



National Audit Office

**BRIEFING FOR THE  
HOUSE OF COMMONS  
ENERGY AND CLIMATE  
CHANGE SELECT  
COMMITTEE  
NOVEMBER 2011**

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# Performance of Ofgem 2010-11

Our vision is to help the nation spend wisely.

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The National Audit Office scrutinises public spending on behalf of Parliament. The Comptroller and Auditor General, Amyas Morse, is an Officer of the House of Commons. He is the head of the NAO, which employs some 880 staff. He and the NAO are totally independent of government. He certifies the accounts of all government departments and a wide range of other public sector bodies; and he has statutory authority to report to Parliament on the economy, efficiency and effectiveness with which departments and other bodies have used their resources. Our work led to savings and other efficiency gains worth more than £1 billion in 2010-11.

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# Introduction

## Aim and scope of this briefing

This is the second briefing that the National Audit Office has prepared for the Energy and Climate Change Select Committee on the performance of Ofgem.<sup>1</sup> The primary purpose of the briefing is to provide the Committee with a summary of Ofgem's performance during 2010-2011. It draws on Ofgem's Annual Report and Accounts 2010-2011, recent work undertaken by the National Audit Office and other published sources. The content of the briefing has been shared with Ofgem to ensure that the evidence presented is factually accurate, but the content of the briefing is the sole responsibility of the National Audit Office.

<sup>1</sup> The first briefing examined Ofgem's performance during 2009-10 and is available at [www.parliament.uk/documents/commons-committees/energy-and-climate-change/NAO%20Briefing%20for%20ECCC%20on%20Performance%20of%20Ofgem\\_P1%20\(2\).pdf](http://www.parliament.uk/documents/commons-committees/energy-and-climate-change/NAO%20Briefing%20for%20ECCC%20on%20Performance%20of%20Ofgem_P1%20(2).pdf)

# Part One

## About Ofgem

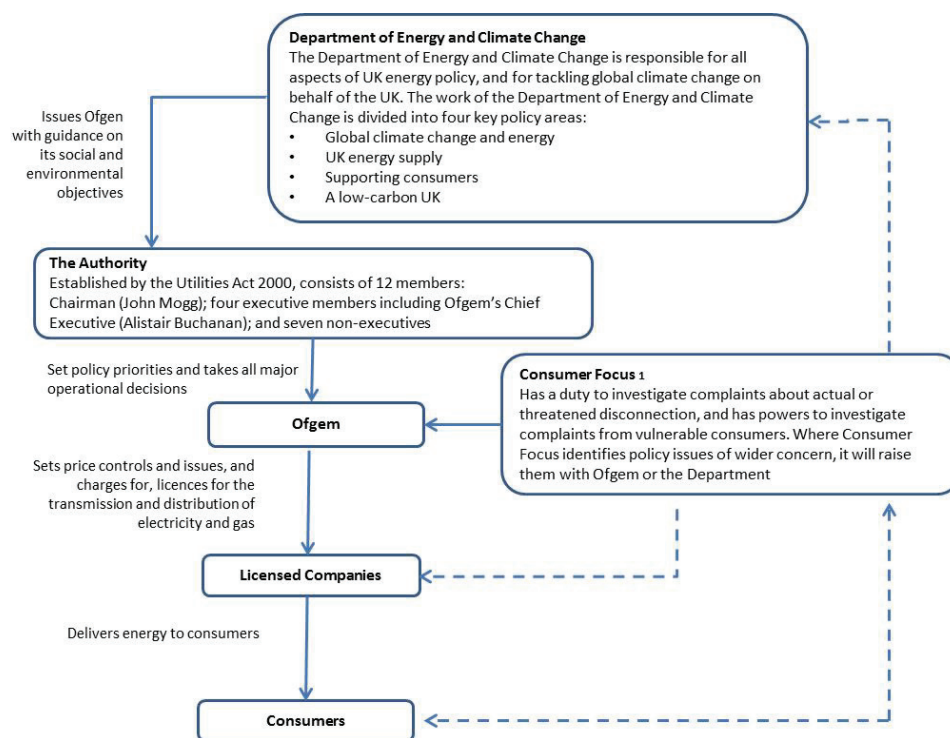
### Ofgem's responsibilities

**1.1** The Office of Gas and Electricity Markets (Ofgem), which was established in 2000 as a non-ministerial department, operates under the direction and governance of the Gas and Electricity Markets Authority (the Authority). The Authority, which is independent of ministerial control, is responsible for the economic regulation of the electricity and gas industries in Great Britain. It sets Ofgem's strategy and policy priorities, and takes decisions on price controls; generation, retail and wholesale market interventions; enforcement; and a wide range of other regulatory matters. In doing so it must have regard to guidance on social and environmental objectives issued by the Secretary of State.<sup>2</sup>

**1.2** Ofgem is responsible for carrying out the Authority's duties on its behalf (**Figure 1**). Its powers are provided for under various Acts of Parliament including the Gas Act 1986, the Electricity Act 1989, the Competition Act 1998, the Utilities Act 2000, the Enterprise Act 2002 and the Energy Acts of 2004, 2008 and 2010. Its main statutory duty is to protect the interests of present and future consumers of gas and electricity through a regulatory regime, supported by wider powers in legislation, that allow it to:

- issue, enforce, modify or revoke licences to operate in the electricity or gas markets;
- set price controls for monopoly owners of gas distribution networks and electricity transmission and distribution networks; and
- carry out investigations under the Competition Act 1998 into companies suspected of engaging in anti-competitive behaviour, and take action following breaches of legislation in respect of the gas and electricity sectors in Great Britain.

<sup>2</sup> Department of Energy and Climate Change, *Social and Environmental Guidance to the Gas and Electricity Markets Authority*, January 2010  
[http://www.decc.gov.uk/assets/decc/what%20we%20do/uk%20energy%20supply/energy%20markets/regulation/1\\_20100121172046\\_e\\_@@\\_guidancegaselecmarkets.pdf](http://www.decc.gov.uk/assets/decc/what%20we%20do/uk%20energy%20supply/energy%20markets/regulation/1_20100121172046_e_@@_guidancegaselecmarkets.pdf)

**Figure 1****Regulatory responsibilities for energy and gas markets****NOTES**

1. On 14 October 2010 the Government announced that Consumer Focus would be abolished and that some of its functions were likely to transfer to Citizens Advice, Citizens Advice Scotland and the General Consumer Council for Northern Ireland. Consumer focus will continue operating until the transfer is completed following the passage of the Public Bodies Bill and any necessary secondary legislation.

Figure Source: National Audit Office

**1.3** In addition to its statutory duties, Ofgem also delivers a number of environmental programmes on behalf of government, such as the Renewables Obligation, which gives renewable energy generators a subsidy for each megawatt hour of renewable electricity they produce.

**1.4** To support the achievement of its primary objective, to protect the interests of current and future gas and electricity consumers, Ofgem sets out strategic priorities in its *Corporate Strategy and Plan*.<sup>3</sup> It introduced four new strategic priorities in 2010-11, to reflect the need for major changes in the energy industry and Ofgem's increased involvement in delivering government programmes, namely to:

- build a low carbon economy;

<sup>3</sup> Ofgem, *Corporate Strategy and Plan 2011-2016*, March 2011

<http://www.ofgem.gov.uk/About%20us/CorpPlan/Documents1/Corporate%20Strategy%20and%20Plan%202011%20-%202016.pdf>

- help to maintain the security of energy supplies;
- promote quality and value for energy consumers; and
- ensure the timely and efficient delivery of government programmes for a sustainable energy sector.

## How Ofgem is organised

**1.5** Ofgem is headed by a Chief Executive who is also the accounting officer. He is supported by a senior management team, which is responsible for the management and resourcing of the business, under the direction of the Gas and Electricity Markets Authority.

**1.6** As at 31 March 2011, Ofgem had two business units (**Figure 2**):

- **Ofgem:** responsible for statutory regulation, it employed 210 staff.
- **Ofgem E-Serve:** responsible for delivering environmental programmes on behalf of government and incorporating group functions such as finance and human resources. As at 31 March 2011 it had 206 staff. It has its own Management Committee, which is responsible for all operational matters relating to E-Serve's management and resourcing.

A further 35 people worked in the Gas and Electricity Markets Authority, including Corporate Affairs staff and the Chairman and seven non-executives.

**1.7** In September 2011, Ofgem introduced a new organisational structure. Group functions were transferred out of Ofgem E-Serve into a separate business unit, and the Smarter Grids and Governance team within its regulatory business was split into two separate teams.

**Figure 2**

Ofgem's organisational structure as at 31 March 2011

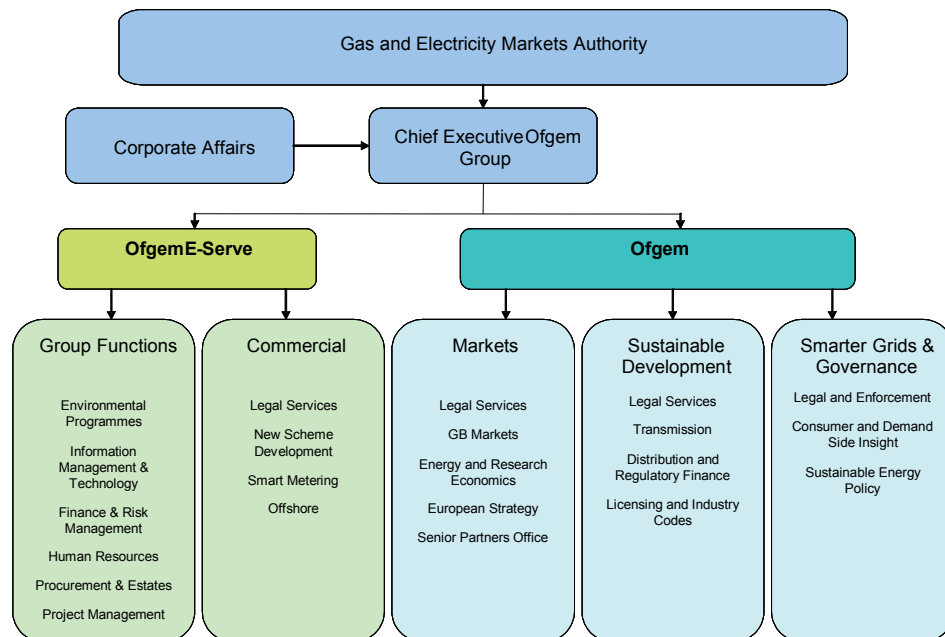


Figure Source: Ofgem

## Where Ofgem spends its money

**1.8** Ofgem's gross expenditure in 2010-11 was £58.8 million. This was £7.7 million (15 per cent) higher the previous year, mainly due to increased spending on delivering government environmental programmes. Ofgem's accounts show that spending by Ofgem E-serve accounted for £40.5 million (69 per cent) of this total. Ofgem's accounts also show how it has allocated its costs across its four strategic priorities, which individually incorporate both regulation work and environmental programmes, (**Figure 3**). Staff costs were £32.5 million, a 24 per cent increase on the previous year, and spending on contractors was £11.8 million, which was 30 per cent higher than the previous year.



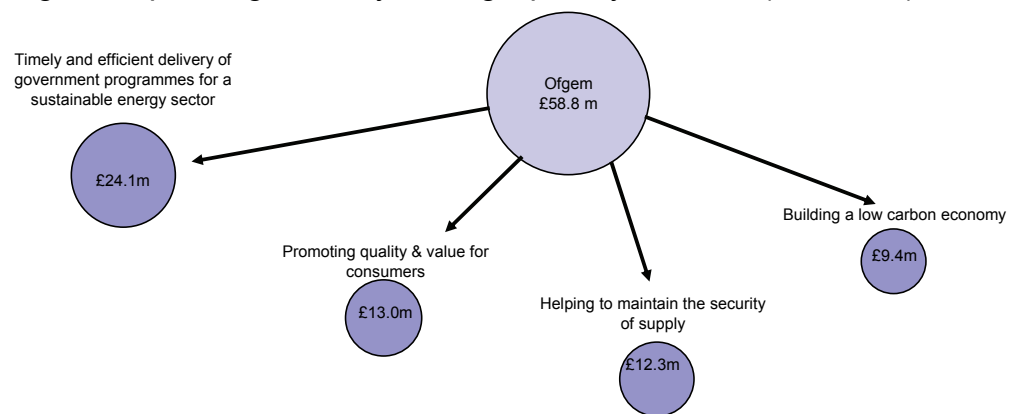
**Figure 3****Ofgem's operating costs by strategic priority 2010-11 (£ millions)**

Figure Source: Office of Gas and Electricity Markets (Ofgem) Annual Report and Accounts 2010-11

**1.9** Ofgem estimates that the total value of the environmental programmes it administers was around £5 billion in 2010-11, compared to £150 million in 2001-02.<sup>4</sup> Some of these programmes are funded through levies and other obligations placed on industry, which feed through to higher energy bills for consumers.

## Recent developments

**1.10** Important recent developments include the publication of Ofgem's review of retail energy markets and the government's plans for electricity market reform, the completion of a review undertaken by the Department of Energy and Climate Change of Ofgem's regulatory functions and the introduction of a new price control framework for operators of gas and electricity networks.

**1.11** In March 2011, Ofgem published the findings of its *Retail Markets Review*, which examined the operation of electricity and gas for households and small businesses in Great Britain.<sup>5</sup> It concluded that action was needed to address weaknesses in competition and remove confusing tariffs. Remedies proposed by Ofgem include restricting the number of tariffs for some products and, to improve market liquidity, requiring the big six energy companies to auction up to 20 per cent of their power generation output. Ofgem is currently developing its proposals further and intends to publish them with supporting impact assessments later in 2011.

<sup>4</sup> Ofgem, *Delivering Efficient regulation for energy consumers*, Factsheet 99, March 2011.  
<http://www.ofgem.gov.uk/Media/FactSheets/Documents1/costfsupdate.pdf>

<sup>5</sup> Ofgem, *The Retail Market Review - Findings and initial proposals*, March 2011.  
[www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/RMR\\_FINAL.pdf](http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/RMR_FINAL.pdf)

**1.12** The Department of Energy and Climate Change set out its plans for Electricity Market Reform in a White Paper in July 2011.<sup>6</sup> The reforms are designed to attract investment of more than £110 billion and deliver a secure and affordable supply of electricity. Key areas in the White Paper for Ofgem included the action it is taking to improve market liquidity, to allow independent generators to compete in the market, and its review of the electricity market balancing mechanism, to ensure National Grid can match electricity supply to demand.

**1.13** In July 2011, the Department of Energy and Climate Change also published the results of its review of Ofgem's regulatory functions, which was carried out to meet a commitment made in the Coalition Programme for Government.<sup>7</sup> The Department identified a need for greater clarity in the respective roles of Ofgem and government and improved transparency around Ofgem's regulatory decision-making. The Department intends to publish a statutory 'Strategy and Policy Statement to clarify responsibilities and provide context for Ofgem's independent regulatory role. Ofgem has already taken action in response to the Review, for example by setting up a new transparency section on its website, which includes details of payments to suppliers over £25,000 and senior staff expenses.<sup>8</sup>

**1.14** During the year Ofgem developed a new framework for controlling the prices that gas and electricity network operators charge for their services, known as **RIIO**, which stands for Revenue=Incentives+ Innovation+Outputs. The previous system – the 'RPI-X' framework – limited annual price increases over five year price control periods to the Retail Prices Index less a specific percentage. The new framework will extend the price control period from five to eight years. Network operators will also have to meet new performance targets, set in consultation with consumers and network users. Failure to meet them will result in automatic penalties. The new framework is designed to incentivise operators to innovate and better meet the needs of consumers and network users. It will be implemented over the next two price control periods for gas distribution and gas and electricity transmission, starting in 2013, and in 2015 for electricity distribution. Ofgem estimates that RIIO will reduce investment costs by £1 billion over the next decade compared to what costs would have been had it continued with the RPI-X regime.<sup>9</sup>

**1.15** The Treasury established a new control framework, known as the 'levy-cap', which, from 2011-12, will limit the total levy cost to industry and consumers of certain programmes administered by Ofgem on behalf of government. The programmes which are funded by levies on industry and consumer bills and are covered by this cap are the Renewables Obligation, the Renewable Heat Incentive, Feed-in-Tariffs and the

<sup>6</sup> [http://www.decc.gov.uk/en/content/cms/legislation/white\\_papers/emr\\_wp\\_2011/emr\\_wp\\_2011.aspx](http://www.decc.gov.uk/en/content/cms/legislation/white_papers/emr_wp_2011/emr_wp_2011.aspx)

<sup>7</sup> Ofgem Review Final Report, DECC, July 2011 <http://www.decc.gov.uk/assets/decc/11/meeting-energy-demand/energy-markets/2151-ofgem-review-final-report.pdf>

<sup>8</sup> See <http://www.ofgem.gov.uk/About%20us/transparency/Pages/transparency.aspx>

<sup>9</sup> Ofgem, *RIIO - a new way to regulate energy networks*, Factsheet 93 (October 2010) <http://www.ofgem.gov.uk/Media/FactSheets/Documents1/re-wiringbritainfs.pdf>

Warm Home Discount.<sup>10</sup> The cap represents the upper limit on the combined value of these programmes, and for 2011-12 was set at £2.15 billion. Responsibility for ensuring that costs remain within this cap rests with the Department of Energy and Climate Change, rather than Ofgem.<sup>11</sup> Ofgem's responsibility is to administer the schemes and to collect and publish data on costs.

## Capability and leadership

**1.16** The Department of Energy and Climate Change examined Ofgem E-Serve's delivery capabilities in a review of the delivery landscape, which it published in May 2011.<sup>12</sup> The review found that Ofgem E-Serve had provided valuable market knowledge, delivery experience and, through its established relationship with the energy companies, effective enforcement and compliance procedures and knowledge of regulatory design. However, the review also found that working relationships between Ofgem and the Department had not been fully effective, and it identified scope for improving governance, reporting and programme and performance management. The review document contained a joint action plan developed by the Department and Ofgem E-Serve, which included proposals to introduce a comprehensive Memorandum of Understanding covering the entire relationship and Service Level Agreements for each programme.

**1.17** As at October 2011 Ofgem was in the process of conducting a staff Survey, as part of the wider Civil Service People Survey. The Civil Service People Survey aims to provide consistent and robust metrics to help government understand how it can improve levels of engagement across the Civil Service. As part of this survey, civil servants across all participating organisations are asked a range of questions across nine themes which seek to measure their experiences at work. The questions in this survey include an assessment of leadership and their capability to manage change. As part of the annual survey, participating organisations also receive an engagement index, assessing the level of staff engagement determined by: the extent to which staff speak positively of the organisation, are emotionally attached and committed to it, and are motivated to do the best for the organisation. The survey results will allow Ofgem to compare its scores with other regulators and government departments.

<sup>10</sup> Department of Energy and Climate Change, *Business Plan 2011-2015*, May 2011.

<http://www.decc.gov.uk/assets/decc/about%20us/decc-business-plan-2011-2015.pdf>

<sup>11</sup> HM Treasury, *Control framework for DECC levy-funded spending*, March 2011. [http://www.hm-treasury.gov.uk/d/control\\_framework\\_decc250311.pdf](http://www.hm-treasury.gov.uk/d/control_framework_decc250311.pdf)

<sup>12</sup> Department of Energy and Climate Change, *Review of DECC's Delivery Landscape*, May 2011 <http://www.decc.gov.uk/assets/decc/About%20us/1656-delivery-review.pdf>

## Part Two

### Financial management

**2.1** To control costs and drive out waste, public bodies need professional financial management and reporting. In particular, they need to be better at linking costs to services and benchmarking performance to determine whether costs are justified and value for money can be improved. Organisations also need to move their risk management arrangements from a process-led approach to one which supports the efficient and effective delivery of services. Organisations have to publish Statements on Internal Control<sup>13</sup> with their Annual Financial Statements which describe their arrangements for risk management, internal control and governance.

#### **Financial outturn for 2010-11 and comparison with budget**

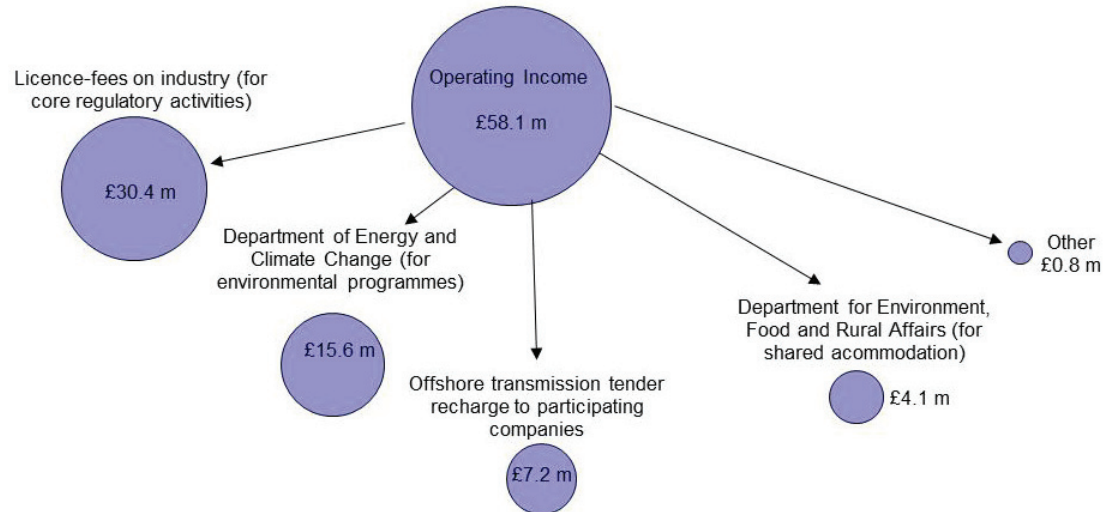
**2.2** Ofgem's gross spending of £58.8 million in 2010-11 was 25 per cent less than the main estimate approved by Parliament of £78.7 million. Spending on core regulatory activities, excluding overheads and group costs, was £18.3 million in 2010-11, which was 25 per cent less than the budget of £24.4 million. Spending by Ofgem E-Serve, including all group overheads and corporate costs, was £40.5 million, which was 25 per cent less than the budget of £54 million. Ofgem's accounts do not show the total cost of core regulatory activities including overheads and group costs. Ofgem's underspending was due to a combination of cost reductions resulting from some programmes not proceeding as planned and efficiency savings (paragraphs 2.6 to 2.7).

**2.3** Ofgem's operating income in 2010-11 was £58.1 million, comprising £30.4 million from licence fees and £27.7 million other income. (**Figure 4**). It received a further £697,000 from public funds to meet the cost of its administration of Climate Change Levy exemptions. In addition, Ofgem collected from licence fee payers and transferred £5.1 million to the Department for Business Innovation and Skills for services provided by Consumer Focus and Consumer Direct, and a further £1.1 million to the National Measurement Office for metrology services.

<sup>13</sup> From 2011-12 Departments will produce a Governance Statement rather than a Statement on Internal Control.

**Figure 4 : Ofgem's operating Income 2010-11**

Ofgem's operating income in 2010-11 (£ millions)



Source: Ofgem Annual Report and Accounts 2010-11

**2.4** As part of HM Treasury's alignment project to remove reporting inconsistencies across government departments, departments collecting revenue due to the Consolidated Fund, are required to separately account for revenues in a "trust statement", with effect from the year ending 31 March 2011. Ofgem collected net receipts totalling £114.4 million that were due to the consolidated fund as follows:

- Fines and penalties £24.8 million;
- Fossil Fuel Levy (net of administration costs) £89 million; and
- Interest on the Fossil Fuel Levy £0.6 million

**2.5** Two cases accounted for more than 90 per cent of receipts from fines and penalties during the year. The largest was a £15 million penalty placed on National Grid Gas in 2009, and upheld by the Supreme Court in August 2010, for abusing its dominant position and acting anti-competitively in the gas meter market. The second largest was an £8 million penalty placed on National Grid Gas in January 2011 for breaches of licence obligations relating to the reporting of mains decommissioning activities, the costs of which were met by levying distribution charges on gas shippers, which are ultimately borne by consumers. As at 31 August, there were 11 ongoing investigations relating to 12 companies.

## **Progress on efficiency and cost reduction**

**2.6** Since 2005, Ofgem has sought to control its own costs by limiting annual increases to its projected annual 'baseline' costs to the Retail Prices Index less a specific percentage, known as RPI-X. Ofgem applies this to the cost of its regulatory activities and to its environmental programmes, adjusting the baseline for its environmental programmes where necessary to reflect changes in its responsibilities. Ofgem estimated that its RPI-3 per cent cost control regime would deliver savings of £12.5 million over the period 2010-15.

**2.7** Ofgem's target for 2010-11 was to limit cost increases to RPI less 3 per cent, against a baseline for the year of £81.5 million, giving a 'budget ceiling' for the year of £81 million<sup>14</sup> against which it set its budget at £78.7 million. As Ofgem set its savings target and budget for 2010-11 before the start of the financial year, it did not reflect the cost-reduction measures that were subsequently introduced by the coalition government, such as the pay freeze for staff that it introduced in accordance with cabinet office guidelines, which accounted for £1.2 million of savings in 2010-11, spread across Ofgem's activities. Ofgem's final spending for the year was £58.8 million, 25 per cent less than budgeted. Ofgem has identified the main areas in which its costs were reduced as follows:

- a £5.3 million reduction in the cost of core regulatory activities funded by licence fees;
- a £6.4 million reduction in the cost of the smart metering programme as a result of the Department of Energy and Climate Change deciding to take responsibility for programme management. Ofgem's charges to the Department of Energy and Climate Change for its smart metering work included overheads, at 23 per cent of Ofgem's costs of managing the programme. Ofgem's smart metering cost reduction included some efficiency savings, including in corporate and overhead costs. In addition, there were some associated savings in information and communications technology costs;

<sup>14</sup> Ofgem, *Corporate Strategy and Plan 2010-15*, March 2010.

<http://www.ofgem.gov.uk/About%20us/CorpPlan/Documents1/Corporate%20Strategy%20and%20Plan%202010-2015.pdf>

- a £2.9 million saving resulting from a change in the scope of the Renewable Heat Incentive; and
- a reduction of £2 million in the cost of administering the offshore transmission tendering process.

Ofgem carried forward £5.3 million of regulatory activity savings and this will be offset against future licence fee charges over the period up to 2014-15.

## **NAO reports on financial management**

**2.8** Robust cost estimates underpin good planning, decision-making and management. In our 2010-11 report on *Preparations for the roll-out of smart meters*,<sup>15</sup> we found that Ofgem, which managed the first phase of the programme on behalf of the Department of Energy and Climate Change, had remained within the overall annual budget set by the Department. Ofgem and the Department did not, however, agree a budget for the first phase of the programme, which started in December 2009, and Ofgem's monthly spending forecasts for this phase were not linked to completing specific tasks. Ofgem subsequently agreed a budget of £7.5 million in July 2010 for an additional phase, which it completed in March 2011 at a cost of £6.12 million, which was 18 per cent less than forecast.

## **NAO financial audit findings**

**2.9** Our financial audit work indicates that Ofgem has sound systems of financial controls and reporting. The Comptroller and Auditor General gave an unqualified opinion on Ofgem's 2010-11 accounts and Trust Statement. All previous years have also received an unqualified audit opinion.

**2.10** Under HM Treasury's alignment project, for the year ended 31 March 2011 Ofgem was required for the first time to produce a separate Trust Statement for material income streams which, either by convention or statute, were due to the Consolidated Fund. The Trust Statement was audited by the Comptroller and Auditor General, and received an unqualified audit opinion.

<sup>15</sup> C&AG's report, *Preparations for the roll-out of smart meters*, HC 1091 Session 2011-12.  
[http://www.nao.org.uk/publications/1012/smart\\_meters.aspx](http://www.nao.org.uk/publications/1012/smart_meters.aspx)

## **Issues raised in Statements on Internal Control**

**2.11** We work with Departments to improve their published Statements on Internal Control. We aim to ensure that the processes by which Statements are produced are robust and that the statements comply with Treasury guidance.

**2.12** Ofgem's Statement on Internal Control identified no significant internal control issues. It reported that during the year, a number of key activities had been undertaken to monitor and enhance the internal control environment including:

- strategic risks were reviewed by the Senior Management Team, Management Committee and the Audit Committee;
- the appointment of a Risk Manager in August 2010 to further enhance risk management; and
- the completion of a risk management assurance audit by Deloitte in December 2010, which gave Ofgem an overall opinion of 'Satisfactory Assurance'.



# Part Three

## Use of information

**3.1** Public bodies need robust and timely information on context, activities, costs, progress against their objectives, and the cost-effectiveness of their activities. They also need to be able to interpret that information, by reference to trends, expectations, benchmarks and other comparisons, to identify problems and opportunities. Public bodies need reliable information on which to design and deliver services and monitor quality, be confident about their productivity, and drive continuous improvement.

**3.2** The Coalition Government has pledged, under the transparency agenda, to make more government information available to the public to help improve accountability and deliver economic benefits. Ofgem is independent of government, and so is not subject to the reporting framework that requires central government departments to publish Quarterly Data Summaries showing progress against specific milestones, input indicators and impact indicators. The principles of providing transparent data to support public accountability are nevertheless relevant to Ofgem.

### **Reporting performance: Annual Reports and Corporate Plans**

**3.3** Ofgem has designed its performance measurement system around its four strategic priorities, which together cover both its regulation activity and its management of environmental programmes (paragraph 1.4). Individual priorities have an associated set of activity-based deliverables that describe specific outputs, such as the publication of key documents or achievement of certain milestones. Each year, Ofgem sets out in its five-year Corporate Strategy and Plan a new schedule of deliverables due in each quarter of the forthcoming financial year, and it reports on performance against them in its annual report. These are equivalent to the milestones published in departmental business plans.

**3.4** Ofgem reports on its operational performance using corporate performance indicators, which cover areas such as response times to complaints. It also reports on performance against its internal sustainable development targets, which provide a measure of Ofgem's progress towards operating its business more sustainably.

**3.5** Ofgem does not identify and report progress against measures that are equivalent to the impact indicators in departmental business plans, although it publishes a range of market data, for example in its regular Electricity and Gas Supply Market Reports.<sup>16</sup>

**3.6** We reported in our briefing on Ofgem's performance in 2009-10 that Ofgem's performance system did not provide a measure of the effectiveness of its regulatory activities or the delivery of environmental programmes.<sup>17</sup> In evidence given to the Committee of Energy and Climate Change's inquiry into Electricity Market Reform, the Chief Executive of Ofgem said in January 2011 that Ofgem was examining its approach to performance indicators.<sup>18</sup>

**3.7** Ofgem has taken steps in its internal performance monitoring system to provide a stronger focus on outcomes and has increased its monitoring of external data and qualitative outcomes. It is also trialling a new quarterly performance report for the Gas and Electricity Markets Authority. It has not introduced measures of the effectiveness of its regulatory activities and delivery of environmental programmes in its public reporting.

## **Performance reported by Ofgem**

**3.8** Ofgem's deliverables for 2010-11 were set out in its Corporate Strategy and Plan for 2010-15.<sup>19</sup> Ofgem confirmed in its annual report that it had achieved 41 of the 48 deliverables it had set itself for 2010-11 (**Figure 5**). Key deliveries achieved during the year included the launch of Feed-in-Tariffs in April 2010, commencing the second round of tenders for offshore electricity transmission networks in November 2010 and completing a follow-up probe into vulnerable customers in March 2011.

<sup>16</sup> See, for example, Ofgem, *Electricity and Gas supply Market Report* October 2011.

[http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/SMR\\_Oct\\_2011.pdf](http://www.ofgem.gov.uk/Markets/RetMkts/rmr/Documents1/SMR_Oct_2011.pdf)

<sup>17</sup> [http://www.nao.org.uk/publications/1011/performance\\_of\\_ofgem.aspx](http://www.nao.org.uk/publications/1011/performance_of_ofgem.aspx)

<sup>18</sup> <http://www.publications.parliament.uk/pa/cm201012/cmselect/cmenergy/742/11011802.htm>

<sup>19</sup> <http://www.ofgem.gov.uk/About%20us/CorpPlan/Documents1/Corporate%20Strategy%20and%20Plan%202010-2015.pdf>

**Figure 5**

## Ofgem's performance against deliverables by strategic theme

Theme	Number in Corporate Plan	Total achieved in year	Deferred to 2011-12	No longer apply
1. Building a low carbon economy	4	4	0	0
2. Helping to maintain security of supply	7	6	0	1
3. Promoting quality and value for customers	25	21	2	2
4. Timely and efficient delivery of Government programmes	12	10	1	1
<b>TOTAL</b>	<b>48</b>	<b>41</b>	<b>3</b>	<b>4</b>

Figure Source: Ofgem Annual Report and Accounts 2010-11

**3.9** Ofgem completed the three deferred deliverables by July 2011. It:

- published a consultation on proposals for aligning the methods used by electricity distribution network operators to determine charges for users of their higher voltage electricity networks. The aim of the proposed changes is to better protect the interests of current and future network users.
- took decisions on the certification of transmission system operators under the European Third Package of energy legislation, which requires operators to unbundle from gas production, electricity generation and supply interests.
- published guidance on applying for the Renewable Heat Incentive in advance of it going live.

**3.10** The four deliverables that Ofgem reported no longer applied were to :

- consult on the methodology used in gas entry substitution, which involves the transfer of unsold entry capacity on the gas transmission system to meet demands elsewhere. The consultation was not needed because market participants showed insufficient demand for additional capacity on the network.

- publish a consultation on security of energy supplies to the Olympics because there were no submissions from network companies for additional Olympic-related funding or requests for service quality derogations.
- publish initial consultation on regulatory arrangements for independent distribution network owners and independent gas transporters, as Ofgem concluded that other projects designed to enhance the regulatory framework for independent network companies provided a better use of Ofgem's resources.
- publish guidance on the carbon capture and storage levy. This was not needed following the government's decision to fund the first carbon capture and storage project from general taxation.

**3.11** Ofgem reported that in 2010-11 it had fully achieved 12 out of its 15 corporate performance indicators, which cover its performance, for example, on responding to complaints and paying invoices. The indicators it did not meet were:

- responding to 90 per cent of complaints on enforcement matters, confirming whether it would investigate within 4 weeks. Ofgem attributed this to the number of cases it received and resource difficulties;
- responding to 10 per cent of suppliers who have submitted Carbon Emissions Reduction Target (CERT) schemes for approval within 10 days of submission deadline, because legislative changes to the scheme rules required a change in the guidance issued by Ofgem, which delayed the processing of submissions; and
- following up with 100 per cent of generators' outstanding issues in their applications for accreditation for Feed in Tariffs within 10 working days. Ofgem attributed this to the large number of microgenerator applications received at the end 2009-10 seeking to migrate from the Renewables Obligation to Feed in Tariffs.

**3.12** As a public body, Ofgem must comply with central government sustainability requirements: the Sustainable Operations on the Government Estate (SOGES); and the coalition government's commitment that all Departments cut their carbon emissions by 10 per cent within a year from May 2010 and its subsequent Greening Government Commitments.

**3.13** In addition to addressing its performance in its annual report, in July 2011 Ofgem reported its progress against its Sustainable Development Action Plan targets.<sup>20</sup> Ofgem reported that it had met all the government's targets for 2010 and 5 of the 7 targets for 2020. Its total carbon emissions reduced by 16 per cent during the year 2010-11, from 986 tonnes to 826 tonnes, and by 42 per cent since 2004. Ofgem reported that it had achieved or was on course to achieve 24 of the 34 sustainable development targets it set for itself (**Figure 6**) and, additionally, that none of its waste was sent to landfill. Targets that it did not achieve included reducing total waste produced by 5 per cent compared with 2009 and undertaking a minimum of 20 per cent of official journeys between London and Glasgow by rail, although Ofgem told us that proportion had subsequently increased to 30 per cent.

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**Figure 6**

Ofgem's performance against its 2010 Sustainable Development Action Plan targets

Theme	Number in Plan	Total achieved or on course	Total not achieved or not on courses
1. Climate change and energy efficiency	16	10	6
2. Waste management and recycling	6	5	1
3. Procurement	3	3	0
4. Travel	5	3	2
<b>5. People</b>	4	3	1
<b>TOTAL</b>	34	24	10

Figure Source: Ofgem 2010 *Internal Sustainability Performance Report*, July 2011<sup>21</sup>

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<sup>20</sup> Ofgem, 2010 *Internal Sustainability Performance Report*, July 2011.

<http://www.ofgem.gov.uk/ABOUT%20US/CORPPLAN/Documents1/internalsusreport.pdf>

<sup>21</sup> <http://www.ofgem.gov.uk/About%20us/CorpPlan/Documents1/internalsusreport.pdf>

## Part Four

### Service delivery

**4.1** Public services are different in the ways they are delivered but their quality and cost effectiveness depends on a number of common minimum requirements. For example, service delivery requires a well thought-out delivery model, sound programme and project management, strong commercial skills, mature process management and a real understanding of customer needs. Many of our reports to Parliament cover these issues.

**4.2** In this section we focus on developments in the delivery of Ofgem's programmes.

#### **Developments in delivering energy and environmental programmes**

**4.3** The programmes delivered by Ofgem had a total estimated value in 2010-11 of around £5 billion (**Figure 7**).

**4.4** Significant developments during last year in the programmes delivered by Ofgem include:

- In December 2010, the Department of Energy and Climate Change announced that it would bring forward its statutory consultation on the banding of the Renewables Obligation from spring 2012 to summer 2011, and announce its decisions in the autumn.<sup>22</sup> The Department also introduced new mandatory sustainability standards for biomass and sustainability criteria for bio-liquids. Ofgem has forecast that the new sustainability standards will increase its Renewables Obligation administration costs in 2011-12 by 50 per cent compared to the previous year, to £3.3 million.<sup>23</sup>

<sup>22</sup> [http://www.decc.gov.uk/en/content/cms/news/pn10\\_126/pn10\\_126.aspx](http://www.decc.gov.uk/en/content/cms/news/pn10_126/pn10_126.aspx)

<sup>23</sup> Ofgem, *Consultation on Ofgem's costs for administering the Renewables Obligation*, July 2011.

[http://www.ofgem.gov.uk/Sustainability/Environment/RenewablObl/Documents1/RO%20Costs%202011\\_12%20Consultation.pdf](http://www.ofgem.gov.uk/Sustainability/Environment/RenewablObl/Documents1/RO%20Costs%202011_12%20Consultation.pdf)

**Figure 7****Programmes delivered by Ofgem and their associated costs/values in 2010-11**

<b>Programme</b>	<b>Description</b>	<b>Type of cost</b>	<b>£ million</b>
Renewables Obligation /Renewable Energy Guarantees of Origin	Places an obligation on suppliers to source an annually increasing amount of electricity supplies from renewable sources	Cost to suppliers	1,300
Carbon Emissions Reduction Target	Requires all domestic gas and electricity suppliers with more than 50,000 customers to make savings in carbon emissions by promoting the uptake of low carbon energy solutions such as loft insulation.	Cost to suppliers	1,200
Community Energy Savings Programme	Requires gas and electricity suppliers and electricity generators to deliver energy saving measures to domestic consumers in specific low income areas of Great Britain	Cost to suppliers	100
Offshore Transmission Licensing	Award licences to operate offshore transmission networks through a competitive tender process	Transfer value of transmission assets in the first tender round	2,200 <sup>1</sup>
Climate Change Levy exemption	Administering the Climate Change Levy exemptions, which includes issuing Levy Exemption Certificates and providing information on exemptions to HM Revenue and Customs	The saving that suppliers make as a result of claiming exemptions	200
Low Carbon Networks Fund	Provides financial support to projects sponsored by electricity distribution network operators to try out new technology that supports low carbon energy use. It is funded by Distribution Network Operators, who can recover the cost from customers.	Value of awards	62
Feed-in Tariffs	Requires licensed electricity suppliers to pay a tariff to small-scale low-carbon generators for the electricity they produce.	Cost to suppliers	12 <sup>2</sup>

**NOTES**

1. This is the total value of the first and second tenders. Not all of these were completed in 2010-11.
2. 2010-11 was the first year of the Feed-in Tariffs scheme. Ofgem expects the cost to be significantly higher in 2011-12.
3. The Renewable Heat Incentive and Warm Home Discount are not included above as these programmes did not come into operation until 1 April 2011.

Figure Source: Ofgem

- In March 2011, Ofgem awarded the first licence to operate a high voltage offshore transmission link to TC Robin Rigg Ofo Ltd. This company will operate the £65 million link transporting renewable electricity from the 180 megawatt Robin Rigg wind farm in the Solway Firth to the onshore grid for a period of 20 years.
- During 2010-11, Ofgem made the first awards, totalling £62 million, from its £500 million Low Carbon Networks Fund. The awards are designed to speed up the development of smart grids, which could allow the operators of electricity transmission and distribution networks to better manage supply and demand, to meet low carbon energy use. The awards were made to CE Electric (£26.8 million), UK Power Networks (£24.3 million), Western Power Distribution (£7.8 million) and Central Networks (£2.8 million).<sup>24</sup> These projects are funded by Distribution Network Operators, who are permitted to recover a designated cost from customers.
- Feed in Tariffs were introduced in April 2010 to boost the generation of electricity from smaller sources of sustainable generation and as at March 2011, Ofgem had registered more than 40,000 installations. The scheme requires Licensed Electricity Suppliers to pay a generation tariff and an export tariff to small-scale low-carbon generators for the electricity they generate and they export to the grid. Suppliers are responsible for registering eligible installations, processing generation data, and making relevant payments. Ofgem is responsible for maintaining a central register of accredited Feed-in-Tariff installations and ensuring that suppliers comply with scheme requirements.
- The Renewable Heat Incentive is a government scheme that provides financial support to non-domestic renewable heat generators and producers of biomethane. During 2010-11, Ofgem prepared for the implementation of this scheme, which it expects to administer. On 29 September 2011, the Department of Energy and Climate Change announced that it would not launch the Renewable Heat Incentive for non-domestic generators on 30 September 2011 as originally planned, as the European Commission had raised concerns that the tariff for larger installations with a capacity to generate one kilowatt thermal or more from biomass had been set too high. The Department reported on 26 October 2011 that the European Commission had given state aid approval to the scheme, subject to the large biomass tariff being reduced from 2.7 pence to 1 pence per kilowatt hour. The Department intends to launch the scheme by the end of November 2011, subject to Parliamentary approval.



- The Warm Homes Discount scheme, which came into operation in April 2011, was designed to replace existing voluntary social tariffs, discounts and rebates. It requires energy suppliers with more than 250,000 domestic customers to provide an annual discount on electricity bills to all low income pensioners. Suppliers must also provide discounts to a selection of other energy consumers who are recipients of certain benefits prescribed by Government or who suppliers can demonstrate are in fuel poverty or at risk of fuel poverty. The estimated value of the scheme over the four years to 2014-15 is £1.13 billion. Ofgem's role is to monitor and, where necessary, help suppliers comply with their obligations.

### **NAO reports on service delivery**

**4.5** In our report *Preparations for the roll-out of smart meters*,<sup>25</sup> we examined the effectiveness of programme management, which was performed by Ofgem on behalf of the Department of Energy and Climate Change. We found that there had been significant weaknesses in the programme management of the first phase of the programme. The Department had not initially established an agreement with Ofgem that clearly identified the activities that would be needed to complete the first phase, key priorities or how Ofgem's performance would be measured. The Department announced in December 2010 that it would manage the next stage of the programme itself. Its decision was informed by a review of programme governance arrangements and strategic options for subsequent phases. The Department concluded that the cost of managing the programme itself would be broadly similar to the cost of continuing to outsource programme management to Ofgem, but managing it in-house would increase the likelihood of success by strengthening programme leadership and capability. These changes achieved a clearer separation of duties between programme delivery and the regulation of the energy industry's management of the roll-out.

<sup>25</sup> C&AG's report, *Preparations for the roll-out of smart meters*, HC 1091 Session 2011-12.  
[http://www.nao.org.uk/publications/1012/smart\\_meters.aspx](http://www.nao.org.uk/publications/1012/smart_meters.aspx)

# Appendix One

## Relevant NAO reports since 2008

<b>Title</b>	<b>Date</b>	<b>Link</b>
Preparations for the roll-out of smart meters, HC 1091, Parliamentary Session 2011-12	June 2011	<a href="http://www.nao.org.uk/publications/1012/smart_meters.aspx">http://www.nao.org.uk/publications/1012/smart_meters.aspx</a>
Performance of Ofgem	October 2010	<a href="http://www.nao.org.uk/publications/1011/performance_of_ofgem.aspx">http://www.nao.org.uk/publications/1011/performance_of_ofgem.aspx</a>
The Electricity Generating Landscape in Great Britain	July 2010	<a href="http://www.nao.org.uk/publications/1011/electricity_generating.aspx">http://www.nao.org.uk/publications/1011/electricity_generating.aspx</a>
Review of the UK's Competition Landscape	March 2010	<a href="http://www.nao.org.uk/publications/0910/competition_landscape.aspx">http://www.nao.org.uk/publications/0910/competition_landscape.aspx</a>
Protecting consumers? Removing retail price controls HC 342, Parliamentary Session 2007-2008	March 2008	<a href="http://www.nao.org.uk/publications/0708/protecting_consumers_removing.aspx">http://www.nao.org.uk/publications/0708/protecting_consumers_removing.aspx</a>

# Appendix Two

## Other sources of information

### Reports from the Committee of Public Accounts since 2008

Title	Date	Link
Protecting consumers? Removing retail price controls, Fifty-second Report of Session 2007-08 HC 571	October 2008	<a href="http://www.publications.parliament.uk/pa/cm200708/cmselect/cmpubacc/571/571.pdf">http://www.publications.parliament.uk/pa/cm200708/cmselect/cmpubacc/571/571.pdf</a>

### Recent reports from Central Government

Title	Date	Link
Ofgem Review Final Report, DECC	July 2011	<a href="http://www.decc.gov.uk/assets/decc/11/meeting-energy-demand/energy-markets/2151-ofgem-review-final-report.pdf">http://www.decc.gov.uk/assets/decc/11/meeting-energy-demand/energy-markets/2151-ofgem-review-final-report.pdf</a>
Review of DECC's Delivery Landscape, DECC	May 2011	<a href="http://www.decc.gov.uk/assets/decc/About%20us/1656-delivery-review.pdf">http://www.decc.gov.uk/assets/decc/About%20us/1656-delivery-review.pdf</a>

## Where to find out more

The National Audit Office website is

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