



Reflecting on our Corporate Strategy 2009-14

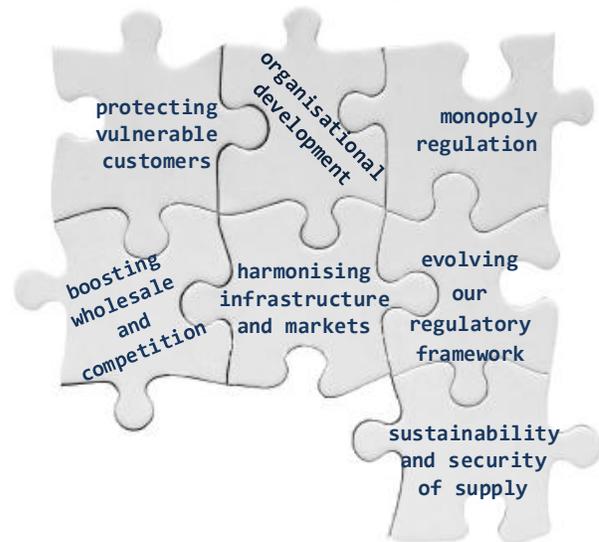
A mid-term review discussion paper

July 2011

Background

- the Utility Regulator has existed, in its current form, since 1 April 2007.
- we are the independent economic regulator of the electricity, gas, water and sewerage industries in Northern Ireland.
- we developed our first Corporate Strategy in 2009 – to cover the period to 2014.
- our strategy was developed in the context of eight challenges and drivers:
 - ⇒ unstable prices for consumers and the need for concerted actions
 - ⇒ the benefits of boosting competition in the retail and wholesale sectors
 - ⇒ environmental sustainability
 - ⇒ security of supply issues
 - ⇒ the need to ‘harmonise’ our strategy with others
 - ⇒ the growing importance of EU-level factors to our work
 - ⇒ technological and information advances
 - ⇒ the need for us to run a fit-for-purpose office.
- in light of these drivers and challenges, we identified seven strategic themes which, taken together, set out the direction of our Corporate Strategy.
- Figure 1 sets out the strategic themes

Figure 1: Corporate Strategy themes



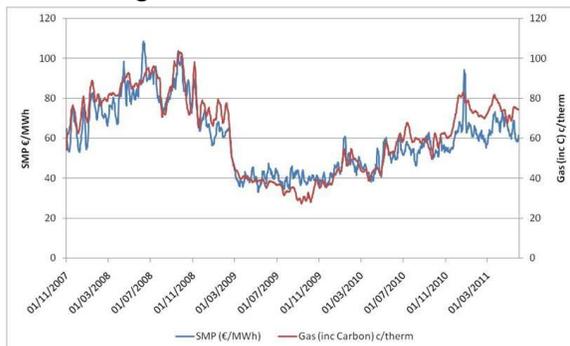
The focus of our mid-term review

- the focus of our review is twofold:
 1. identifying internal or external developments that have occurred since 2009 (e.g. strategic reviews or legislation).
 2. if there are new and/or significant developments since 2009, how do they impact on our strategy and how should they be reflected (if at all) in an updated strategy.

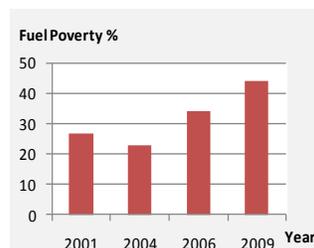
Key developments - impacting on challenges and drivers since 2009

Consumer prices and the need to optimise the benefits from renewable energy and minimise the impact on fuel poverty

- we took a decision in 2010 to cancel certain Generating Unit Agreements to deliver savings to consumers.
- the first price control for water and sewerage services in Northern Ireland, PC10, was published in 2010, identifying £91 million of efficiencies over a three-year period.
- while consumer energy prices decreased, and were stable in 2009 and 2010, increasing volatility on international wholesale markets (see graph below) during 2011 is increasing costs.



- the level of fuel poverty in Northern Ireland has increased in the last few years.



- we published a consultation paper in early 2010 to inform the wider discussion on fuel poverty and set out the options for assisting vulnerable consumers with energy affordability.
- our social action plan provided direction to our work on addressing social need and this has included significant initiatives (such as research on debt relating to energy consumers).
- an annual cost reporting regime was introduced for all gas network operators which will allow us to more closely monitor performance against each operator's price control reviews.
- work on the next electricity network price control (RP5) has commenced and will consider carefully the level of investment required and medium term plan for renewable integration.

Boosting competition

- new suppliers entered the domestic energy markets in Northern Ireland during 2010, providing competition to incumbent suppliers.
- domestic consumers began switching suppliers from 2010, although levels of switching remain low.
- de-regulation of the domestic energy market commenced in the Republic of Ireland in 2011.
- Ofgem's Retail Market review proposals were published in March

2011, and propose an overhaul the energy market in Great Britain to 'work more effectively in the interests of consumers'.

- we published a paper reviewing the impact of the introduction of retail competition in electricity.
- we investigated the business electricity market in Northern Ireland in 2010 and produced a report outlining initiatives to improve information and communication for business consumers.
- we are reviewing competition in the wholesale market and reviewing market power and liquidity.
- there were two major acquisitions in the electricity industry in 2010 – ESB acquired the NIE network business and the AES corporation acquired Premier Power Limited.

Environmental sustainability and security of supply issues

- the Strategic Energy Framework (SEF) was published by the Department of Enterprise, Trade and Investment (DETI) in 2010, and set a target of 40% electricity consumption from renewables by 2020.
- following consultation with the UR and other stakeholders, the Department for Regional Development (DRD) produced its Social and Environmental Guidance to inform investment decisions for NI Water's PC10.

- the environmental sustainability agenda has been advancing – review of renewables support mechanisms, the DETI review of energy saving approaches, an EU review of Energy Services Directive.
- a consultation into electricity connections policy was completed and we are now looking at contestability for connections in the future.
- we published a new Framework Document for the Northern Ireland Sustainability Energy Programme (NISEP - formerly the Energy Efficiency Levy).
- along with DETI we carried out a feasibility study to extend the natural gas network to other parts of Northern Ireland.
- we have published the criteria to be used in determining the most appropriate gas storage regulatory framework for Northern Ireland.
- we carried out an investigation on major water supply failures during late 2010/early 2011, and our report included a water recovery action plan with 56 actions.

Harmonising markets

- a high-level workplan to harmonise arrangements for gas on the island of Ireland (called the Common Arrangements for Gas – CAG) was published in 2011.
- market development has enabled:
(1) increased trading across the interconnector to Scotland – the

export capacity of the Moyle interconnector increased from 80 MWs to 300 MW and, (2) the planning of a future East-West interconnector to Wales.

- the proposal to change to a global aggregation settlement was published for consultation in 2010, with the main objective of allowing all suppliers to be treated equally within the Single Electricity Market (SEM).
- we have continued to work on the harmonisation of systems between all-island suppliers and the network operators, which will be implemented by May 2012.
- the Department of Energy and Climate Change (DECC) have issued electricity market reform proposals, with potential implications for the carbon tax and the Renewables Obligations Certificates regime.
- the Department of Business, Innovation and Skills (BIS) issued its Principles of Economic Regulation which reaffirms the importance of stable and predictable regulatory frameworks.
- reviews of Ofgem and Ofwat were due to report in Spring 2011.
- we developed a Memorandum of Understanding with DRD to support the operation of NI Water within a regulatory framework and being largely publicly funded.

The growing importance of EU-level factors

- the EU Third package (IME3) became law in September 2009 and introduced a series of measures around consumer protection, competition and regulatory requirements, and also amended our statutory duties.
- we are working with both Ofgem and CER to increase integration between markets.
- a new Europe-wide energy regulator (ACER) was established in early 2011, and will play a key role in the integration of the EU's energy markets- we are working with Ofgem to ensure adequate representation.

Technological and information advances

- work continues across Europe on biogas projects which feed directly into the grid.
- we are supporting a smart metering trial targeting vulnerable consumers.
- along with DETI, we are creating a plan for smart metering in Northern Ireland.
- the development of a Smart Grid in Northern Ireland is being progressed within network development proposals for RP5.

A fit-for-purpose office

- we established a dedicated unit to support the development of retail competition.

- as a multi-utility regulator we are uniquely placed and we have sought to exploit this.
- an internal project was established along with an associated board advisory group - to drive forward best practice in our approach to regulating across the different utility sectors.
- we have taken steps to minimise our costs in light of the constraints on public sector spending.

Impact on our Corporate Strategy (in relation to themes)

Monopoly regulation

- protecting consumers through our scrutiny of tariffs and utility company costs remains as relevant in 2011 as it was in 2009.
- we will continue to enhance our understanding of utility companies' costs through cost reporting and monitoring.
- we will exploit our cross utility focus to further develop our cross-utility workstream to stay apprised of regulatory developments elsewhere and build regulatory best practice.
- the cross-utility workstream will inform a consistent approach, wherever appropriate, to price controls and focus on opportunities to reduce costs, while incentivising utility companies to provide efficient and effective services to consumers.
- we will work with DRD and stakeholders to ensure that the

regulatory regime continues to protect and provide value to consumers under the current arrangements.

Sustainability and Security of Supply

- given the greater emphasis on sustainability, the need to mainstream this in our work is paramount.
- we are aware of the impact of climate change, and will take steps with regulated companies - given recent adverse weather events - to mitigate the impact of these events on consumers.
- our scrutiny will take account of the SEF objective (of 40% of electricity generated from renewable sources by 2020 – this is currently around 10%) while balancing this with any impact on costs to consumers.
- we will work with DETI to ensure that any new and revised support mechanisms for renewables in NI are fit for purpose.
- a possible role in relation to renewable heat will be kept under review, particularly as it impacts on gas.
- we will take account of developments in GB, including the electricity market reform in our work (e.g. on the future of the NI Renewables Obligation).
- any roll-out of smart metering will be considered in the context of realistic benefits to consumers.
- we will continue to engage with stakeholders to address barriers and

realise effective demand side participation in the energy market.

- we will consider the impact of extreme weather conditions on security of supply, consider the risks, the need for investment and benefits to consumers.
- consideration will be given to the many water industry reviews which have been published and are aimed at addressing sustainability, affordability and regulatory issues.
- we will support and assist DRD in the preparation of a Water Strategy for Northern Ireland.

Protecting vulnerable consumers

- ultimately, the best way to protect vulnerable consumers is by limiting or preventing price increases through effective regulation of monopolies and the promotion of competition.
- while our focus is on economic regulation, we stand ready to contribute to initiatives that protect vulnerable consumers.
- fuel poverty remains an issue for the NI Executive, and we remain ready to provide independent advice and information on energy-related options.
- we will specifically roll-out consumer protection provisions arising from IME3.
- our social action plan commitments will remain a key reference point for our work on protecting vulnerable consumers.

Boosting competition

- our corporate strategy set out our commitment to retail competition and major progress has been made in making choice a reality for consumers.
- we will continue to encourage retail competition and we will set out our view on the future development of the retail market through a policy position paper, which we will consult on during 2011.
- this policy position paper will also address the high level question of how regulation protects consumers where competition is not effective.
- we will monitor consumer benefits from competition by researching their attitudes and expectations.
- we will review new entrants' behaviour in the retail market, and promote the development of relevant codes of practice.
- we will monitor and review arrangements to ensure an appropriate level of liquidity in the electricity market.
- we will continue to represent the consumer interests in any review of Generating Unit Agreements.

Harmonising energy markets

- we believe that harmonising energy markets has the potential to deliver significant benefits to Northern Ireland consumers.
- we will assess options for progressing the harmonising of all-island retail systems.

- the SEM Committee is working towards an enduring solution for Transmission Loss Adjustment Factors and Generator Transmission Use of System charges to be effective from October 2011.
- along with CER, we will work to implement the Common Arrangements for Gas project to the benefits of consumers on the island of Ireland.
- EU framework guidelines on market harmonisation could require changes to the SEM design by 2014 - we are working on this via the SEM Committee.
- we will continue to engage with stakeholders to develop the SEM in line with realisable benefits to consumers.

Evolving our regulatory framework

- the need to evolve our regulatory framework remains important.
- we will consider our approach in dealing with competition and related issues in light of the emerging framework in GB.
- we will fully implement the IME3 requirements to ensure enhance levels of consumer protection.
- through co-operative arrangements that we are establishing with partner organisations (e.g. Ofgem), we will seek to influence developments at a European level in relation to energy.
- we will continue to work with the DRD, NI Water and other stakeholders to develop and apply

our regulatory framework for PC13 which delivers benefit to water consumers.

Organisational development

- we will examine the structure of our organisation, looking for potential changes that improve our strengths and make us a better fit-for-purpose team.
- given the broader public sector environment we will continue to exercise prudence in setting out budget and manage our costs carefully.
- we will ensure we optimise the use of available resources across the utility sectors.

What do you think?

The purpose of this short paper is to generate discussion to inform our mid-term review.

We have set out our view on key developments in the wider environment since 2009.

An assessment of the impact of these developments on our work is also presented.

Our overall view is that the strategic direction outlined in our Corporate Strategy 2009-14 remains relevant and is the right high-level approach at this time.

The mid-term review does however prompt consideration on the evolution of strategic workstreams and we allude to these in this paper. Specifically, we have identified a need for us to:

- utilise our cross-utility workstream more to drive best regulatory practice (e.g. cost reporting and monitoring);
- mainstream sustainability across all aspects of our work, engaging with key stakeholders to support key sustainability targets;
- strategically set out the direction for the future development of retail competition;
- seek to influence developments at a European level in relation to energy.

We would therefore welcome stakeholders' views on the following:

- have we considered all of the key external developments that have occurred since 2009;
- do you agree with our overall view that the strategic direction set out in our corporate strategy remains relevant and is the right high-level approach;

- do you agree with the four areas where we think we need to evolve our strategic workstreams; and
- is there anything else that we need to consider regarding our strategic direction over the period to 2014 (when the current corporate strategy period ends).

How to comment on our mid-term review

- we welcome views on this mid-term review
- contributions can be sent to us via:
 - e-mail – elena.ardines@uregni.gov.uk
 - postal:
Elena Ardines
Utility Regulator
Queens House
14 Queen Street
Belfast
BT1 6ED.
- we would appreciate any comments **by 9 September 2011.**