- identify areas for future policy work
- monitor supplier performance and determine if suppliers are complying with their licence conditions (relating to customers who have a disability, a chronic sickness, are of pensionable age, or are on low incomes)
- identify and assess particular issues of concern with supplier performance
- encourage best practice through the publication of data

Our latest quarterly and annual reports can be found at our Social Obligations Monitoring webpage.¹²⁵

Energy Best Deal

2014 was the seventh year of a successful partnership with Citizens Advice (a registered charity that provides free and independent advice to consumers) delivering the Energy Best Deal. The campaign provides Citizens Advice advisers and other advice workers with the training needed to deliver face-to-face advice to lower income households on energy rights and how to get the best from their energy deal.

10,349 consumers and 5,408 frontline workers attended Energy Best Deal sessions in 2013-14. An independent evaluation of Energy Best Deal in this period found that 97% of

¹²⁵ <https://www.ofgem.gov.uk/about-us/how-we-work/working-consumers/supplier-performance-social-obligations>.

consumers found the session useful and that 35% had taken action to get a better deal on their energy bills since the session. In addition 4,318 consumers received one-to-one 'Energy Best Deal Extra' advice.

Debt Assignment Protocol

In 2014 we concluded our review of the process that is used to transfer debt between suppliers where indebted prepayment meter customers try to switch. We identified a number of issues with the process that result in a poor customer experience and contribute to a low switching rate among this customer group. Ten of the largest suppliers committed to change their processes by end-April 2015. We also committed to update our regular monitoring which we will use to evaluate the impact of these changes.

Non-domestic consumers

Protecting businesses from misleading marketing

The Business Protection from Misleading Marketing Regulations 2008 includes a number of protections such as the prohibition of advertising products in a way that misleads traders. They also set out conditions under which comparative advertising to consumers and Business is permitted. In November 2013 we were given concurrent powers with the CMA to enforce the regulations in the energy sector.

Back billing

Back billing happens when suppliers do not bill a customer for some time, only to later issue a bill for energy that has been used, but not previously billed. Ofgem continued to monitor suppliers' practices in 2014 in relation to micro-businesses back-billing. Suppliers have started moving towards a one year back-billing limit and after 2014, a number have committed to this one year limit.

Protecting domestic and non-domestic consumers

Consumer Vulnerability Strategy

The Consumer Vulnerability Strategy and associated work programme was published in July 2013 and in 2014 we have updated it to reflect new research, activity and insight.

Guaranteed Standards of Performance

In 2014 we consulted on reforming the supplier Guaranteed Standards of Performance. This included issuing a draft Statutory Instrument. We used these consultations to build on the data previously gathered and we intend to finalise our reforms in 2015. Our proposals will see a revised performance standards regime featuring standards on appointments, fixing faulty metering, fixing faulty prepayment meters, and reconnection following disconnection for debt. Our proposals will see consumers receive £30 where a supplier fails a performance standard.

Consumer Insight and engagement

In 2014, we continued to commission and publish a wide range of research to inform policy decisions and put consumer perspectives at the heart of our regulatory processes. We listen to consumers through regular surveys and workshops, and through innovative approaches such as video research and ethnographic in-home interviewing. Some examples from 2014 include:

- Qualitative research with a range of business customers to understand their views of the electricity connections market.
- Quantitative research with non-domestic (business) consumers to track their engagement and satisfaction with the energy market.

- Research commissioned to understand the impact of advice received by vulnerable consumers through the Government's Warm House Discount scheme. This was accompanied by ethnographic 'pen portraits' to enable stakeholders to see first-hand the impact of these schemes.
- A large quantitative study to act as a baseline to monitor how market engagement changes going forward.
- Our annual tracking survey continued to monitor consumer engagement in the market.

5.2 Dispute settlement

Under Article 37(11) of the Electricity Directive any party that has a complaint against a transmission or distribution system operator in relation to that operator's obligation may refer the complaint to the regulatory authority. Each regulatory authority is required to issue a decision within two months following receipt of the complaint. Member states are required to ensure that regulatory authorities have the powers to enable them to make such decisions.

Sections 44B-D of the Electricity Act set out our determination functions and procedures under Article 37 of the Electricity Directive. These sections were amended by the Electricity and Gas (Internal Markets) Regulations 2011. Under Article 37, any dispute that is referred to us for determination is determined by us or, if we think fit, by an arbitrator appointed by us. The decision is binding on the parties to the dispute. However any party can seek a judicial review of our decision.

No new Article 37 disputes were raised in 2014. In March 2014 the Authority reached a decision on one Article 37 dispute, first raised in 2012. The dispute related to which party had responsibility for enabling third party access to a licence exempt distribution system at Heathrow Airport. One of the parties subsequently sought a judicial review of this decision. In November 2014 the judicial review was granted and the matter was remitted to the Authority for our reconsideration.

Sections 27B-D of the Gas Act 1986 set out our dispute resolution functions and procedures under Article 41(11) and Article 41(4)(e) of the Gas Directive. They were amended by the Electricity and Gas (Internal Markets) Regulations 2011. Under Article 41, any dispute that is referred to us for determination is determined by us or, if we think fit, by an arbitrator appointed by us. The decision is binding on the parties to the dispute. However any party can seek a judicial review of our decision. No Article 41 disputes were raised in 2014.

6. Glossary

A

ACER

Agency for the Cooperation of Energy Regulators

B

BBL

Balgzand Bacton Leiding Company

BETTA

British Electricity Trading Arrangements

BSC

Balancing and Settlement Code

BSUoS

Balancing Services use of System

C

CAM

Capacity Allocation Mechanism

CEER

Council of European Energy Regulators

CESP

Community Energy Saving Programme

CERT

Carbon Emissions Reduction Target

CfD

Contracts for Difference

CM

Capacity Market

[CMA](#)

Competition and Markets Authority

[CMP](#)

Congestion Management Procedures

[CMU](#)

Capacity Market Unit

[CSS](#)

Consolidated Segmental Statements

[CUSC](#)

Connection and Use of System Code

D

[DCC](#)

Data and Communications Company

[DECC](#)

Department for Energy and Climate Change

[DNO](#)

Distribution Network Operator

[DPCR5](#)

Distribution Price Control Review 5

[DSO](#)

Distribution System Operator

[DUoS](#)

Distribution use-of-system

E

ENS

Energy Not Supplied

EWIC

EirGrid East-West Interconnector

G

GB

Great Britain

GDN

Gas Distribution Network Company

H

HHI

Herfindahl-Hirschman Index

I

ICE

Intercontinental Exchange

IFA

Interconnexion France-Angleterre

IOSCO

International Organisation of Securities Commissions

ITPR

Integrated Transmission Planning and Regulation

L

LDZ

Local Distribution Zones

LNG

Liquefied Natural Gas

LOLE

Loss of Load Expectation

M

MFE

Minor Facility Exemption

MIR

Market Investigation Reference

MPP

Multiple Purpose Project

N

NBP

National Balancing Point

NETA

New Electricity Trading Arrangements

NGET

National Grid Electricity Transmission

NGG

National Grid Gas

NGGT

National Grid Gas Transmission

NGIL

National Grid Interconnectors Limited

NRA

National Regulatory Authority

nTPA

negotiated Third Party Access

NTS

National Gas Transmission System

O

OCM

On-the-day Commodity Market

OFT

Office of Fair Trading

OFTO

Offshore Transmission Owners

OTC

Over the Counter

R

REMIT

Regulation (EU) No 1227/2011 of the European Parliament and of the Council on wholesale energy market integrity and transparency adopted on 8 December 2011

RMR

Retail Market Review

rTPA

regulated Third Party Access

S

SMI

Supply Market Indicator

[SMICOP](#)

Smart Metering Installation Code of Practice

[SO](#)

System Operator

[SSEPD](#)

Scottish and Southern Energy Power Distribution

[SWW](#)

Strategic Wider Works

T

[TCLC](#)

Transmission Constraint Licence Condition

[The Electricity Directive](#)

2009/72/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in electricity

[The Gas Directive](#)

2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas

[TNUoS](#)

Transmission Network Use of System

[TPI](#)

Third Party Intermediaries

[TSO](#)

Transmission System Operator

U

[UNC](#)

Uniform Network Code

[UTCCR](#)

Unfair Terms in Consumer Contracts Regulation 1999

[UCTA](#)

Unfair Contract Term Act 1977

Northern Ireland National Report 2015



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1 Foreword

Protecting the short and long term interests of consumers is what we are about. Striking the right balance in doing our job is what we aim for. We don't regulate energy utilities in Northern Ireland in isolation from what is happening elsewhere.

Developments in the wider environment have an impact on our work. European legislation to promote energy competition is the basis for the major project to deliver a new wholesale electricity market, the I-SEM, for the island of Ireland. Other EU legislation such as the energy efficiency directive continues to be an important backdrop for our regulation.

Changes to the UK's competition arrangements, and the Competition and Markets Authority (CMA) inquiry into the energy supply market is an important context for our work. We have also increased our involvement with the UK Regulators' Network (UKRN) and the UK Competition Network (UKCN) as a tangible sign of our desire to be an even better regulator by learning from others and sharing experiences and insights.

Our objective is to add value in a Northern Ireland context. We contributed to the Assembly's Enterprise, Trade and Investment Committee electricity policy inquiry. The shared statutory objectives which we have with the Department of Enterprise, Trade and Investment (DETI) means that we work closely with them across the range of our energy responsibilities.

Engagement with industry and consumers is important to us. Our intentions are clear: we will respond positively to opportunities to meet and engage with stakeholders. During the last year our Board had the opportunity to meet with the leadership team of several companies. Our Board also approved a memorandum of understanding with the Commission for Energy Regulation and the Consumer Council for Northern Ireland. We also sought to reach out to consumer interests across Northern Ireland and our Board conducted visits and meetings in Fermanagh and Londonderry/Derry during the year.

Recognising that we work in a complex environment helps us to appreciate that we can't deliver without the involvement and co-operation of others. Following the publication of our Corporate Strategy 2014-2019 in May 2014 we have focused on delivering our strategy objectives. It is pleasing to note the progress that has been made during the first year of our five-year strategy.

My non executive board colleagues and I would like to express our appreciation and gratitude to our staff for the progress that has been made during the last year which is testament to their enthusiasm and commitment. I would also like to thank my board colleagues for their ongoing support and dedication.

Bill Emery

Chairman, Utility Regulator

2 Main developments in the gas and electricity markets¹

Main conclusions of the report and a general evaluation of market development and regulation.

2.1 Electricity

We published our price control determination for the period 1 January 2013 - 30 September 2017 (called RP5) on 23 October 2012. Our determination followed a public consultation on our proposals, which were published in April 2012. A separate public consultation was also conducted on an element of the final price control, relating to NIE Transmission and Distribution (NIE T&D) capitalisation practice. The final determination included a decision on the NIE T&D capitalisation practice. NIE T&D rejected our determination in November 2012. In 2013 the price control was referred to the Competition Commission (CC). After significant engagement with the CC during its inquiry, a provisional determination was published in November 2013. A further period of engagement preceded the publication of the CC's final determination by us in April 2014.

The Single Electricity Market (SEM) continues to deliver benefits to consumers. The SEM ensures there is greater transparency around the costs of generation ensuring appropriate costs for consumers. Further development of new generation on the island of Ireland has increased investment and competition in the wholesale market.

The Market Monitoring Unit (MMU), which is based at our offices, has continued to monitor the SEM over the past year. The MMU engaged with generators and operators to monitor compliance with the market rules.

The Third Internal Energy Market Package (IME3) has continued to promote the liberalisation of the energy market across the European Union (EU). IME3 requires the separation of the transmission network from generation and supply (this is called unbundling). IME3 specifies several unbundling options to ensure separation of the transmission network from generation and supply.

We are required to certify transmission system operators as being in compliance

¹ This report covers developments during the period from January 2014 to December 2014. Where data for the is provided 2014 is the appropriate reference year.

with the full ownership unbundling requirements or one of the alternative unbundling models set out in IME3.

During 2014, the Utility Regulator finalised TSO certification applications from NIE T&D, SONI and Mutual Energy Ltd (Moyle interconnector). This followed on from work in 2013 whereby the Utility Regulator issued a preliminary decision to the European Commission (EC) in February of that year. The preliminary decision recommended qualified approval for the current Transmission System Operator (TSO) arrangements on the island of Ireland. In April 2013 the Commission set out its decision relating to TSO certification in Northern Ireland. The Commission considered that the arrangements of transmission system operation in Northern Ireland, which are shared between SONI and NIE, deliver more effective independence than the independent transmission operator (ITO) model. The Commission agreed that the arrangements meet the requirements of Article 9(9) of the Directive therefore SONI should be certified as the transmission system operator for Northern Ireland. The final decisions relating to certification for Mutual Energy², NIE³ and SONI⁴ were published on 26 June 2014. Licence modifications have also been completed in respect of TSO certification.

Further progress has been made to ensure that our electricity market is compatible with the European Target Model. The SEM will require significant modifications to implement the Target Model. The magnitude of change required for the SEM to achieve this is considerably greater than most other markets in Europe. This is due to its centralised, gross mandatory pool design which differs in a number of key respects from the prevailing market design in most other European Member States.

The first key deliverable is increasing the efficiency of cross border electricity trading in all European electricity markets by 2014. For the island of Ireland this will be 2017 (given the greater changes required to the market). This will be a legal requirement on Member States.

Working with CER colleagues on the SEMC will create a new electricity market for the Republic of Ireland and Northern Ireland from 2017. We call this the Integrated Single Electricity Market (I-SEM). It is expected that the benefits of the

²

http://www.uregni.gov.uk/publications/moyle_interconnector_tso_certification_final_decision_letter_26_june_2014/

³ http://www.uregni.gov.uk/publications/nie_tso_certification_final_decision_letter_26_june_2014/

⁴ http://www.uregni.gov.uk/publications/soni_tso_certification_final_decision_letter_26_june_2014/

I-SEM will be market transparency and efficiency of interconnection with the wider European market. The I-SEM will also facilitate increased competition in the electricity market in Northern Ireland and Ireland. The high-level design for the I-SEM was published on 17 September 2014⁵ setting out the key features of the wholesale electricity trading arrangements.

⁵http://www.allislandproject.org/en/wholesale_overview.aspx?article=d3cf03a9-b4ab-44af-8cc0-ee1b4e251d0f

2.2 Gas

In 2014 the rollout of the gas distribution network in Northern Ireland (NI) continued across both distribution areas with 182,000 properties now connected in the Greater Belfast distribution area of PNGL (Phoenix Natural Gas Ltd) and 25,000 properties now connected in the ten towns distribution area of FE(firmus energy). The number of properties that are readily connectable, including connected properties, is 383,000. This represents nearly 54% of properties within NI.

Natural gas is not available in much of the west of NI. During 2014 the Utility Regulator conducted a competitive process to award high pressure and low pressure gas conveyance licences that will see the Northern Ireland network extended to a number of towns and major industrial facilities in the western half of the region. There was a three month application period between February and May 2014. Four applications were received for each of the high pressure and low pressure licences to be awarded. The Utility Regulator announced its [final decision](#) in November 2014, subject to consultation on licences. The high pressure network licence was awarded to Northern Ireland Energy Holdings while the low pressure licence was awarded to Scotia Gas Networks. It is expected that the first consumer will be connected in the second half of 2016 with all the towns being connected by Q4 of 2017.

2014 was the first applicable year of the GD14 Price Control. The GD14 determination was published on the 20 December 2013 and covered both DSO's, PNGL and FE.

We are continuing to progress arrangements for harmonising gas transmission systems as required by the EU Gas Regulation (EC) 715/2009 and the network codes. We also work closely with OFGEM and Commission for Energy Regulation (Ireland) on cross-jurisdictional issues.

3 The electricity market

3.1 Network regulation

3.1.1 Unbundling

Report on TSO certification, DSO provisions regarding branding and resources and new developments regarding certification revisions

- Articles 10,11 2009/72/EC and Article 3 Regulation (EC) 714/2009
- Article 26

NIE (the transmission owner) applied for certification under Directive 2009/72/EC on 30 January 2013 on the grounds of Article 9(9) of the Directive. By the date of application NIE ownership had been acquired by ESB which had extensive generation and supply interests in the SEM. The SEM Committee (SEMC), which had determined that TSO certification was a SEM matter, issued its preliminary decision to the EC on 12 February 2013. This recommended certification subject to certain qualification measures including transfer of the transmission planning function from NIE to System Operator Northern Ireland (SONI). The EC made a decision to approve the certification of SONI subject to the qualification measures in the SEM Committee preliminary decision and to some additional measures. The decision on certification for SONI was taken in June 2014, and the relevant licence changes have now been implemented.

Moyle Interconnector Limited, which owns the electricity interconnector between Northern Ireland and Scotland, applied for certification on the grounds of ownership unbundling on 25 January 2013. The SEM Committee issued a preliminary decision to the EC on 7 May 2013 recommending certification subject to certain qualification measures. The European Commission did not raise any objections to certification of Moyle Interconnector Limited as a fully unbundled TSO. The decision on certification for SONI was taken in June 2014, and the relevant licence changes have now been implemented.

3.1.2 Technical functioning

- Balancing services (Article 37(6)(b), Article 37(8))
- Security and reliability standards, quality of service and supply (Article 37(1)(h),)

Report relevant security and reliability regulation and data

- Monitoring time taken to connect and repair (Article 37(1)(m))

Clarify here at least if there is in your country a definition for “time to connect” for consumers and for producers

- Monitoring safeguard measures (Article 37(1)(t))
- RES regulatory framework: Report on connection, access and dispatching regimes for RES-E, in particular on priority issues. Report also on the balancing responsibility for RES-E. (Article 11 Regulation (EC) 713/2009)

The wholesale electricity market in Ireland (SEM) is a gross mandatory pool, with energy prices set ex-post. Balancing services are paid for through imperfections charges, constraint payments and make whole payments. These are pass-through costs; generators recover their short-run marginal costs. SONI is obliged under its licence to take into account the quantity, nature and cost when purchasing System Support Services.

Monitoring of security and reliability standards, time taken to connect and repair and safeguard measures are currently conducted through licence compliance. Transmission licences are held by NIE, Moyle and SONI.

The loss of load expectations statistic is used by SONI as a security standard, which is concerned with the likely number of hours of shortage in a year. The security standard for NI is 4.9 hours per annum and if this standard is exceeded it indicates a higher than acceptable level of risk.

The System Operator, SONI, annually publishes the Generation Adequacy Statement⁶ which provides its forecast of generation capacity and forecast electricity demand for the upcoming ten-years. This allows for the assessment of capacity margins and identifies areas in which these could be increased, which highlights area of potential future investment. Above all the Generation Capacity

⁶ http://www.eirgrid.com/media/All-Island_GCS_2013-2022.pdf

Statement provides an estimation of future security standards based on expected generation capacity margins.

3.1.3 Network tariffs for connection and access

- Article 37(1)(a), Article 37(6)(a), Article 37(8), Article 37(10), Article 37(12) , art 37(3)(c) and (d)

Report on relevant new tariff regulation provisions

- Prevention of cross-subsidies (Article 37(1)(f))

Specify the methodology used in tariff regulation (i.e. cost plus vs incentive regulation), the method of checking undertaking's cost data, methodology for allocation of costs to grid users and if benchmarking is used please describe methodology used by NRA

Electricity Suppliers in Northern Ireland pay a number of regulated charges which they pass on to their customers. Regulated charges for the use of the electricity distribution network in Northern Ireland and a levy known as the Public Service Obligation (PSO) are set by NIE and SONI, and the maximum amount recoverable is approved by the Utility Regulator. The "Regulated Tariffs Values" for the tariff year beginning October 2014 was published by the Utility Regulator on 22 Aug 2014⁷, detailing the use of system tariffs for that year.

The transmission network owner in NI is NIE plc. NIE is also the distribution system owner and operator. The current 5 year price control commenced in 2012. NIE is allowed revenue and therefore annual Distribution Use of System tariffs (DUoS) are determined by the terms of this price control. It also receives a Use of System allowance (UoS) from the TSO. The allowed capital expenditure (CAPEX) is limited (e.g. replacement of assets.) with exceptional items individually approved by the regulator. During 2009 work began on the fifth price control for NIE plc, to run from 2012. Following the rejection of this price control (called RP5) by NIE T&D we referred the matter to the Competition Commission (CC) in April 2013.

After significant engagement with the CC, a provisional determination was

⁷http://www.uregni.gov.uk/uploads/publications/2014_08_22_Regulated_Entitlement_Values_-_Information_Note_-_Aug_2014_v6.pdf

published in November 2013, following further engagement the CC's final determination was published on the 15 April 2014⁸.

The CC was required to determine whether NIE T&D's current price control conditions operate or may be expected to operate against the public interest and if so, set a new revenue control for NIE T&D and otherwise modify NIE T&D's licence conditions.

The CC specified widespread modifications to the conditions and set a new amount for NIE T&D's maximum regulated revenue over the original price control period (from April 2012 to September 2017). The CC has also included further conditions to improve the reporting and monitoring of information to the Utility Regulator.

The CC's determination of NIE's maximum regulated revenue allowed it 6.42% less revenue than was allowed in the UR's Final Determination. The CC also stated that the NIE T&D's weighted average cost of capital should be 4.1%. The new price control conditions will apply from October 2014 until September 2017.

Subsequent to making this determination the role of the CC in relation to these matters has transferred to a new body the Competition and Markets Authority (CMA).

NIE T&D is prohibited under licence obligations to provide or receive any cross-subsidy from any other business of the Licensee, this also includes any affiliate or related undertaking of the Licensee (whether or not a Separate Business).

The Utility Regulator has a statutory duty to promote competition, where appropriate, in the generation, transmission, distribution and supply of electricity. Our Forward Work Program 2014-15 had identified the introduction of contestability in the electricity connections market as an area where competition can be established. This will allow choice in who carries out the work associated with connecting to the electricity network in Northern Ireland.

We issued a call for evidence in Sept 2014 and a contestability workshop was held in October 2014 with stakeholders which led to the development of a

⁸ <https://www.gov.uk/cma-cases/northern-ireland-electricity-price-determination>

Contestability working group⁹, work in this area will be continuing through 2015.

3.1.4 Cross-border issues

- Access to cross-border infrastructure, including the procedures for the allocation of capacity and congestion management (Article 37(6)(c), Article 37(8), Article 37(9), use of revenues for interconnectors (article 37(3)(f))

Report in particular on cases where specific cross-border cooperation between NRAs happened besides the general activity of the NRA in the frame of ACER/FG

- Monitoring technical co-operation between Community and third-country TSOs (Article 37(1)(s))
- Monitor TSO investment plans in view of TYNDP art 37(1)(g)
- Cooperation (Article 37(1)(c))

Other relevant cooperation agreements/activities of the NRA besides the RI

The Moyle Interconnector between Scotland and Northern Ireland lies within a Member State and has not previously been regarded as an interconnector for the purposes of the Electricity Directive. Nonetheless, Moyle has aimed to comply with the requirements of the directive regarding congestion management.

The interconnector owners are required to prepare relevant access arrangements in respect of the Interconnector. The purpose of these rules is to set out the auction mechanism including how participants can make an offer to acquire capacity units, together with the requirements on the Interconnector owner in terms of accepting an offer for capacity units from a participant. The access rules also address other areas including the curtailment approach should capacity become unavailable due to an outage.

Moyle Interconnector access rules are approved annually by both Utility Regulator and Ofgem with input from the Regulator in Ireland regarding the East West Interconnector.

⁹ http://www.uregni.gov.uk/electricity/contestability_working_group/

The export and import capacity of Moyle has been limited due to a number of technical faults. A fault on one line of Moyle occurred between 24 August 2011 and 19 February 2012. This fault reduced export and import capacity to 250MW. A second fault has since occurred on the second line beginning on 23 June 2012. This fault has not been resolved, resulting in a reduced export and import capacity of 250MW. Work is ongoing to increase the capacity on the line.

3.1.5 Compliance

- Compliance of regulatory authorities with binding decisions of the Agency and the Commission (Article 37(1)(d)) and with the Guidelines (Article 39)

Which decisions/actions have been taken following binding decisions of the Agency or the Commission.

- Compliance of transmission and distribution companies, system owners and electricity undertakings with relevant Community legislation, including cross-border issues (Article 37(1)(b), Article 37(1)(q), Article 37(3)(a),(b),(e) and Article 37(5) all but (a) and (c) + imposing penalties (Article 37(4)(d))

Report in particular on monitoring systems for TSO certification compliance and in the next future NC compliance. Report on other compliance cases and existing active monitoring methods

Compliance of transmission and distribution companies, system owners is through their licences. There are no issues to report.

3.2 Promoting Competition

3.2.1 Wholesale markets

Please provide a brief illustration of the state of competition of wholesale market and the main changes in the recent year

The all-island Single Electricity Market is the combination of two separate jurisdictional electricity markets in the Ireland and Northern Ireland and is governed by the SEMC. The SEMC comprises of representatives from: the Commission for Energy Regulation for Ireland, the Utility Regulator for Northern Ireland and an independent member.

The Single Electricity Market (SEM) has been in place since 2007 and ensures that the price of electricity charged to consumers reflects the costs of producing the electricity.

The SEM Committee meets monthly to take decisions on SEM matters. It comprises members of our board, the CER Commissioners and two independent members.

2014 was the seventh full year of operation of the Single Electricity Market. The SEM is a gross mandatory pool with gate closure at 10.00 hrs day ahead. The ex-post market schedule sets the half hourly system marginal price and allocates infra marginal rent to those included in the schedule. Capacity payments are made to all available generators based on an annually calculated capacity pot. Regulated directed contracts and also non directed contracts provide hedging for market participants. The market is operated by SEMO – the Single Electricity Market Operator which is a joint venture between the system operators in NI and Ireland.

Along with CER we have taken major steps to deliver the new electricity market, the I-SEM. This includes ensuring that the market design is compliant with the European target model, as well as delivering key benefits for consumers.

This has resulted in the advancement of a significant project to integrate the current SEM so as to facilitate a pan European electricity market. The new I-SEM project is timely, allowing the two regulators to take account of other changes in the electricity market since its opening, changes which include a substantive increase in renewables on the system and interconnection with GB with the east

west interconnector. The redesign is focused on ensuring the most efficient deployment of all the power on the system and achieving an acceptable level of security of supply.

It is expected that the benefits of the I-SEM will be market transparency and efficiency of interconnection with the wider European market. The I-SEM will also facilitate increased competition in the electricity market in NI.

During 2014 we achieved two significant milestones:

1. following extensive consultation, the SEM Committee agreed the preferred option for the high level design for the I-SEM in September 2014; and

2. published a project plan in October 2014 setting out the detail of how the I-SEM will go live by October 2017.

Due to the significant work being carried out in relation to changes being proposed to the wholesale trading arrangements in the near future, to comply with the European target model, the SEM has not undergone any significant changes in 2014.

We also took steps to promote sustainability. In order to address the impacts that increasingly high levels of wind place on the electricity system, we have been progressing the delivery of a secure, sustainable electricity system (DS3) programme with CER. The objective of DS3 is to facilitate increased levels of renewables and effectively decrease the levels of curtailment.

Curtailment and increased levels of renewable penetration will also be a major factor in the implementation of the I-SEM. The current operational limit on fluctuating generation (such as wind) at any given time is 50%. The DS3 programme's objective is to increase 50% penetration level to 75%.

In December 2014 the SEM Committee approved a high level design for the procurement of system services. These additional system services will allow the electricity system to respond more flexibly to fluctuations in wind on the system. These services will be procured through a competitive process where sufficient competition exists or through regulated tariffs where this is not the case. Along with CER, we have limited the level of spend on such systems to reflect the level of benefit that will be received by consumers from such services.

3.2.1.1 Monitoring the level of prices, the level of transparency, the level and effectiveness of market opening and competition

- Article 37(1)(i),(j) (k), (l) (u) and Article 40 (3)

Report separately the three issues: prices, transparency and effectiveness of competition. In particular regarding prices report on fundamentals, price developments and liquidity. Regarding transparency report on the access to prices and on how robust prices are and if at national level transparency obligations regarding pricing exist.

Price

We continue to examine where competition can be enhanced and costs reduced for consumers. While demand levels in 2014 are nearly identical to those in 2013, prices have been consistently lower in each period during 2014.

The SEM market monitoring unit (MMU) is based at our offices and has continued to monitor the SEM over the past year. Our MMU has carried out a number of internal investigations into bidding in the SEM. A quarterly market update has also been developed that provides an overview of the SEM and sets out recent trends in the market on pricing, demand, scheduling and contract prices. This report also provides additional transparency on the SEM market.

The MMU forms part of a Market Power Mitigation strategy developed by the Regulatory Authorities (RAs) during 2006. The MMU reviews the behaviour in the market on an ex-post basis. This includes investigating the exercise of market power and monitoring the compliance of market participants with their licence obligations in relation to participation in the market.

The MMU publishes a public report on the Single Electricity Market (SEM) for each quarter¹⁰, the latest publication covers Q4 2014¹¹. These reports provide a particular focus on recent trends in the market in relation to pricing, demand, scheduling and forward contract prices.

¹⁰ http://www.allislandproject.org/en/mmu_decision_documents.aspx?article=28a9ebd4-217d-46f7-8ac1-fabf27afc473

¹¹ <http://www.allislandproject.org/GetAttachment.aspx?id=71ba4d23-7eba-4877-80dc-9082cbb83aae>

MMU quarterly reports (Q4 2014) - key facts:

- the system marginal price (SMP) in the SEM reduced from €66/MWh in 2013 to €57/MWh in 2014;
- gas continued to be the dominant fuel in the SEM, contributing 44% of the fuel mix in 2014; and
- levels of demand were broadly similar to those seen in 2013.

The MMU continuously reviews generator participants' behaviour in the market, including investigations into the exercise of market power. It also monitors the compliance of market participants with the bidding code of practice and other market rules. The MMU is also the point of contact for participants who wish to register complaints relating to market behaviour.

Transparency

The Market Operator for the SEM (SEMO) publishes all commercial and technical data relating to bids for any trading day.¹² This information is published four days after the trading day, and also includes all relevant price information for each half hour period.

Market opening

Over 2014 we have worked towards an enduring solution to facilitate new entry into the market. We moved forward the licensing arrangements for aggregated generator units (AGUs) and demand side units (DSUs). AGUs are a collection of generators each with a capacity of no greater than 10MW. A DSU is a site which offers the ability to reduce demand at certain times.

Effectiveness of competition

The SEM Committee publishes an annual report providing an overview of the market structure and developments in the market over the previous year. The report for 2014 is due for publication in the second half 2015.

On 19 December 2014, the RAs published information regarding generators' financial performance. The paper follows the financial reporting template to be

¹² <http://www.sem-o.com>

completed by generation companies with a combined capacity greater than or equal to 25 MW. This report covers the financial year from April 2013 to March 2014¹³.

3.2.2 Retail market

Please provide a brief illustration of the state of competition of retail market and the main changes in the recent year

Competition in the retail market was set up in Northern Ireland in a progressive way, starting with the non-domestic sector in 1999, and extending to the domestic market in 2007.

New suppliers entered the electricity market from June 2010 in the electricity market. Since then, more suppliers have been attracted to the Northern Ireland market. By December 2014, there were 8 active suppliers in the electricity sector, 5 of them operating in both, domestic and industrial sectors.

To keep the development of the retail energy sector in Northern Ireland under closer review, we regularly gather and analyse market information. Over 2014 we have consulted on a Retail Energy Market Monitoring (REMM) framework that we are implementing in 2015. This framework will enhance the monitoring of the retail energy sector that we currently perform.

We publish some of the information we collect in the form of monitoring reports that aim at increasing transparency over the retail energy markets. The Quarterly and Annual Transparency Reports (QTRs and ATRs)¹⁴ provide a range of information about the retail energy market in Northern Ireland.

Over 2014, the market share of the previously incumbent supplier in the domestic non-prepayment sector has decreased slightly, from 78.1% customer numbers in Dec 2013, to 77.8% in December 2014. The decrease of the previously incumbent supplier share in the prepayment sector has been more significant, from 65% at the end of 2013, to 61% at the end of 2014.

Competition is more mature in the non-domestic market. By the end of 2014, the share of the new suppliers in the non-domestic sector was c82% of the volume

¹³ Report on Generator Financial Performance in the SEM - <http://www.allislandproject.org/GetAttachment.aspx?id=7c74b846-b1fd-4ba4-aa4f-67f6eccd82c>

¹⁴ <http://www.uregni.gov.uk/retail/reports/>

supplied to this sector.

Also, the level of switching activity has reduced in the domestic sector from 2013. The number of domestic switches in 2014 was c44,800 compared to 72,000 domestic switches in 2013. However, the level of switching activity has increased in the non-domestic sector, with more than 6,300 non-domestic switches in 2014, versus c3,300 in 2013.

Competition in the retail market was set up in Northern Ireland in a progressive way, starting with the non-domestic sector in 1999, and extending to the domestic market in 2007.

3.2.2.1 Monitoring the level of prices, the level of transparency, the level and effectiveness of market opening and competition

- Article 37(1)(i),(j),(k),(l),(u) and Article 40 (3)

Report separately the three issues: prices, transparency and effectiveness of competition. In particular regarding prices report on fundamentals, price developments and liquidity. Regarding transparency report on the access to prices and on how robust prices are and if at national level transparency obligations regarding pricing exist. Please report here separately dual fuel prices

In the monitoring of the energy retail market, the key indicators are: market shares, active suppliers in each market segment, market activity per market segment, rates of switching, domestic prices in Northern Ireland and a price comparison with other EU countries. Future work in terms of collecting and assessing further retail information will be included into this series of reports.

Northern Ireland electricity domestic price for medium customers – using the tariff applying from October 2013, for an average customer consuming 3,300 kWh per annum, is close to the median of the EU countries in the band of 2,500-4,999 kWh.

The customer complaints procedure in Northern Ireland is detailed on our website: www.uregni.gov.uk/customer_information. In the first instance customers are asked to resolve any difficulty with their supplier. All domestic suppliers are required by licence to have a Code of Practice on complaint handling. This details a procedure to facilitate the fair and prompt settlement of complaints and disputes as well as a system for reimbursing or compensating complainants. They are also

required under the licence to inform customers of the role and contact details of the Consumer Council Northern Ireland (CCNI)¹⁵ both in contracts and on bills.

If customers are not satisfied with the supplier's handling of, or response to, a complaint, they may ask CCNI to intervene on their behalf. The CCNI has statutory responsibility to assist energy customers with complaints at the second stage (after the supplier process has been exhausted).

The Utility Regulator deals directly with complaints and disputes, with regard to the transmission and distribution operator. Details of our process are given on our website

www.uregni.gov.uk/publications/appeals_complaints_and_disputes_policy_updated_june_2013

With regard to complaints, IME3 has been implemented and all suppliers are fully compliant with the Code of Practice on Complaints Handling. The Utility Regulator continues to work with suppliers on their Codes of Practice to ensure provision of an accessible, equitable and transparent, simple and inexpensive complaints procedure.

- Article 37(1)(k)

Under its Competition Law powers, the Utility Regulator has not been involved in any cases of restriction of competition or restriction of contractual practices.

- Article 37(1)(l)

The EU's IME3 directives set out a series of measures to make sure consumers are adequately protected in the energy markets.

We have implemented some of the requirements to protect consumers in energy markets through supply licence modifications. Potential supplier mis-selling and poor customer information at the point of sale are barriers to promoting consumer confidence in energy markets. We have mandated that all suppliers must comply with a supplier marketing code of practice which has clear, firm and enforceable rules for protecting consumers. This code of practice was developed through a process of extensive stakeholder engagement and consultation. The Code is due to come into effect in 2014.

¹⁵ Consumer Council for Northern Ireland <http://www.consumercouncil.org.uk/>

In addition to developing the marketing code of practice, we have also approved interim codes of practice for: the payment of bills; provision of services for persons who are of pensionable age or disabled or chronically sick; complaints handling procedure; prepayment meter customers; and the efficient use of electricity/gas. This process has ensured that all suppliers are providing high levels of customer protection. We will develop minimum standard guidance for these codes and the suppliers' codes will be updated to reflect these minimum standards.

In the past we have with Power NI and NIE to ensure that Supplier of Last Resort (SoLR) arrangements are in place and fully tested. This will provide reassurance to customers on continuity of supply in the unlikely event of any supplier exiting from the market. Power NI has been appointed to immediately assume responsibility for providing supply in this situation.

We now have a role in legal dispute resolution between customers and suppliers. If a customer's billing dispute cannot be resolved by engagement with the supplier, or intervention by CCNI, we may legally determine on the billing dispute. In 2013-14 we made a determination on the first formal billing dispute which was referred to us.

3.2.2.2 Recommendations on supply prices, investigations and measures to promote effective competition

- Article 37(1)(o)

Report on recommendations at national level on supply prices and competition

Describe system of regulated prices (if they exist)

- Article 37(4)(b)

Report on investigations carried out, main results and possible measures adopted

Report on tariff deficit if it exists

Electricity supply licensees require transparency of customers' terms and conditions, including price. These conditions apply to all licensees and are legally binding. Electricity customers are guaranteed the right to be supplied under fair and transparent terms. They cannot be discriminated in terms of price and the regulatory framework includes legally binding supplier of last resort provisions.

The Utility Regulator has the powers necessary to investigate and enforce effective competition and the functioning of the retail market. We regularly request information to the network and supply companies, and monitor the received data.

3.3 Security of supply (if and insofar as NRA is competent authority)

Implementation of safeguard measures Art. 42

The Fuel Security Code is designed as a Northern Ireland response to a Fuel Security Event. The Fuel Security Code currently in force in Northern Ireland under the Electricity (Northern Ireland) Order 1992 as amended (the 1992 Order) was drafted in 1992.

The objectives of the Fuel Security Code are to assist with the effective management of an event where primary fuel supplies for electricity generation are disrupted: a Fuel Security Event.

The Code enables Government to direct the electricity industry to provide information on power supplies and to take specific action to manage such disruption in a way to ensure as far as is reasonably practical.

3.3.1 Monitoring balance of supply and demand

- Article 4

SONI prepare an annual Generation Capacity Statement which covers both demand predictions and the generation margins. The latest statement published in December 2013 shows:

- Current level of electricity peak demand is 1810 MW¹⁶. This has been forecasted to reach 1824 MW¹⁷ by 2024. This forecasted peak is a decrease on previous estimates¹⁸;
- The large reduction in demand forecasts in NI and Ireland has led to an increase in generation adequacy. However, due to environmental constraints a number of generation plant are expected to be decommissioned by 2016 (loss of 260MW of capacity);
- During the period 2015 to 2020 there is sufficient generation capacity to achieve compliance with the generation security standard. The reduction in capacity at Ballylumford at the end of 2018 is likely to result in the surplus dropping to levels of under 300 MW;

¹⁶ Observed generation, excludes house load.

¹⁷ Total Energy Requirement

¹⁸ Further information available at:

<http://www.eirgrid.com/media/Generation%20Capacity%20Statement%202014.pdf>

- By 2021, more severe restrictions are placed on the Kilroot coal plant, and this could have the result of pushing Northern Ireland into deficit. This is based on the assumption that forecasts of demand, generation capacity and availability are achieved. It also relies on imports from GB and a reliance on generation in RoI. There remains however a risk of operational scenarios that could result in load shedding due to a generation capacity shortfall as generators unit sizes are large and there is a dependency on imports;
- There is currently 2381MW of installed capacity, this figure excludes available capacity via imports on interconnector and tie lines. There is also 738 MW of Partially dispatchable or non dispatchable generation capacity (including 658MW of Wind) installed on the NI system;
- Imports of 250 MW from GB and 100 MW from Ireland are expected to be available to support security of supply.
- In June 2013, along with the Department of Enterprise, Trade and Investment (DETI), the Utility Regulator published an information paper on electricity security of supply in Northern Ireland. The paper set out the factors contributing to the security of supply risk and identified options for addressing the risk. An information paper around electricity security of supply considerations was published in December 2013. This work was progressed further in 2014 and a paper on Security of Supply in Northern Ireland was published by the Utility Regulator and DETI in December 2014.

The most significant transmission project in NI is the second north-south interconnector. Preparatory work is ongoing for this; however the project is encountering significant opposition from residents along the route. Some delays are now expected due to other planning issues that have arisen in the Republic of Ireland. To view SONI's most recent Generation Adequacy Report (2014) see:

<http://www.soni.ltd.uk/media/documents/Operations/CapacityStatements/All%20Island%20Generation%20Capacity%20Statement%202015%20-%202024.pdf>

3.3.2 Monitoring investment in generation capacities in relation to SoS

- Article 37(1)(r)

Operational network security

- Article 7 2005/89/EC

Investment in interconnection capacity for the next 5 yrs or more

- Article 7 2005/89/EC

Expected future demand and envisaged capacity for the next 5 years and 5-15 years

Article 7 2005/89/EC

In addition to the Generation Capacity Statement SONI are required by licence to publish an annual “Transmission System Capacity Statement” this details the statutory operational requirements, the existing network, its configuration and its planned development over the ten year period to 2023¹⁹.

3.3.3 Measures to cover peak demand or shortfalls of suppliers

- Article 4

The Transmission System Capacity Statement analyses the potential for the system to meet peak demand.

¹⁹ <http://www.soni.ltd.uk/AboutUs/News/TenYearTransmissionForecastStatement2013.html>

4 The gas market

4.1 Network regulation

4.1.1 Unbundling

- Articles 10,11 2009/73/EC Article 3 Regulation (EC) 715/2009
- Article 26

Report on TSO certification, DSO provisions regarding branding and resources and new developments regarding certification revisions. Report also on storage and LNG

NI has two Distribution System Operators (DSOs) Phoenix Natural Gas Limited is solely a Network Operator, with no supply business and firmus energy (Distribution) Limited continues to have an integrated supply business (firmus energy (Supply) Limited). firmus energy (Distribution) Limited however does not have at present , more than 100,000 connected customers, therefore it remains an integrated Distribution and Supply business.

The arrangements for unbundling at the transmission level are being examined as necessary as part of the certification process required under the third energy package.

Previously we stated that the Utility Regulator had received an application from BGE(UK) to be certified as an Independent Transmission Operator (ITO) on 4th July 2012 and which was submitted under article 10 of Directive 2009/73/EC. That application was withdrawn on 1 April 2014 and on the same day an application for certification under the fully ownership unbundled model was submitted. The Utility Regulator is considering the application in conjunction with Ofgem and the CER who received similar applications in respect of BGE(UK) and BGE.

4.1.2 Technical functioning

- Balancing services (Article 41(6)(b), Article 41(8))
- Security and reliability standards, quality of service and supply (Article 41(1)(h))

Report relevant security and reliability regulation and data

- Monitoring time taken to connect and repair (Article 41(1)(m))

Clarify here at least if there is in your country a definition for “time to connect” for consumers and for producers

- Monitoring access to storage, linepack and other ancillary services (Article 41(1)(n))
- Monitoring correct application of criteria that determine model of access to storage (Article 41(1)(s))
- Monitoring safeguard measures (Article 41(1)(t))

NI currently has no gas storage facilities; however Islandmagee Storage Limited is progressing plans to develop an underground natural gas storage facility in the Larne Lough area of Northern Ireland.

The project has been granted planning permission, a gas storage licence from the Utility Regulator, and a Mineral Licence from DETI. During 2014 the developers continue to seek the further consents that are needed before the project can proceed to full construction and operation.

4.1.3 Network and LNG tariffs for connection and access

- Article 41(1)(a), Article 41(6)(a), Article 41(8), Article 41(10) and Article 41(12)

Report on relevant new tariff regulation provisions

- Prevention of cross-subsidies (Article 41(1)(f))

Specify the methodology used in tariff regulation (i.e. cost plus vs incentive regulation), the method of checking undertaking's cost data and if benchmarking is used please describe methodology used by NRA

- Regulated and negotiated access to storage 41(1)(s)

Report on the decisions adopted by MS

Distribution

In NI for gas distribution the entry-exit tariff model is applied. Information is

collected in relation to volumes, revenues and costs, split across relevant customer categories, which are then used to calculate appropriate tariffs. A combination of incentive-based regulation, along with performance-based outputs is implemented for distribution companies. A price control is applied, alongside a performance-based system, which is adjusted, via the “Uncertainty Mechanism” based on actual performance, with incentives included to encourage efficiency and network growth. The next price control, referred to as GD17, will be for a 6 year duration, for the period, 1 January 2017 – 31 December 2022.

The distribution system operator proposes the tariff structure; the Utility Regulator reviews and approves the structure, and then monitors execution. In terms of the regulatory period, the distribution system operators have licences extending 20 to 40 years. In terms of investment incentives, a higher RoR for the Distribution system operators (DSOs) is fixed until the end of 2016 to encourage investment. DSOs provide information on tariffs and connection charges to market participants and other interested parties; this information is available on the website of the individual DSOs.

Regulations for guaranteed standards of service measures which have to be upheld by the distribution licence holders have been consulted on and are in effect from April 2014. In terms of access to the grid in Northern Ireland there have been no cases of refusal of access to the grid to date.

Transmission

At the transmission level, the tariff methodology is set by the Utility Regulator and tariff setting is overseen on an annual basis. The transmission tariffs are calculated by collecting forecast volumes, capacity bookings and revenue requirements from the power and distribution sectors at the beginning of the gas year. The individual submissions are then totalled and capacity and commodity tariffs are calculated for all sectors. A reconciliation process is applied at the end of the year when actual volumes, capacity and revenues are known.

During 2014 we consulted on the introduction of gas entry charges in light of the new network code on CAM. We also reviewed the draft EU Network code on harmonised tariff structures for gas to ensure that any changes we made to the charging regime took account of the draft code where sensible to do so. The introduction of gas entry charges in light of CAM will be completed for October 2015.

The TSOs are also price controlled in NI. The regulatory approach to the price control depends upon the financing model under which the TSO operates.

To improve the rate at which certain pipelines are financed, the Utility Regulator has employed a mutualised financing model where the normal regulatory control over any allowed operational expenditure accrued by the TSO has been removed. The resulting transfer of risk onto consumers, through potential inefficient operating costs, can be limited through corporate governance licence conditions contained within the conveyance licence held by the TSO. One of which is a condition that, in the form of a shadow price control, allows the Utility Regulator to review the level of operating expenditure forecast to be incurred by the TSO.

Where a more standard regulatory model is used, a 'pain-gain' mechanism is applied at the transmission level where TSOs can share in any CAPEX efficiencies gained.

LNG

We have no LNG in NI.

4.1.4 Cross-border issues

- Access to cross-border infrastructure including allocation and congestion management (Article 41(6)(c), Article 41(8), Article 41(9), Article 41(10) and Article 41(12))

Report in particular on cases where specific cross-border cooperation between NRAs happened besides the general activity of the NRA in the frame of ACER/FG. Provide case study/data on standard contracts t.b.d by ACER (i.e. average cost/conditions of importing/exporting 1 MW). Only provide text explanations in the National Report as data are included in the data base.

- Cooperation (Article 41(1)(c))

Other relevant cooperation agreements/activities of the NRA besides the RI

- Monitoring investment plans and assessment of consistency with Community-wide network development plan Article 41(1)(g)

The Utility Regulator and Commission for Energy Regulation (CER) and Ofgem have been involved in joint regulatory work in the context of EU network codes, Capacity Allocation Mechanism (CAM), tariffs, and balancing in compliance with Gas Regulation (EC) No 715/2009. All three NRAs continue to monitor the development of the EU network codes and to assess the potential impact to their networks.

4.1.5 Compliance

- Compliance of regulatory authorities with binding decisions of the Agency and the Commission (Article 41(1)(d)) and with the Guidelines (Article 43)

Which decisions/actions have been taken following binding decisions of the Agency or the Commission

- Compliance of transmission and distribution companies, system owners and natural gas undertakings with relevant Community legislation, including cross-border issues (Article 41(1)(b), Article 41(1)(r), Article 41 (3) and Article 41(5)) + imposing penalties (Article 41(4)(d))

Report in particular on monitoring systems for TSO certification compliance and in the next future NC compliance. Report on other compliance cases and existing active monitoring methods

Compliance of transmission and distribution companies, system owners is through their licences. There are no issues to report.

4.2 Promoting Competition

4.2.1 Wholesale markets

Please provide a brief illustration of the state of competition of wholesale market and the main changes in the recent year

All gas for NI is purchased at the UK NBP.

4.2.1.1 Monitoring the level of prices, the level of transparency, the level and effectiveness of market opening and competition

- Article 41(1)(i) , (j), (k) (l) (u) and Article 44(3)

Report separately the three issues: prices, transparency and effectiveness of competition. In particular regarding prices report on fundamentals, price developments and liquidity. Regarding transparency report on the access to prices and on how robust prices are and if at national level transparency obligations regarding pricing exist.

As above all gas for NI is purchased at the UK NBP.

4.2.2 Retail market

Please provide a brief illustration of the state of competition of retail market and the main changes in the recent year

The gas market in the Greater Belfast area has been open to competition to domestic customers since 2007. However, there were no competing suppliers in the domestic market until 2010. In this distribution licensed area there has been six active gas suppliers in the non-domestic sector during 2014: SSE Airtricity Gas Supply (AGS), firmus energy, Electric Ireland, VAYU, LCC Power and Flogas Natural Gas. In the Greater Belfast licensed area there has been two active gas suppliers in the domestic sector in 2014. AGS is subject to a price control over the domestic and small I&C (industrial and commercial) customers who consume less than 25,000 therms per annum in the Greater Belfast area. A maximum average tariff is employed in these sectors for customers of AGS. Other suppliers are free to compete against this maximum average tariff. In the Greater Belfast area, during 2014 the total market share of the incumbent supplier (AGS), remained at 72% throughout the year.

The ten towns gas area opened to competition for large I&C (industrial and commercial) customers in October 2012. AGS entered this market to compete against the incumbent firmus energy from 1 January 2013. In the ten towns large I&C market the market share of the incumbent supplier (firmus energy), based on number of large I&C connections, fell from 92% to 86% during 2014. The domestic and small I&C customers (using less than 25,000 therms per annum) were supplied exclusively by the incumbent supplier (firmus energy) during 2014. The domestic and small I&C market will be open to full competition from 1 April 2015. There is an incentive in the distribution price control on firmus energy to price competitively to acquire domestic and small I&C customers.

4.2.2.1 Monitoring the level of prices, the level of transparency, the level and effectiveness of market opening and competition

- Article 41(1)(i),(j) (k), (l) (u) and Article 44 (3)

Report separately the three issues: prices, transparency and effectiveness of competition. In particular regarding prices report on fundamentals, price developments and liquidity. Regarding transparency report on the access to prices and on how robust prices are and if at national level transparency obligations regarding pricing exist. Make reference to dual fuel if necessary.

SSE Airtricity Gas Supply (Northern Ireland) Limited (AGS) has a regulated tariff for domestic and small industrial and commercial customers (using less than 25,000 therms per annum). The Utility Regulator enters into a formal tariff review process with AGS twice per year with a view to tariff changes being effective from 1st April and 1st October each year. The Utility Regulator also monitors gas prices on an ongoing basis and an ad-hoc tariff review for AGS may be initiated at any stage if the Utility Regulator considers that gas prices have increased or decreased enough to warrant a tariff review.

The Utility Regulator monitors the AGS regulated tariff against the tariffs of other supply companies in NI, the UK and ROI. The Utility Regulator published transparency reports every quarter which provides comparisons of the gas tariffs in NI, GB and ROI: http://www.uregni.gov.uk/publications/qtrs_2014

During 2014 the AGS regulated tariff for domestic customers (based on the standard domestic tariff) was consistently lower than the domestic tariffs in ROI

and the average of the big six suppliers in GB. Supply companies have a licence obligation to inform customers at least 21 days in advance of any change (increase or decrease) in the tariff. Suppliers are also required to provide advanced notification of when customer is coming to the end of a fixed term or discounted tariff period (no less than 28 days but no more than 42 days before).

The Utility Regulator also reviews the AGS gas purchasing strategy each year and also receives weekly and monthly gas purchasing reports from AGS showing the volumes and cost of gas purchased for the short and long term future.

The Utility Regulator monitors the effectiveness of competition in the retail gas markets in NI. There are two retail markets in NI: the Greater Belfast market and the Ten Towns market. Competition in these markets is monitored by the Utility Regulator on a quarterly basis and an analysis of the competition is published in the Utility Regulator's transparency reports:

http://www.uregni.gov.uk/publications/qtrs_2014

In the Greater Belfast market there are currently two active gas suppliers for domestic customers. The domestic market share of the incumbent gas supplier (AGS) remained relatively stable at 72% during 2014 (based on number of domestic connections). Other gas suppliers have expressed interest in entering this domestic market in the short to medium term future. During 2014 the number of active suppliers for non-domestic customers in Greater Belfast grew from four to six suppliers. The total I&C market share of the incumbent gas supplier (AGS) remained stable at around 66% during 2014 (based on number of I&C connections).

In the Ten Towns market, the large I&C market (customers using more than 732,500kWh per annum) is open to competition. In this market there are two active gas suppliers: the incumbent supplier (firmus energy) and AGS. During 2014 the market share of the incumbent supplier fell from 92% to 86% (based on number of large I&C connections). The remaining market of small-medium I&C customers and domestic customers will be open to competition from April 2015.

4.2.3 Recommendations on supply prices, investigations and measures to promote effective competition

- Article 41(1)(p)

Report on recommendations at national level on supply prices and competition

- Article 41(4)(b)

Report on main investigations, results and possible measures adopted

Report on tariff deficit if it exists

In the Greater Belfast gas market SSE Airtricity Gas Supply (Northern Ireland) Limited (AGS) is price regulated for customers using less than 25,000 therms per annum. A price control is determined and published for Airtricity which sets out a procedure which Airtricity must comply with in setting tariffs. The price control also sets out a level of operating expenditure for the company for each year of the control which is then used when compiling the supply opex costs for the tariff. At each tariff change the Utility Regulator publishes a paper which provides detail on the various elements of the tariff, details of any over/under recovery which has been built up or lost in previous tariff periods and therefore incorporated into the new tariff and comparisons with tariffs in GB and ROI.

4.3 Security of supply (Article 5) (if and insofar as NRA is competent authority)

The Department of Energy and Climate Change (DECC) is the designated Competent Authority with respect to the security of supply for the UK Member State (as notified to the Commission under Regulation 994). As such a number of the requirements of Article 5 of Directive 2009/73/EC are carried out by DECC. However the Utility Regulator does contribute to some of the elements identified below.

4.3.1 Monitoring balance of supply and demand

100% of Northern Ireland gas supplies are currently provided from Great Britain via the National Transmission System Exit Point at Moffat. As such the wider monitoring of UK demand and supply is largely carried out by DECC and National Grid. However the Transmission System Operators in Northern Ireland and the Republic of Ireland regularly engage with National Grid on demand and supply issues downstream of Moffat.

There are also a number of government and TSO groups that have been established between the UK and Ireland to facilitate communication on emergencies and security of supply. These groups also co-ordinate the work required under Regulation 994.

4.3.2 Expected future demand and available supplies as well as envisaged additional capacity

Forecast Total Volumes (bcm)									
2014/2015	2015/2016	2016/2017	2017/2018	2018/2019	2019/2020	2020/2021	2021/2022	2022/2023	2023/2024
1.158	1.125	1.229	1.251	1.186	1.237	1.172	1.239	1.248	1.256

All of NI gas supplies are currently provided from Great Britain via the NTS Exit

Point at Moffat. As noted previously there is significant industry interest in developing gas storage facilities in the Larne area of NI which could strengthen security of supply within the region.

The Utility Regulator and the NI TSOs annually produce a gas capacity statement which examines the ability of the gas network to meet future supply and demand scenarios over a ten year period. This assessment included the proposed Islandmagee storage project and network extension to the West and North West as discussed above.

This approach ensures that any areas requiring investment are identified and addressed so that future demands on the system can be met. The capacity statement is published on the Utility Regulator website.

4.3.3 Measures to cover peak demand or shortfalls of suppliers

- Art 41(1)(t): implementation of safeguard measures

The transmission companies in Northern Ireland have emergency arrangements in place to deal with either a physical disruption to the network or a restriction in gas supplies. The arrangements are a legal requirement and are contained within each TSO's Safety Case. The safety case outlines the emergency stages and the actions that are to be undertaken at each stage.

Additionally power stations are required to hold reserves of alternative fuels to enable fuel switching in the event of a restriction to gas supplies. The emergency measures are tested annually alongside the Republic of Ireland and Great Britain exercises.

Gas Supply licenses in NI also require that suppliers have access to gas supplies to meet peak demand during severe winter conditions.

5 Consumer protection and dispute settlement in electricity and gas

5.1 Consumer protection

- Compliance with Annex 1 (Article 37(1)(n)) and (Article 41(1)(o))
- Ensuring access to consumption data (Article 37(1)(p)) and (Article 41(1)(q))

Article 11A of the Electricity Order and Article 10A of the Gas Order provides the Authority with powers to impose conditions on licensees to give effect to this obligation. Part VI of the Energy Order provides the Authority with such enforcement powers as are necessary to compel compliance. The conditions which ensure that these consumer protection measures are adhered to are set out in part II of the electricity supply licences, Customer Related Conditions and Part 2 of the Gas Supply licences, Conditions Applicable to the Supply of Gas by the License Holder. The implementation of the third package has seen these conditions further enhanced.

The Utility Regulator ensures customer access to consumption data via conditions in the gas and electricity supply licences. Licence Condition 38 and 44 in electricity supply licences and 2.19 and 2.28 in gas supply licences ensures that customers have access to, and are informed of their consumption and that information is provided in such detail and format as is approved by the Utility Regulator and the consumer representative body. Licence conditions were updated as a result of the third package to ensure that consumers are entitled to further detailed information on their electricity and gas consumption.

The Utility Regulator has consulted on and implemented licence modifications under the EU Third Internal Energy Package. The licence modifications implemented under the EU Third Internal Energy Package also required Gas and Electricity suppliers to develop and publish Codes of Practice to enhance the consumer protection measures. The licence conditions ensure that customers are provided with access to their consumption data and transparent information in relation to tariffs, terms and conditions and complaints handling procedures. It also requires suppliers to offer customers a range of payment methods, to facilitate supplier transfers within 15 working days, and to provide a code of

practice on provision of services for vulnerable customers. Licence conditions also set out timeframes for suppliers providing terms and conditions to new customers and for suppliers to give notice to customers at least 21 days prior to any changes to the terms (including price) being made. Suppliers must also inform customers of their right to withdraw prior to when the terms of their contract are changing. Suppliers also have a licence condition requiring final bills to be issued to customers within six weeks from the date the change of supplier takes place.

5.2 Dispute settlement

- Article 37(11), 37(5)(c), Article 37(4)(e)
- Article 41(11) and Article 41(4)(e)

Report on cases, in particular on major issues concerning network users (access tariffs, connection disputes/refusals...), including producers and consumers

As a direct result of Directive 2009/72/EC the Utility Regulator was given the legal authority to act as a dispute resolution authority for certain matters in relation to electricity.

Prior to the implementation of the Directive into national law, the Utility Regulator had been, as it still is, able to determine certain complaints or disputes, such as disputes arising between an electricity distributor and any person requiring a connection to that distributor's distribution system.

On the implementation of the Directives, the Utility Regulator's dispute resolution remit was extended further, as now individuals and companies are able to refer certain disputes or complaints regarding the transmission and distribution of electricity in Northern Ireland to the Utility Regulator for resolution.

In June 2011 the Utility Regulator published its "Policy on the Resolution of Complaints, Disputes and Appeals". This sets out procedures which the Utility Regulator will generally follow when dealing with a complaint or dispute which it has been requested to determine. This policy was amended in June 2013²⁰.

Under the Gas (NI) Order 1996 billing disputes must in the first instance be referred to the Consumer Council for Northern Ireland. The Consumer Council has 3 months in which to resolve the matter to the customers' satisfaction or the matter is referred to the Utility Regulator. We have had no referrals during this period.

The Gas Market Opening Group (GMOG) was established by the Utility Regulator to address any operational barriers to entry into the Greater Belfast gas market. The group has now been extended to cover the Greater Belfast gas market and the Ten Towns gas market. The group includes active representation from supply and distribution license holders, the DETI in NI, the Consumer Council in NI and

²⁰ http://www.uregni.gov.uk/publications/appeals_complaints_and_disputes_policy_updated_june_2013

the Utility Regulator. The GMOG identifies barriers to entry into the gas market in NI; these issues are then discussed with the group with a view to making a decision on the best way to address each issue.

The Utility Regulator also initiated the set-up of a Gas Supplier Forum group. This group identifies any requirements for supplier to supplier agreements in relation to customer switching and overcoming supplier barriers to competition. Agreements are then drawn up to be included in the Supply Meter Point Agreement. This group includes active representation from gas supply licence holders, the Consumer Council NI and the Utility Regulator; however the Distribution licence holders also attend to ensure all decisions made for supplier agreements will work in accordance with the distribution market rules.

In 2014 the Utility Regulator has dealt with a total of seven disputes, one relating to billing and six relating to network access.