

October 2000

Utilities Act

**Standard licence conditions
Volume 1**

Final proposals

Summary

The Utilities Act received Royal Assent on 28 July 2000. The Act has a significant impact on both gas and electricity licences. The Act will require distributors of electricity to be authorised by licence or exemption. There will therefore be a new licence to distribute electricity. The public electricity supply (PES) and second tier electricity supply licence will be brought together into a single type of supply licence. There will be consequential amendments to gas licences.

The Act makes provision for standard licence conditions in electricity, reflecting existing provisions in gas. These standard licence conditions will be determined by the Secretary of State. Ofgem has consulted twice previously on what obligations it might be appropriate to include in each type of electricity licence and the amendments necessary to the existing standard conditions in gas licences. Ofgem has considered the comments received and this paper summarises the previous proposals in the last consultation and the responses received. The paper also details Ofgem's final proposals in respect of the standard licence conditions. The draft versions of each of the seven licence types are published separately.

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1. Introduction

Purpose of document

- 1.1 The purpose of this document is to seek views on the final draft versions of the standard licence conditions in gas supply, shipping and transportation and electricity supply, distribution, generation and transmission.

Background

(i) Legal background

- 1.2 The Utilities Act received Royal Assent on 28 July 2000. The Utilities Act will modernise the framework for energy regulation in Great Britain. The Act amends both the Gas Act 1986 and the Electricity Act 1989 and provides for various pieces of secondary legislation.
- 1.3 The Utilities Act will have a significant impact on both gas and electricity licences. Existing arrangements will change quite substantially in a number of ways.
- 1.4 The Utilities Act introduces a new prohibition on the activity of distribution without a licence or exemption. Electricity supply and distribution will become separate licensable activities with a bar on the same legal entity holding both an electricity supply and an electricity distribution licence. The distinction in legislation between Public Electricity Supply (PES) and second tier electricity supply licences will be removed.
- 1.5 The concept of standard licence conditions, already used in gas, will be extended to electricity. Initially, the Secretary of State will determine the standard licence conditions for each licence type. Thereafter it will be for the Authority to propose modifications to licences.
- 1.6 The Utilities Act establishes a mechanism by which the standard conditions of electricity licences may be modified by the Authority with majority consent. The collective licence modification procedures are revised in relation to gas. The Secretary of State is provided with powers to prescribe in secondary legislation numerical values for the key

parameters to be used for determining consent. Where sufficient opposition exists among eligible licence holders to block a modification, the Authority may make a reference to the Competition Commission. DTI have consulted once on these blocking minority thresholds¹ and Ofgem expects that there will be a further consultation on this before the thresholds are determined.

(ii) Policy background

- 1.7 The government has made clear that the regulatory framework in gas and electricity, including the licensing regimes, should be aligned as far as possible² as well as being updated. The Utilities Act recognises the changes in gas and electricity markets that have already taken place, that is, increasing competition within, and convergence between, the two energy markets. It is also intended to ensure sufficient flexibility to adapt to changes that may take place in the future without the need for further primary legislation. The desire for flexibility and adaptability suggests that, while primary legislation should be able to provide the overall structure for energy regulation, detailed provisions should be set by secondary legislation and licence conditions which can be amended relatively quickly.
- 1.8 Ofgem has followed this policy by aligning provisions in the standard licence conditions as far as practicable by amending existing provisions in both gas and electricity, introducing new obligations in one fuel where the other has such an obligation and removing obligations from gas or electricity or both where it is thought that an obligation is no longer required. The Act includes a new principal objective on the Authority to “protect the interests of consumers, wherever appropriate by promoting effective competition”. Ofgem has considered this objective in relation to aligning customer protection obligations, such as the terms to be included in a domestic supply contract and when splitting the Social Action Plan provisions between supply and distribution/transportation.

¹ Modification of standard conditions of gas and electricity licences by the Gas and Electricity Markets Authority (Collective licence modifications), March 2000

² A Fair Deal for Consumers, Modernising the Framework for Utility Regulation, The Future of Gas and Electricity Regulation – The Government’s Proposals for Legislation, DTI, October 1999

- 1.9 The separation of electricity distribution from supply is a key policy objective ensuring that monopoly networks are separate from competitive activities. Ofgem has separately consulted on the financial ringfencing provisions deemed necessary to ensure effective separation and has already introduced obligations to effect managerial and operational separation.
- 1.10 The introduction of Great Britain wide licences is intended to reflect the fact that most companies operate on a Great Britain wide basis and most conditions apply across Great Britain.

Consultation

- 1.11 Given its new principal objective, Ofgem is keen to ensure that certain regulatory safeguards are focused on an appropriate group of customers. Ofgem has consulted separately in July 2000 on the categories of gas and electricity customers who should continue to benefit from certain regulatory safeguards. The outcome of this consultation is explained in Chapter 4 and Appendix 1 contains a summary of the responses received.
- 1.12 Ofgem has previously consulted on standard licence conditions in November 1999³ and February 2000⁴, on behalf of the Secretary of State. Both of these consultations were accompanied by draft versions of the standard licence conditions for each of the licence types.
- 1.13 Ofgem chaired a small informal working group which met fortnightly between July and September inclusive and which discussed specific licensing issues. The group was made up of representatives from both gas and electricity sectors, by all licence types, consumer representatives and DTI.
- 1.14 Ofgem has also consulted separately on issues that arise from the change in legislation and which impact on the standard licence conditions. A joint Ofgem/DTI decision document on the proposed licence conditions for the New Electricity Trading Arrangements (NETA) was published in June 2000. Ofgem is proposing changes to the Master Connections and Use of System Agreement (MCUSA) which will result in the

³ Initial Proposals on Standard Licence Conditions – A Consultation Paper

⁴ Utilities Bill Standard Licence Conditions – Volume 1 Consultation Paper

Connections and Use of System Code (CUSC) being implemented in place of MCUSA through the power in the Utilities Act to introduce NETA. Other consultations on issues that follow from the Utilities Act include that on financial ring-fencing in distribution⁵ published in April 2000 and that on non-discrimination in supply published in July 2000⁶. Chapter 6 contains more detail on the latter and responses are summarised in Appendix 2.

1.15 In addition to these consultations, Ofgem has consulted in other areas, outside of the changes resulting from the Utilities Act, where licence modifications have resulted or may result. The Social Action Plan⁷ modifications proposed in May 2000 have been included in existing licences and the obligations have been transferred to the standard licences, split as appropriate between supply and distribution/transportation. For completeness, Ofgem has included proposed modifications which are currently being voted on. These are the modifications to the Marketing condition⁸ and the modifications proposed in the March consultation, Supplier's Right to Object to Customer Transfer on the Grounds of Insufficient Termination Notice. These will only be included in the standard licence conditions determined by the Secretary of State where voting demonstrates a sufficient majority of licensees in favour.

Structure of this Document

1.16 Chapter 2 sets out the background to this consultation and Chapter 3 sets out the policy in respect of issues common across more than one licence type. Chapter 4 explains the policy in relation to customer protection issues whilst Chapter 5 deals with other general policy issues. Chapter 6 deals with the issues affecting the supply licences in both gas and electricity whilst chapter 7 discusses those affecting distribution. Chapters 8 to 11 deal with the issues relating to transportation, transmission, generation and shippers' licences respectively. All of the foregoing include a summary of Ofgem's proposals on each of the issues as set out in the previous consultation on standard licence conditions, a summary of responses to that consultation, and Ofgem's views. Chapter 12 identifies the stakeholders, that is, those parties which have a particular interest in this consultation and Chapter 13 outlines the next steps. Chapter 14 contains the Appendices.

⁵ Electricity Distribution Licences: Proposals on Standard Conditions for the Financial "Ring-fence" – Response to Consultation

⁶ Gas and Electricity Supply Licences: Proposals for Standard Non-discrimination Licence Conditions

⁷ Enhancing Social Obligations: Decision Document

⁸ Marketing Gas and Electricity: Decision Document and Proposals on the Modification of Licence Conditions, June 2000

1.17 Volumes 2 to 8, which accompany this document, set out the proposed draft standard conditions for each licence type:

Electricity Supply	Volume 2
Electricity Distribution	Volume 3
Electricity Transmission	Volume 4
Electricity Generation	Volume 5
Gas Supply	Volume 6
Gas Shipping	Volume 7
Gas Transportation	Volume 8

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Timetable

1.18 The deadline for responses to this consultation is Friday, 8 December 2000.

Responses should be sent to:

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Contact

1.19 If you have any questions about this document or the associated standard licence conditions, Amanda McIntyre on 020-7932-6358 will be pleased to assist you.

Confidentiality

1.20 In accordance with our normal practice, we intend to make responses to this consultation publicly available, through the Ofgem library. However, if asked to do so, we shall respect the confidentiality of any response. Respondents wishing their responses to remain confidential should clearly mark the documents to that effect.

2. Background to this consultation

Previous consultation

- 2.1 As stated in Chapter 1, Ofgem has previously consulted twice on what conditions might be appropriate for the new standard licences and published two versions of the draft standard licence conditions for each type of licence. The first consultation was in November 1999 when Ofgem set out its initial proposals and met with industry and consumer representatives to discuss these. The second consultation was in February 2000. Since February, Ofgem has met with licence holders and consumer groups and discussed the detail of the standard licence conditions. Ofgem received thirty three responses to this consultation. Ofgem has received comments from licensees, consumer representatives and other interested parties and made appropriate amendments to the standard licence conditions. Respondents' views are summarised by issue in the following chapters.
- 2.2 In the previous consultations, Ofgem explained how the proposals would affect the existing licensing regime and, in particular, how the licences would be structured. Ofgem's general approach is that all conditions appropriate for all licensees of a particular type should be standard conditions. Some licensees will require amended standards where part of a condition needs to be revised to apply to the individual circumstances of the licensee in question, eg, some standard conditions need to be revised in part for the two Scottish companies in respect of their distribution and supply licences. Special conditions, such as price controls, are likely only to be necessary for some licensees to provide further regulatory protection or to promote competition.
- 2.3 There will be a single set of standard conditions for each type of licence. These standard conditions will be divided into groups. Not all groups of standard conditions will necessarily apply to all licensees. The licences are structured around the key activities they govern by means of grouping together all of the standard conditions that relate to these key activities. Where appropriate, therefore, the draft licences group together standard conditions with respect to those that apply to all licensees and which are common across all licence types eg the licence fees condition (Section A), those that apply to all licensees of a particular licence type (Section B), those that apply to the domestic customer sector (Section C in supply), and those obligations falling on the

dominant licensees (Section D in supply and Section C in distribution/transportation). The generation licence has Sections that are appropriate to companies generating in Scotland and those involved in nuclear generation. The transmission licence has Sections that contain conditions which are only appropriate to transmission licence holders operating in England and Wales or Scotland respectively.

- 2.4 On granting a licence, it is intended that the Authority will have the power to issue a direction applying particular groups of standard conditions to each licensee. So, for example, a supplier intending to supply only in the industrial and commercial market would not have the group of standard conditions relating to domestic customers applied. It is generally intended that this power will be limited to applying, disapplying or reapplying groups of standard conditions. However, the Authority retains the flexibility to use this power in respect of individual conditions within the groups.

Utilities Act 2000

- 2.5 The Utilities Bill was introduced in Parliament on 20 January and published on 21 January. The proposals will have a significant impact on both gas and electricity licences as explained in Chapter 1. The provisions in the Bill were amended as it completed its passage through Parliament. The Utilities Act received Royal Assent on 28 July 2000.
- 2.6 Ofgem had published the earlier draft standard licence conditions without having seen all of the provisions in the Bill and so a number of assumptions had to be made. In addition, policy intentions in respect of associated secondary legislation had yet to be published. Since the Act received Royal Assent, Ofgem has reviewed the provisions in the Act and made appropriate changes to the draft licences in addition to changes made as a result of consultation.

3. Structure of licences

Definitions and interpretation

- 3.1 Condition 1 in all the draft licences contains the definitions of terms used in the licences and interpretation provisions. The February drafts used the existing licence provisions with the PES licence providing the basis for the electricity distribution and supply condition 1. Definitions were included in this condition, in conditions within which they are used and at the beginning of the Sections in which they were used.

Respondents' views

- 3.2 Industry respondents felt that the definitions could be treated in one way rather than the three outlined above. They were also concerned about how collective licence modification would work for definitions that were in conditions or Sections that might only apply to certain licensees, for example, the domestic supply Section.

Ofgem's views

- 3.3 Ofgem has reviewed the treatment of definitions in all the licences to aid clarity of interpretation and to ensure consistency. To address concerns about the application of the collective licence modification procedures, Ofgem has reordered and redrafted the paragraphs so that the definitions appear first. Definitions contained in other conditions or Sections are cross referred to in condition 1. The interpretation provisions follow the definitions with a paragraph being added which addresses the amendment of a definition contained in a condition or Section of a licence which is not switched on for all licensees.

Revocation provisions

- 3.4 Ofgem proposed in its February consultation on standard licences that the revocation provisions become a standard licence condition. This would enable Ofgem to reflect changes in existing legislation, to accommodate changes in the future and to align gas and electricity in respect of revocation for supplier default.

Respondents' views

3.5 Industry respondents expressed concern about the proposed change. Their main concerns were that there would be an increase in regulatory risk and uncertainty for the licensees, which might affect their financial arrangements, and that the revocation provisions would be subject to change by collective licence modification without an individual licensee's consent or recourse of appeal to the Competition Commission. The industry's preference was for the revocation provisions to remain a term of the licence, not a condition.

Ofgem's views

3.6 Ofgem has acknowledged the strong concerns expressed by licensees. The Licensing Scheme provisions in Schedule 7 to the Act were amended to allow the Secretary of State to make such "amendments relating to the revocation of the licence as the Secretary of State thinks fit". The revocation provisions will therefore remain as a term of the licence, thereby reducing uncertainty. However, there will be several changes to these provisions. They have been updated in respect of legislation references with an interpretation clause being added to allow for future changes to legislation to be incorporated automatically. They have also been amended to facilitate the introduction of Supplier of Last Resort in electricity, the introduction of financial penalties, and alignment, in the following areas:

- updating the references to the Competition Act;
- aligning the timescale for notice of revocation to not less than 24 hours when the licensee is unable to pay its debts;
- aligning as to the minimum sum in relation to the debt threshold for insolvency purposes (£100,000 for all licensees except Transco and NGC for which the sum will be £250,000);
- providing for revocation in the case of non-payment of financial penalties;
- aligning the period within which a licensee must start its licensed activity and the period when the licensee has ceased to carry out its licensed activity; and
- aligning as to revocation if the licensee is convicted of committing an offence under section 43 of the Gas Act/59 of the Electricity Act.

Application conditions

- 3.7 The application conditions provide a mechanism for the Authority to apply, disapply or reapply the activities set out in the Sections of the licences by issuing directions. As the application conditions were drafted in the February versions, such a direction:
- would be capable of switching on or off groups of conditions or individual conditions within the relevant section;
 - might specify 'such other matters as the Authority thinks fit';
 - might specify the area within which the conditions are to apply;
 - did not require the licence holder's consent in order for it to be issued; and
 - was capable of being revoked or varied without the licensee's consent.
- 3.8 Ofgem's aim was to provide the Authority with flexibility to allow the licence to be adapted to reflect changes in the licensee's circumstances and the market. Sections D and C in supply and distribution/transportation respectively are to be switched on for all ex-PESs, BGT and Transco in the first instance.

Respondents' views

- 3.9 Industry was opposed to the application conditions in the above form and claimed that regulatory risk would increase as a result. Companies expressed the following concerns:
- the application conditions afforded the Authority wide discretionary powers, especially the clause 'such other matters as the Authority thinks fit' - the Authority might use this power to introduce additional distribution or supply obligations without consulting on these;
 - the Authority could use these powers for punitive purposes rather than following enforcement procedures. For example, if the licensee was in breach of its domestic supply obligations, the industry was concerned that the Authority might switch off this Section of the licence;
 - the Authority did not have to obtain the licensee's consent to issue, vary or revoke a direction;
 - there was no right of appeal against the issue, revocation or variation of a direction except by Judicial Review;

- these conditions would be subject to change by collective licence modification without an individual licensee's consent or recourse of appeal to the Competition Commission; and
- there were no criteria setting out how the application conditions would be used.

Ofgem's views

3.10 Ofgem has acknowledged the concerns raised by licensees. It has therefore agreed that Sections should be switched on or off with consent and that the drafting "such other matters as the Authority thinks fit" should be removed. Ofgem has retained the flexibility to apply all or some of the conditions in the relevant Section, however, all appropriate sections will be switched on automatically for the ex-PES licensees, BGT and Transco when the standard licence conditions come into force without initially being subject to consent.

3.11 The application conditions will be modified by licence type should the collective modification procedure be invoked, but it is for the Authority to propose modifications.

Licence Fees

3.9 In earlier consultations, Ofgem proposed that the licence fee conditions should be aligned between gas and electricity with the method of apportionment being set out in a subordinate document. The licence fee cap in gas will be removed following the government's stated policy (paragraph 17, DTI's October 1999 paper).

Respondents' views

3.10 Several industry respondents were concerned about the increase in the costs of regulation and requested a cap on Ofgem's costs. More specifically, it was suggested that Ofgem should be subject to a form of RPI-X control with exceptional costs being agreed by the Secretary of State, and that costs should be contestable. Four called for Ofgem to have clear, auditable and transparent efficiency incentives. There were also requests that the principles for allocation of costs were consulted on and that any subsequent variation to the principles be consulted on too. Two respondents would prefer that the principles for allocation be set out in the licence to give more certainty

and enable the licensee to better plan and budget. Advance notification of fees was also requested. One licensee welcomed the facility to make payment in instalments.

Ofgem's views

3.11 Ofgem is aware of licensees' concerns about the costs of regulation. Ofgem will be consulting separately on the changes that need to be made to the existing licence fee arrangements following the Utilities Act 2000. This separate consultation will set out in more detail the financial controls to which Ofgem, as a non-ministerial government department is subject. It also explains the new "efficiency regime" to which Ofgem will be subject and the consultation Ofgem now undertakes on its forward workplan and budget. The consultation also seeks views on the methodology for apportioning costs between licence holders.

Duplication with the Utilities Act

3.12 The February versions of the draft licences included several obligations which reflected government policy but on which Ofgem had not seen the detailed drafting of the Utilities Act. These included:

- a requirement to facilitate competition in the generation and supply of electricity in the distribution licence;
- provision of information to the Consumer Council in all licences; and
- the transfer of licence in all licences.

Respondents' views

3.13 Industry respondents pointed out that these provisions duplicated those in the 2000 Act and that therefore they were not necessary.

Ofgem's views

3.14 Since the Act received Royal Assent, Ofgem has carried out a review of obligations to avoid duplication. As a result of this review, the above conditions have been deleted from all licences in which they appeared.

Scotland

- 3.15 Ofgem proposed Great Britain wide, licences but stated in its February consultation that the detail of the standard licence conditions in relation to Scotland would need to be revised or added to to accommodate the horizontally and vertically integrated Scottish companies.

Respondents' views

- 3.16 Industry respondents highlighted some areas, for example, definition of "Transmission Business", where different versions were needed for England and Wales and Scotland.

Ofgem's views

- 3.17 Whilst pursuing the policy of Great Britain wide licences, Ofgem recognises that there are different trading and structural arrangements in Scotland. Ofgem has revised the conditions where necessary to ensure that those relating to England and Wales and Scotland are in separate Sections of the licence or drafted in such a way that they apply to the licensee depending on where they are operating, for example, the Generation Security Standard in electricity supply which will apply only in Scotland when NETA goes live. However, the transmission licence has seen most change in this respect. Further detail is given in Chapter 9. In addition, some conditions will become supplementary or amended standards for the two Scottish transmission companies in that parts of the conditions need to be revised to recognise the individual circumstances that apply. For instance, the existing condition relating to the Scottish Settlement Agreement in the Scottish composite licences will be included as an amended standard via the Licensing Scheme.

4. Customer protection issues

Categories of gas and electricity customers who should continue to benefit from certain regulatory safeguards

- 4.1 Ofgem published the February versions of the draft standard licence conditions on the understanding that a Statutory Instrument would define the group of customers who would benefit from additional regulatory protection. The supply licences were structured in such a way that these additional obligations would be switched on for suppliers to this group of customers. The term “designated” was used to describe this group. Since then, it has been decided that a statutory instrument was not required and that such a group of customers could be defined through the licences.
- 4.2 The additional regulatory safeguards presently apply to different groups of customers in gas and electricity. In gas, “domestic customers” receive these additional safeguards whilst in electricity the additional safeguards apply to “designated customers”.
- 4.3 A “domestic customer” in gas is defined in section 15A(10) of the Gas Act 1986 as a person who is supplied by a gas supplier with gas conveyed to particular premises at a rate which is reasonably expected not to exceed 2,500 therms (73,200 kWh) per year. This existing definition of a ‘domestic customer’ in relation to gas has been removed from the Gas Act 1986 by the Utilities Act 2000.
- 4.4 A “designated customer” in electricity is defined in the licences as including all those resident in premises used wholly or mainly for domestic purposes, plus business customers expected to use less than 12,000 kWh per year.
- 4.5 The additional regulatory safeguards provided are:
- the duty to offer terms to supply and to provide the customer with a supply on those terms, if requested;
 - the terms of contracts, e.g. payment methods and the right to terminate with 28 days notice;

- the setting of a maximum resale prices for gas and electricity (this safeguard currently applies to all gas customers);
- the requirement to prepare and provide codes of practice on: payment of bills; the use of pre-payment meters; services for the disabled; complaint handling; energy efficiency advice; and site access;
- the application of some prescribed standards of performance; and
- the provision of a bond to ensure that small customers are not required to meet the full cost of any supplier of last resort arrangements should their gas or electricity supplier fail.

4.6 In July 2000⁹ Ofgem consulted on whether the gas and electricity definitions should be the same and what that definition should be. We proposed that the current definitions be replaced with a single definition for gas and electricity of “a customer who occupies premises used wholly or mainly for domestic purposes”.

4.7 The consultation document also invited views on whether maximum resale prices for gas and electricity should be set for all customers or should be limited to a category of customers. At present, maximum resale prices are set in gas for all customers and in electricity for “designated customers”. The current electricity arrangements require an actual price to be fixed through a determination. These prices vary across the regions as they are tied to the local PES tariff and must be amended each time the tariff changes. The current arrangements in gas are that the maximum resale price is related to the cost paid by the landlord. The current electricity arrangements have to be replaced due to the abolition of the PESs and their tariffs. The Utilities Act 2000 has copied the current gas provisions into electricity and therefore the maximum resale price in both gas and electricity could be tied to the landlord’s costs.

Respondents’ views

4.8 A summary of the responses received is given in Appendix 1. The majority favoured both gas and electricity having the same definition. They agreed with Ofgem’s views that it was appropriate to align as a result of the Utilities Act and the increasing convergence between gas and electricity, that it seemed sensible to have a common

⁹ Categories of gas and electricity customers who should continue to benefit from certain regulatory standards, July 2000

definition in a dual-fuel market, and accepted that regulatory protection should focus on those customers most in need of it. However, some consumer representatives and trade associations representing small business stressed the value of additional protection for small businesses. A handful of respondents stated that implementation within the proposed timescale of early 2001 would not be possible. This view is not supported by gas transporters, on whom it is widely acknowledged that the majority of any changes will fall.

Ofgem's views

- 4.9 The responses to the consultation are generally supportive of the move towards a single definition of "small customers" as "customers occupying premises used wholly or mainly for domestic purposes". We consider that in the majority of cases the domestic definition proposed in the paper is the right way forward, with the possible exceptions of energy efficiency and site access codes of practice and the maximum resale price.
- 4.10 It seems sensible, as in the past, to restrict certain types of protection to domestic customers. Standard licence conditions dealing with those safeguards applying only to domestic customers are contained in Section C of the new gas and electricity supply licences. Those sections will be effective only for suppliers whose business includes supply to domestic customers. Ofgem considers, however, that there are particular safeguards that should extend to all customers. The standard licence conditions applying to these wider safeguards are contained in Section B of the supply licences and will be effective for all suppliers.
- 4.11 Whilst it is clear that small businesses may, in many respects, be better placed to operate effectively in a competitive environment than are domestic customers, the arguments of these organisations have some force. Ofgem therefore proposes that codes of practice on site access and energy efficiency should be of universal application. The conditions have been moved to Section B of the supply licences accordingly.
- 4.12 Because of the separate licensing of electricity distribution and supply, the Utilities Act 2000 includes new provisions governing rights of entry by licensed suppliers, distributors and their agents. It is important that all customers should have confidence that these new access provisions will be fairly and reasonably interpreted. The site

access code will have an important role to play here for both domestic and non-domestic customers. It will allow the regulator to intervene early, to prevent abuse. The conditions about site access have been moved to Section B of the gas and electricity supply licences where they will apply to all suppliers.

- 4.13 Universal application of the energy efficiency code may be equally beneficial for small businesses as it has been for householders. Moreover, Ofgem is committed both to contributing to achievement of the UK's declared environmental targets and to helping customers to reduce their expenditure on energy. Basic energy efficiency advice still has a significant role to play on both counts, and the energy efficiency code of practice is an established instrument for furthering those goals. Again, the related conditions have been moved to the relevant licence Sections where they will apply to all suppliers.
- 4.14 Further to paragraphs 4.12 and 4.13, the provisions in supply, with regard to the licensee recording and reporting on their performance, and preparing and reviewing their codes of practice, have also been moved to Section B. This is to ensure that the above two obligations are included. The conditions have been redrafted so that the obligations which are captured, but which continue to apply only to domestic suppliers, for example, complaint handling procedures, do not "bite" on any non-domestic suppliers.
- 4.15 Ofgem has also now amended the licences so that they refer to domestic customers where appropriate instead of designated. The condition in supply which deals with domestic premises has also been revised. It now allows for domestic premises to be included in multi-site contracts with non-domestic premises where the domestic premises is on the same site as a non-domestic premises, for example, a caretaker's flat in an office block. The condition also allows for customers who will now fall under the definition of domestic (when the new standard licences come into force), but who are currently on contracts with non-domestic suppliers, to continue to be supplied under their existing contracts until they change supplier. This prevents the supplier being in breach of its licence if it allows supply to non-domestic customers only. Finally, the condition allows for unanticipated changes in the use of premises, for instance, warehouse to domestic living accommodation. Again, the latter is so that the supplier is not in breach of its licence.

4.16 Obligations have been included in the gas licences to ensure that information relating to whether a property is domestic or not is passed on appropriately, from gas suppliers through shippers to transporters. Ofgem is in discussion with Transco about the modification required to its Supply Point Administration system, so that sites can be identified as domestic.

Social Action Plan

4.17 The February draft of the standard licence conditions consultation included in the draft gas and electricity supply licences the proposals published by Ofgem in its document "Social Action Plan: Enhancing Social Obligations – A Proposals Document", January 2000. The February draft of the electricity distribution and gas transportation licences included Ofgem's proposals, at that time, for the split (and alignment between fuels) of these conditions. These proposals were based on the supplier hub principle, that is, on the expectation that suppliers would act as a one-stop-shop for customers and, therefore, most communication between domestic customers and distributors/transporters would be facilitated through suppliers. The drafts were also based on proposals that had not yet been finalised or voted on.

Respondents' views

4.18 A number of respondents believed that the condition, "Provision of Services for Persons who are of Pensionable Age or Disabled or Chronically Sick", in the electricity supply and distribution licences should be amended to better reflect specific characteristics of the Priority Service Register. For example, in electricity, some customers with medical conditions are connected to life support machines that need a continuous supply of electricity. These customers need advance notice of planned interruptions to the supply, as well as immediate information in the case of an unplanned interruption. It was suggested that, in this case, distributors should contact these customers directly.

4.19 A number of respondents proposed that the condition relating to the preparation and review of customer service codes in the electricity distribution and gas transportation licences should be amended to explain how licensees notify customers as to the existence of statements or codes, as distributors and transporters will not have direct contact with customers on a frequent basis. One consumer respondent believed that the

condition relating to the provision of services for the blind or deaf should be included in the electricity distribution and gas transportation licences.

- 4.20 Consumer representatives provided many comments on all the social obligations in the licences. Specifically, a customer agency respondent has requested that Ofgem should clearly define the kind of information they will require from licensees for the purposes of monitoring compliance. It believed the statistical information provided by the supplier or distributor/transporter should be published. It was also suggested that the information required should be more detailed, to offer a greater insight into activity in areas such as prepayment metering, disconnections and percentage of meters read by suppliers.
- 4.21 Various respondents suggested minor drafting changes to clarify the extent of the obligations.
- 4.22 A consumer agency stressed the need for suppliers to move from debt management to debt prevention, but pointed out that the condition does not suggest that this move has been made. They also felt that disconnection should be used as a last resort and better arrangements should be put in place to deal with customers after disconnection has occurred. In addition they suggested a cap on debt recovery and that there should be an obligation on suppliers to refer customers to independent debt counselling.
- 4.23 One consumer respondent believed that the condition relating to pensioners not having their gas supply cut off in winter should be changed so that it refers to all pensioners and not just to those who the licensee believes cannot pay (as opposed to won't pay). Another respondent suggested that this condition should be introduced in the electricity supply licence as part of the alignment between gas and electricity provisions.

Ofgem's views

- 4.24 The licence amendments proposed in the Social Action Plan have now been incorporated into existing licences. The October final draft licences reflect the changes agreed as part of the Social Action Plan consultation as they appear in the document "Enhancing Social Obligations – Decision Document" published in May 2000. Ofgem has reviewed the agreed Social Action Plan conditions in order to split the obligations appropriately between supply and distribution/transportation.

- 4.25 Ofgem has considered all the comments received as part of its work on the Social Action Plan. This work is ongoing and forms an important element of Ofgem's workplan, particularly with regard to the Authority's new principal objective. Many of the suggestions received had merit, however, they did not follow either from the Utilities Act directly or from the policy pursuant to that Act. That policy is to align the provisions between gas and electricity as far as practicable.
- 4.26 Ofgem has amended the conditions to take into account several comments made by respondents to the February consultation on the standard licence conditions which do fall out of the government policy of alignment wherever practicable. Some minor drafting changes clarify the extent of the obligations, as proposed by respondents, and improve the alignment of the conditions.
- 4.27 Ofgem agrees that there are circumstances, as noted above, in which the distributor will need to contact some customers directly, as well as circumstances in which the customer, or someone on his behalf, might need to contact the distributor directly to ensure that a customer is included in the Priority Service Register. The draft conditions have been amended to allow for this. As a consequential change, an obligation has been placed on suppliers and distributors to keep each other updated about the information in the Priority Service Register. Also, due to the urgency of communicating with some customers on the register, an obligation has been placed on the distributor to contact the supplier with the information as soon as practicable (where the distributor passes on the information through the supplier) and on the supplier to seek that information as soon as is practicable. This condition has not been amended in the gas licences, as there is not the same urgency or likelihood in gas in relation to customers relying on life support machines.
- 4.28 Ofgem recognises that there are circumstances in which a customer will contact the distributor/transporter directly. This applies in such cases as the Priority Service Register, asking for a connection (if this is not done through the supplier) or making a complaint. Ofgem has therefore introduced in the electricity distribution and gas transporters licence the condition, "Provision of Services for Persons who are Blind or Deaf". This is to facilitate effective means of communication between such customers and the network operators.

- 4.29 Ofgem accepts the views of respondents in respect of what type of notification distributors or transporters should have to give customers as to the statements or codes produced by distributors and transporters, and has amended the conditions so that the obligation refers to them giving publicity that they consider to be adequate.
- 4.30 Ofgem has set up a working group comprising consumer and supplier representatives to decide on and monitor the information required against the Codes of Practice.

Standards of performance

- 4.31 Ofgem intends that there should be an obligation on transportation and distribution licensees to pass on compensation payments in relation to guaranteed standards to shippers/suppliers and corresponding obligations for suppliers to make payments to customers. The obligation on transporters to establish standards of performance was included in the February transportation draft licence whilst a provisional condition was included in distribution. These obligations were subject to the detail contained in the Utilities Act.

Respondents' views

- 4.32 Several industry respondents felt that the conditions should be deleted to prevent duplication with the 2000 Act and/or the Regulations giving the Authority the power/duty to prescribe on standards of performance (see sections 54 and 55 and 90 and 91 of the Utilities Act 2000 with regard to electricity and gas respectively).
- 4.33 One industry respondent was concerned that no provision had been made for the costs incurred by suppliers when dealing with customer queries and handling compensation claims. They felt that these costs should be borne by the party responsible for the standards failure, ie the distributor or transporter and that a provision should be inserted in the distribution and transportation licences allowing the recovery of costs by shippers/suppliers which would also encourage those licensees to improve their standards of service.
- 4.34 Two consumer agencies were concerned that the obligation sets no time limit within which payments should be made to customers. They argued that the supplier should make the payment to the customer within 10 working days irrespective of whether the

distributor or transporter has made the compensation payment to the supplier. They also considered that the condition might include a period for the distributor or transporter to pay the supplier/shipper.

- 4.35 One consumer body thought that when Ofgem next exercises its power to set new standards of performance, such standards, including timescales, should be set by statutory instrument. Another felt that there is no reason why compensation payments should be restricted to domestic customers, as the draft February licences indicated.

Ofgem's views

- 4.36 Ofgem is consulting separately on standards of performance¹⁰ and what might be appropriate for both the competitive market and monopoly networks. Until that consultation is concluded, Ofgem proposes that there should be a standard condition on distribution/transportation which contains the obligation to pass on any compensation payments to shipper/suppliers and a corresponding obligation on suppliers/shippers to pass on any compensation payments received from distributors or transporters to customers. Ofgem's present view on timescales for making payment to customers is that the proposed requirement to make such payment to customers "as soon as reasonably practicable after its receipt by the licensee..." is preferable. A stipulated timescale has some attraction in that it ensures the customer receives compensation within a set deadline, but could present cash-flow problems for a small supplier where the distributor or shipper has not made payment in the timescale required. In the separate consultation on Standards of Performance, Ofgem will consider what monitoring will be required and where such an obligation might lie. It will also consider what provision, if any, might be made for any costs incurred by suppliers dealing with customer queries and handling compensation claims on behalf of other parties responsible for the failure to meet the standard.

Deemed contracts

- 4.37 Ofgem originally proposed that the obligations regarding deemed contracts should apply to those suppliers who are supplying domestic customers only. As part of our policy on

¹⁰ Guaranteed and overall standards of performance, a consultation paper, October 2000

alignment, in the electricity supply licence, Ofgem mirrored the existing obligations in gas as far as possible. Again, this proposal was subject to the detail in the Utilities Act.

Respondents' views

4.38 There was widespread support for the introduction of deemed contracts into electricity although some respondents wanted this facility to apply to all groups of customer. One respondent was opposed to the removal of the ability to elect to have deemed contracts in gas for larger customers.

Ofgem's views

4.39 The Utilities Act imposes an obligation on all suppliers, regardless of which customers they serve, to produce a deemed contract scheme. The standard licence condition has been revised accordingly and will now be in section B of the licence which applies to all suppliers.

Supplier of Last Resort

4.40 Ofgem had included proposals in electricity for the appointment of a Supplier of Last Resort (SOLR) for domestic customers, the security arrangements required for domestic suppliers, and the arrangements for a levy to cover payment claims for excess costs. These proposals mirrored the existing arrangements in gas. A SOLR can be appointed to take over the supply of energy to customers if their existing supplier fails. Ofgem recognises that such an obligation may prove burdensome for suppliers in that there will be additional costs in, for example, having to contact these customers, attempt to read their meters, and purchase additional energy to ensure there is sufficient for supply to these customers. Therefore, the provisions sought to ensure that where a supplier is appointed as SOLR, they have certain options available to ensure that they can maintain supply to the customers affected as well as their own customers. Domestic suppliers would be able to recover any excess and unrecoverable costs from a bond that all domestic suppliers must take out. If this bond proved to be insufficient to meet their excess costs, they could submit claims to transporters/distributors to be financed by a levy. The levy would be derived from transporters/distributors raising their use of system

charges in the following year. The cost of the levy, if any was required, would be spread amongst customers.

- 4.41 In the supply licence, conditions set out the obligations and provisions for deemed contracts as explained in paragraph 4.35 above, the security arrangements required for domestic suppliers, and the appointment of a SOLR. In the distribution licence, the arrangements for a levy to cover payment claims for excess costs were set out, again, mirroring the arrangements in transportation.

Respondents' views

- 4.42 There was support for the inclusion of provisions relating to SOLR in electricity but electricity industry respondents believed that there was a need to consult further on these provisions. One respondent was concerned about how the provisions in both gas and electricity would work in practice and suggested that the network operator be responsible for transferring the data regarding the affected customers between the old supplier and the SOLR so that the data is provided in a common format.
- 4.43 PESs suggested that the Authority should determine the amount of the payment claim before the supplier passes this to the network operator and that the Authority should not be able to notify a SOLR in advance of the failed supplier's licence being revoked. Other respondents also believed that the Authority should validate payment claims for excess costs before these are sent to the distributor/transporter.
- 4.44 PESs and another industry respondent suggested that the Authority should have to consult on the establishment of the principles for calculating the sum for security and not just on any variation to these principles. One company was concerned that smaller companies should not be disadvantaged by the additional costs of new security arrangements. There was a suggestion that these provisions should be aligned between gas and electricity.
- 4.45 PESs suggested that the distributor/transporter's right to elect the accuracy of their estimate of how much they need to increase their distribution/transportation charges be removed as it was not necessary and was unduly complicated.

- 4.46 One respondent has suggested that the Authority should direct distributors to make payments and that the timescale for increasing charges should be reconciled to the notice period for changes set out in condition 5 of the distribution licence (Basis of Charges for Use of System and Connection to System: Requirements for Transparency). Another advised that system changes would be required in order for distributors/transporters to differentiate between domestic and non-domestic customers.

Ofgem's views

- 4.47 Ofgem has reviewed the proposed conditions and redrafted them in the light of responses and the provisions in the 2000 Act. For example, the Act permits deemed contracts for all customers and so requires all suppliers to submit a deemed contract scheme. The condition relating to the appointment of a SOLR has been moved to Section B in supply where it applies to all suppliers, but the condition relating to security arrangements remains in the Section that will be switched on for domestic suppliers only.
- 4.48 Ofgem is of the view that it is likely that a number of suppliers would see commercial benefit in taking on the customers of a failed supplier without having to market and so would be willing to take on customer portfolios. Indeed Ofgem is likely to encourage a market solution. However, the Authority should be able to direct a supplier to be a SOLR for both domestic and non-domestic customers in circumstances where there was no market solution. Ofgem will be consulting separately on the principles behind any such direction and on the practical details of such an arrangement.
- 4.49 A direction to appoint a SOLR (or several) would be subject to the tests used in the gas licence as to whether the appointment would "significantly prejudice" the supplier's ability to supply his own customers and fulfil contractual obligations for the supply of energy. This would remain a judgement taken by the Authority.
- 4.50 The Authority should be able to notify, in advance, a SOLR where circumstances have arisen which would entitle the Authority to revoke the other supplier's licence. This appointment of a SOLR can only be effective where the licence of the first supplier has been revoked. It should be possible to split the portfolio of the failed supplier and appoint more than one SOLR.

- 4.51 Domestic customers will have additional protection concerning hardship relating to the terms offered by the SOLR under deemed contract. In other words, deemed contract prices can be varied/capped if the Authority determines that they might cause hardship. Deemed contract prices to non-domestic customers supplied by a SOLR will not be capped in this way.
- 4.52 There will be a requirement to maintain a bond on suppliers who supply to domestic customers only. This bond would provide funds for the unrecoverable costs faced by the SOLR where the deemed contract prices are not sufficient. The Authority would set a cap on the bond. This cap is set out in the condition. The bond should be set at such a level that it does not become a barrier to entry. Because of the increased certainty with regard to the maximum cost of these security arrangements, Ofgem does not propose to build in a process for consultation in the initial determination of the principles for setting the bond. However, there is such a process should Ofgem seek to vary the principles.
- 4.53 There will be levy arrangements for any additional excess costs where the bond proves to be insufficient. There should also be the possibility of levy arrangements for suppliers who supply to non-domestic customers where the amount charged to these customers under deemed contract proves to be insufficient to recover excess costs.
- 4.54 The levy will be recoverable via distributors and transporters on a de minimis level and will be recovered from all customers if used. There is a "de minimis" principle already applied in the electricity licence because of the way "Relevant Licensed Distributor" is defined to mean only those distributors with a distribution services area. This principle has been copied across to gas. The levy in effect only applies to those distributors/transporters who have Section C switched on. The condition relating to the levy has accordingly been moved to Section C in the distribution/transportation licences. However, a SOLR may wish to waive their right to make a claim for costs via the levy.
- 4.55 Where the SOLR is claiming against the levy, there will need to be a test for what can be claimed against the levy and what cannot. The right to elect to treat the estimate of how much the distributor/transporter needs to increase charges as accurate (the actual amount) is to be removed to make for more clarity. The Authority will determine the amount of the payment claim against the levy before the supplier sends it to the

distributors/transporters. This could mean a delay in the supplier receiving payment but would make for more clarity in drafting and simplicity in the setting of increased distribution/transportation charges

- 4.56 Revenue raised via the levy is to be treated as excluded service revenue with any over recovery to be returned via a direction from the Authority. This fits in with the existing price control regime, audit requirements and Ofgem's powers to issue directions regarding treatment of certain price control revenue.

Liaison with Gas and Electricity Consumer Council

- 4.57 In the February versions of the standard licence conditions, Ofgem proposed a new condition concerning licensees' obligations to provide information to the Gas and Electricity Consumer Council (GECC).
- 4.58 Other obligations required licence holders to liaise with the GECC in respect of Codes of Practice.

Respondents' views

- 4.59 The majority of industry respondents confirmed that they did not see the need for a licence obligation to provide information to the GECC, given the new Consumer Council's powers. Consumer groups suggested that annual meetings between the new energy Consumer Council and the suppliers should be made a requirement.
- 4.60 There was some concern that the Consumer Council would not be able to instigate a review of a Code of Practice. It was suggested that, as the Consumer Council will be charged with a role in reviewing the Codes of Practice, there may be a need for it to be able to do so.

Ofgem's views

- 4.61 The Utilities Act provides the GECC with broad information gathering powers. Ofgem believes these powers are sufficiently broad to obviate the need for stipulating that an annual meeting must be held, as the GECC can request information and may choose to

do so via the medium of a meeting. Likewise, Ofgem considers that reviews of Codes of Practice should continue to be requested by the Authority. The Consumer Council could, at any time, request the Authority to instigate a review of Codes of Practice.

- 4.62 The Utilities Act makes the provision of information to the GECC a relevant requirement so that enforcement action could be taken if the licensee refused to provide any information which is not subject to the exclusions to be set out in a Statutory Instrument. As such, the condition about the provision of information to the Consumer Council is no longer necessary and has been deleted from all licences.

Complaint handling procedures

- 4.63 An obligation in each of the supply and distribution/transportation draft licences required the licensees to submit a code of practice on complaint handling. Such an obligation was new for gas licensees but not for electricity licence holders and was included in gas licences as part of the process of alignment.

Respondents' views

- 4.64 With regard to complaint handling procedures, it was proposed that, although the condition (under the Code of Practice) offers a flexible timescale to deal with complex complaints, there should be some stipulation as to a maximum length of time to deal with these. One respondent suggested a system similar to the water industry whereby an allowance can be made for complex complaints which may take longer to resolve than the suggested limit.
- 4.65 One respondent proposed that transporter complaint handling procedures could be audited by the GECC on a regular basis by taking a random sample. It was suggested that this has proved useful for providing feedback to companies.
- 4.66 It was further suggested that it would be difficult for a transporter to differentiate between a domestic and non-domestic customer. Moreover, the transporter is seldom contacted directly by the customer (usually through the shippers and suppliers etc). Consequently, it was proposed that the code should not be limited to domestic customers and should be extended to all customers.

Ofgem's views

4.67 Ofgem considers that domestic customers should continue to receive the certainty and protection afforded by the code of practice on complaint handling. The code will ensure such customers are fully informed about how any complaint should be handled. It will set out avenues of appeal and will also be a useful vehicle for publicising the complaint handling role of the new GECC. Ofgem does not consider it necessary for any complaint handling information to be audited. The GECC will have broad powers to obtain information as explained above and would be able to request information in order to verify figures subject to the exclusions set out in the DTI's paper, "Provision of Information to the Gas and Electricity Consumer Council: Response to Consultation", published this month.

Safety and security of supply

4.68 These conditions include: "Transmission system Security Standard and Quality of Service" in the transmission licence, "Obligations as Respects Emergencies" in the gas shippers' licence, "Security and Emergency Arrangements" in the gas supply licence, "Safety and Security of Supplies Enquiry Service" in the electricity distribution licence and "Emergency Services and Enquiry Service Obligations" in the gas transporters licence.

4.69 Ofgem suggested, in its February draft, the alignment of the condition regarding the enquiry service in the electricity distribution licence and the gas transportation licence.

Respondents' views

4.70 A number of respondents suggested further alignment between the obligations in these conditions.

4.71 One licensee suggested that the Safety and Security of Supplies Enquiry Service condition in the electricity distribution licence should provide for the use of an agent. It was also suggested that the wording "in or around the area" to which the condition refers was too vague.

- 4.72 One licensee pointed out that paragraphs 6 to 11 of the condition “Transmission System Security Standard and Quality of Service” were specific to the Scottish licences. Consumer representatives believed that suppliers should be aware of, and publicise special facilities for deaf and hearing impaired people. They felt it was not sufficient for suppliers to publicise the telephone number on or with each bill, as blind or partially sighted customers might not be able to access the service. With specific regard to gas, one licensee pointed out that paragraphs 1 and 2 in condition 7 in transportation might conflict with the Gas Safety (Management) Regulations.
- 4.73 A number of proposals were made that, whilst they may have merit, do not fall within the remit of the Utilities Act. Either there is no provision in the Act with which they could be associated or they do not follow the policy objective which is alignment where appropriate. These proposals included: the introduction of a national, integrated enquiry service for electricity distribution with a single number; the introduction of a checklist of likely causes of problems to be given to customers to reduce the number of calls; placing an obligation on distribution businesses to provide unplanned outage information to all suppliers automatically to assist them in demand balancing and forecasting; the costs of the single gas emergency call centre being borne by BG Transco plc and recovered via their allowable transportation revenue; the leakage of carbon monoxide or suspected leakage of carbon monoxide being included in the gas licence obligations; Ofgem giving guidance on carbon monoxide identification; the priority in dealing with gas escapes to be to make safe an escape of gas, and not to limit this by time or cost.
- 4.74 A licensee proposed alternative wording to make clear the scope of the service in gas. They felt that any matter or incident that affects the maintenance of the security, availability and quality of service is an emergency, due to the danger inherent in the fuel usage.

Ofgem’s views

- 4.75 The proposed standard condition in transportation has been amended to provide for the use of an agent, as is the case in the existing condition, although BG Transco plc will keep its special condition unamended (that is, it will not provide for the use of an agent). Ofgem has amended the distribution licence to allow for the use of an agent, for

alignment with the gas transporters licence. It has also amended the wording of "in or around the area" to make clear the limit of the conditions.

- 4.76 Ofgem has deleted paragraphs 6 to 11 from the condition that applies to all transmitters. These paragraphs will be in a special condition for the two Scottish companies in respect of their transmission licences.
- 4.77 Ofgem has deleted paragraphs 1 and 2 in condition 7 in gas transportation, to avoid conflict with the Gas Safety (Management) Regulations and has deleted other provisions to avoid duplication with the duties of the Health and Safety Executive. Ofgem has included the modifications agreed in a separate consultation on the Priority Gas Customer list.
- 4.78 Again, due to the safety considerations of gas, references to the address of the emergency service have been deleted, as the telephone number is the most important thing to advise customers of due to the different need for urgency in gas.
- 4.79 The cost limit for the emergency services of £4 has been updated to £4.65, as the condition about the adjustment of amounts by reference to the retail price index to which the amount refers has been updated to reflect the date of the entering into force of the new condition.

Revenue protection

- 4.80 The February draft of the electricity distribution and supply licences included Ofgem's proposals for Revenue Protection. These were based on the existing separated PESs' licences.

Respondents' views

- 4.81 The PESs have expressed in their common response their belief that these conditions should be consulted on, as they affect the treatment of revenue protection. In particular, they believe that the conditions as drafted do not oblige distributors to provide a revenue protection service (although this is a condition of the Distribution Use of System

Agreement). They are concerned about how this affects the Revenue Protection Code of Practice.

4.82 The other main concern expressed by respondents refers to how the obligations between supplier and distributor inter-relate, as they believe the obligations do not provide the same incentives to both parties.

4.83 One company suggested that the condition in the distribution licence should include an obligation to have in place a revenue protection code of practice. It was also suggested that this condition should place an explicit obligation on the distributor to act on the information received from the supplier about suspected meter damage. Respondents also suggested that the supply condition should provide for the licensee to give information to the distributor where the latter suspects a criminal act has taken place and the distributor requests such information.

4.84 Two consumer bodies were concerned that the treatment customers receive now, being disconnected on suspicion of theft and not having the right to a hearing, will contravene the European Human Rights legislation.

Ofgem's views

4.85 Whilst Ofgem has sympathy for the views expressed, it is Ofgem's view that the Utilities Act does not change the treatment of revenue protection. Ofgem is considering proposing licence modifications on this issue in the future, but not as part of the standard licence conditions consultation.

4.86 Ofgem does accept that the information provisions between supplier and distributor need to dovetail, and the October drafts include amendments to this effect.

5. Other general policy issues

New Electricity Trading Arrangements

5.1 The February versions of the electricity licences included policy statements on each of the conditions to be affected or introduced due to the New Electricity Trading Arrangements (NETA).

Respondents' views

5.2 Although respondents replied to the separate consultation on NETA, several also commented on various issues related to NETA in their responses to the previous consultation on the standard licence conditions. The following key issues were raised:

- concerns about the enduring change co-ordination requirement and the obligation to use best endeavours to ensure change to key documents;
- the introduction of a market abuse condition;
- the retention of the generating unit availability condition; and
- the retention of the non-discrimination provisions in electricity sales contracts.

Ofgem's views

5.3 The concerns raised were addressed in the response to the separate consultation on NETA¹¹ and have now been introduced into electricity licences as appropriate, but have not yet been switched on. The conditions have been included in this final draft of the standard licence conditions in such a way that they will apply only when a licensee is operating in England and Wales. The conditions pertinent to NGC are included in the section of the transmission licence that relates only to England and Wales.

Separation of distribution and supply

5.4 Ofgem has consulted separately on two conditions related to the managerial and operational separation of distribution and supply. The February draft of the distribution licence included the versions of these conditions in existence at that time. The existing

¹¹ The New Electricity Trading Arrangements: Proposed licence conditions, Ofgem/DTI conclusions paper, June 2000

provisions from Transco's special conditions were incorporated into transportation following the general policy of alignment wherever practicable. Subsequently, the electricity conditions were amended, agreed, and included in PES licences.

Respondents' views

5.5 Industry respondents expressed concerns about how these conditions work in practice. These respondents also believed that there should be an early review of the separation conditions before derogations given in respect of the conditions expire.

Ofgem's views

5.6 Ofgem recognises the concerns expressed and has agreed to consult on these conditions through the collective licence modification procedure before the first derogations end in March 2002. Due to the timescales, the standard licence conditions will include the separation conditions now included in electricity distribution and the versions that were published in February in gas transportation.

Ring-fencing

5.7 Ofgem included proposed ringfencing modifications in the February versions of the draft licences. A separate consultation on financial ringfencing in distribution was carried out and a decision document was published in April (see Chapter 1).

Respondents' views

5.8 A number of concerns were expressed about the extent of the changes proposed. In particular, some companies were concerned that some of the changes were not a direct result of the Utilities Act. For example, they were concerned by the definition of "Ultimate Controller" which it was proposed would replace "Ultimate Holding Company".

Ofgem's views

- 5.9 Existing PES licences contain conditions which implement a financial ring-fence around the regulated business. This helps fulfil the Director's duty under section 3 of the Electricity Act to ensure that licence holders are able to finance authorised activities. The Authority will have a similar duty introduced by section 13 of the Utilities Act. To assist in ensuring that the electricity distribution businesses continue to retain access to necessary finance, readily and at reasonable cost, and that the regulator has access to all necessary information to secure that this is so, Ofgem considers that it would be appropriate that distribution licences should include financial ring-fencing conditions no weaker than those presently applying to the PESs. However, as part of the separation of supply from distribution, it is necessary to consider what restrictions should be in the new licences. It is not merely a matter of transferring over the existing obligations in the exact same form.
- 5.10 As part of alignment, Ofgem considers it important to standardise, as far as practicable, ring-fencing provisions across all monopoly energy network licensees. Certain modifications have been included to bring the distribution licence ring-fencing provisions into line with those of BG Transco plc's gas transportation licence where appropriate. Distributors and transporters who have had a Distribution/Transportation Services Direction, will have similar ring-fencing conditions applied. However, all licensed distributors and transporters will have a restriction on disposing of or relinquishing operational control over assets that form part of the system of supply without the consent of the Authority.
- 5.11 Similarly, Ofgem has decided that financial ring-fence conditions should not be included in electricity supply licences. In a competitive market, provided that there are appropriate arrangements for the orderly transfer of customers in the event of the financial failure of a supplier, financial ring-fence conditions are not necessary. This relaxation in respect of supply licences brings the position in electricity into line with that already existing in gas supply licences.
- 5.12 The final proposals take into account responses to previous proposals. Specifically, the definition of "Ultimate Controller" and the proposed restrictions on dividend payments have been revised to address these concerns.

Regulatory Accounts

5.13 In February, Ofgem included the existing obligation to produce regulatory accounts as a standard licence condition in all licences with the exception of the gas shippers' licence. It was proposed that it would be in section D and C in supply and distribution/ transportation respectively, section B in transmission where it would apply to the three transmission licensees, and in section B of the generation licence, but with an individual switch on/off mechanism. In the latter case, the condition would be switched on for those generators who have this in their licence already. Ofgem has also carried out some alignment across all the licences, such as the substitution of "affiliate" for "subsidiary" in the generation licence.

Respondents' views

5.14 Electricity suppliers felt that it was inappropriate to have to produce separate "in" and "out" of area accounts given that there would be one supply licence, that the obligation was inconsistent with price controls and that it should be deleted.

5.15 Some industry respondents believed that the condition should be switched on for all licensees in supply and transportation/distribution. One respondent was concerned that the obligation in generation should be switched off for small generators.

5.16 Several respondents queried the definition of "separate business" in the licences, pointing out that this did not seem to work, and was inconsistent between licences. Other inconsistencies in the drafting were also highlighted.

Ofgem's views

5.17 Ofgem has issued a separate consultation on Regulatory Accounts in August 2000 and the extent to which these are required in the future. That consultation indicated that Ofgem considered that regulatory accounts would no longer be required for competitive activities. Until that consultation process is complete (the closing date was 5 October 2000 and responses are currently being considered), the conditions will remain in the standard licences. The definitions of "separate business" will also remain as presently

exist. In electricity supply, separate regulatory accounts will continue to be required for In Area and Out of Area. Whilst there will indeed be one supply licence, there will be additional obligations on ex-PES suppliers in respect of their existing authorised areas (supply services area). In addition, price controls for “first tier supply” will still be in effect when the new standard licence conditions come into force and so information on this section of supply will still be required. However, Ofgem has taken this opportunity to align further the provisions across gas and electricity. Ofgem has also incorporated drafting to ensure that a licence holder with more than one licence where the provision applied would not have to produce the same set of accounts under each licence.

Metering

- 5.18 Metering obligations were divided between the electricity supply and distribution businesses in the February drafts and were subject to some amendments designed to recognise the development of competition in these areas. There was also alignment between gas and electricity in respect of a requirement to ensure regular meter reading.
- 5.19 Ofgem had previously consulted on whether reliance on the Competition Act might be sufficient with regard to meter reading services.¹² In the electricity supply licence in February, a regulatory mechanism was included, designed to ensure that where ex-PES supply businesses continued to have their own meter reading businesses, they would be required to choose the most economic alternative rather than relying solely on their own meter reading businesses. (Effectively they would have to go out to competitive tender in purchasing their meter reading requirements).
- 5.20 This proposal was so that ex-PES suppliers would not discriminate in the provision of such services and would undertake them in the most efficient and economic manner practicable having regard to the alternatives available. This proposal was thought appropriate because ex-PES suppliers who retain meter reading business will inherit a dominant position and Ofgem wanted to reduce the barriers to entry into meter reading.
- 5.21 In addition, ex-PES suppliers were to be required to provide non-discriminatory access to a system supporting prepayment metering.

¹² Initial Proposals on Standard Licence Conditions – A Consultation Paper, November 1999

Respondents' views

- 5.22 Many of the replies we received about metering were requesting either clarification or changes that were outside the remit of the introduction of standard licence conditions. For example, one company has queried the way metering services have been split between the ex-PES supply and distribution businesses. They believe that the obligation to provide such services until competition develops should rest with the distribution business, to avoid discrimination in the provision of the services by the ex-PES suppliers. These and other points raised will, of course, be considered but outside the consultation on the standard licence conditions.
- 5.23 Some respondents made proposals for further alignment between electricity and gas metering conditions, though no one proposal was put forward by more than one respondent. A number of respondents were unhappy with the introduction into the electricity supply licence of an obligation to read and inspect meters once every two years. Some industry participants argued that any obligation to physically visit the premises would discourage investment in remote meter reading technology. Consumers representatives, on the other hand, were concerned that one reading every two years was inadequate and suggested that the frequency of required visits be increased. It was also suggested, by some industry participants, that this condition should not be introduced, as they argued it had not resulted from the passing of the Utilities Act.
- 5.24 Many industry players argued that competition in data services was sufficiently advanced in the electricity market to negate the need for any obligation on dominant suppliers to provide these services. Others argued that such an obligation would give dominant suppliers a competitive advantage, as they would have access to sensitive commercial information.
- 5.25 One respondent suggested that the opportunity should be used to create a clearer regulatory framework for metering, which might be through making metering a separate licensable activity. One company believed that the condition, "Supply and Return of, and Information etc Relating to, Gas Meters", in the gas shippers' licence is out of date, as it does not reflect the growing liberalisation of the metering services. They believed this condition should be changed as part of Ofgem's planned consultation on metering liberalisation. In their common response, the PESs proposed that electricity supply

condition 10 (Duty to offer terms for meter provision) should be merged with electricity supply condition 21 (Agreements for the provision of meters).

- 5.26 One consumer body suggested that Ofgem should anticipate future changes in the liberalised market such as developments in metering technology and transitional arrangements. Specific comments were made in respect of the gas supply provisions about adjusting charges where meters have been found to have registered erroneously. These included the consideration of cases of total meter failure, giving the customer a choice as to the type of refund they get and providing the customer with a payment arrangement when the meter is found to be under registering.

Ofgem's views

- 5.27 Ofgem believes that the level of alignment achieved in metering is the maximum sensible given the inherent differences between gas and electricity metering. The requirement on electricity suppliers to physically read the meter every two years was introduced as part of the alignment with gas and therefore its inclusion in the standard licence conditions is warranted. In addition, the requirement is necessary for reasons of safety and security. It may be that with advanced metering the same imperatives would not apply, but Ofgem will need to review this in due course.
- 5.28 Competition in meter and data services was introduced to the electricity market in April 2000. Many PES businesses have either contracted out these services or created independent metering businesses to compete in the market. Continuing to require dominant suppliers to provide data services by licence condition may in itself prevent the further development of competition in this area. Ofgem has therefore decided to withdraw the conditions requiring dominant supply businesses to offer terms for the provision of data services and not to discriminate in their provision. However, the Competition Act will provide protection should a dominant supplier use its position to restrict the availability of data services to competitors.

Provision of information to the Authority

- 5.29 This condition was included in all licences in the February versions but there were differences between each of the versions in each of the licences.

Respondents' views

5.30 One respondent suggested that this condition should be aligned throughout the licences.

Ofgem's views

5.31 Ofgem has taken this opportunity to align the provisions in this condition, as far as practicable, throughout all the licences. Amendments include the removal of the provision allowing the Authority to ask for more extensive accounting information than that provided under the Separate Accounts condition. Ofgem believes this is unnecessary because further information could be requested under the general nature of this condition. Other amendments relate to further points of alignment.

Industry Agreements and Codes

5.32 As stated in the February consultation paper, Ofgem included a new standard licence obligation in all licences requiring licensees to co-operate in taking steps to procure the necessary changes to relevant industry agreements and codes. Licensees were required to use their "best endeavours" and the relevant agreements and codes were not listed.

Respondents' views

5.33 Several industry respondents felt that having to use "best endeavours" was too stringent and that "reasonable endeavours" should be used. Licensees also commented on the breadth of the condition and expressed a preference to see a list of agreements included. A few licence holders considered that the obligation would be onerous and was open-ended. Concern was also expressed about agreements where the licensee did not have governance. Innocent breaches might occur. Licensees also considered an appeal to the Authority for determination of disputes to be necessary where there may be a delay.

Ofgem's views

5.34 Licensees will have to make changes to industry agreements and codes as a result of the changes in legislation eg the separation of supply and distribution in electricity. The

condition was and is intended to serve as a marker to industry as to what is expected. Ofgem has considered the views put forward and has amended the condition in all licences in three key ways. First, the licensee must now use “reasonable endeavours” which follows the NETA change co-ordination condition; second, lists of electricity and gas agreements and codes, which have the inbuilt flexibility to be amended, are included respectively in each licence as appropriate; and third, a sunset clause has been included such that the obligation finishes at the end of next year.

6. Supply licences

Marketing condition

6.1 In the February drafts, Ofgem included the proposed enhancements to the marketing condition. The extension of the condition for a further two years until 2002 was proposed. Other enhancements included other methods of communication in which a contract might be agreed, eg, electronic communication, a conversation, etc and ensuring that marketing material was not misleading amongst others. These enhancements have been consulted on separately as highlighted in Chapter 1.

Respondents' views

6.2 Many suppliers have expressed the view that they want the conditions to end in 2002. Industry respondents were also uncertain as to the status of the proposals in the February 2000 drafts given that there was a separate Ofgem consultation on the marketing condition. They sought reassurance that Ofgem would not seek to impose any modifications that were not agreed as part of that separate consultation.

6.3 Two national consumer bodies made various suggestions as to how they believed the condition could be improved, for example, that it should remain in place indefinitely, that the EU Distance Selling Directive should be complied with, and that sales agents should be salaried and not paid on a commission only basis.

Ofgem's views

6.4 The marketing licence condition has been extended until March 2002. As it stands it can only be extended for two years at any one time. Ofgem's view is that suppliers should take full responsibility for ensuring that they, and their agents, comply with the condition. Ofgem has no evidence that it is commission only sales agents who cause complaints. It is the management of the agents which is important.

6.5 The EU Distance Selling Directive is an additional piece of legislation which does not impact the licence condition. The Directive includes obligations to provide details on the consumer's right of withdrawal from a contract (like the condition).

6.6 Further amendments to the condition, for example, to include within the condition conversations that may take place in public spaces and lead to a domestic supply contract, have been consulted on separately and are currently being voted on. For completeness, Ofgem has included the proposals in these draft versions of the new standard licence conditions. However, the final versions will reflect the outcome of the separate consultation.

Debt blocking and assignment

6.7 Ofgem removed the provisions relating to debt blocking and assignment in February because consultation was to take place separately on this. Ofgem subsequently consulted on these issues.

Respondents' views

6.8 Two industry respondents were concerned that the removal of the right to object because of debt may provide an incentive for customers to avoid paying their bills by frequently changing supplier. Another thought that there would be administrative difficulties and that the only sanction available in respect of customers that do not pay their bills would be expensive litigation.

6.9 Two respondents stated that the risks involved in supplying customers would increase which would in turn lead to increased tariffs. A number of respondents suggested that the removal of the right to object would lead to suppliers protecting their future income by requesting prepayment meters and/or security deposits.

6.10 Several industry respondents said that this proposal was subject to ongoing consultation and the provisions should not have been removed from the standard licence conditions.

6.11 One consumer representative believed that the proposed changes would lead to an increase in credit vetting, security deposits, prepayment meters and an increase in tariffs and that the introduction of debt recovery agents would exacerbate the position of those in payment difficulties.

Ofgem's views

6.12 The February 2000 consultation paper explained Ofgem's position regarding the reform of arrangements covering suppliers' rights to object to the transfer of customers in debt, and the assignment of final unpaid bills. In line with Ofgem's initial proposals, in the consultation paper "Customers in Debt and their Access to the Competitive Market" (December 1999), the original draft standard conditions did not include obligations in respect of debt objection and debt assignment. In view of the comments that have been received on these proposals, and the desire to give further consideration to the interests of all parties, Ofgem has decided to reintroduce the existing licence conditions on debt objection and debt assignment into the drafts. However, Ofgem's objective remains to achieve reform, and this document is therefore without prejudice to further proposals from Ofgem in this area.

Price comparison

6.13 In February, Ofgem included a proposed licence condition which would apply only to one of a number of price comparison initiatives that Ofgem is working on – the Energy Cost Index (ECI).

Respondents' views

6.14 In their responses to the consultation paper, suppliers were generally not in favour of an ECI.

Ofgem's views

6.15 Ofgem has therefore decided to develop the policy further by devising the rules for calculating the index. This will be market tested together with other price comparison initiatives. A consultation paper will be published by the end of January 2001 giving the results of the market research and proposals for future development.

Termination of contracts

6.16 The February drafts included the existing obligations in the licences. However, a consultation document published in March 2000¹³, and a subsequent letter modifying the original proposal following supplier comment, proposed a modification to the standard conditions of gas suppliers' licences and the electricity Master Registration Agreement. These modifications would remove the right of a supplier to raise an objection to prevent a customer transferring to another supplier in circumstances where the customer had not cancelled his or her contract with the first supplier. In gas, a supplier may raise an objection for both domestic and industrial and commercial customers. In electricity, this right is defined in the Master Registration Agreement (MRA) and is limited to designated customers.

Respondents' views

6.17 Of industry respondents, only two commented on this proposal in their response on the standard licence conditions. Both gave qualified support, one with regard to domestic customers, except where they had contracts for the supply of energy and other goods or services, and one as long as care was taken to ensure that problems with erroneous transfers did not result.

Ofgem's views

6.18 Having carefully considered the response to the documents referred to in paragraph 6.16, Ofgem has revised the proposed modification to the gas supply condition only in respect of domestic customers at this time. Ofgem is giving further consideration to proposals in respect of industrial and commercial customers and will co-ordinate any agreed change to the Master Registration Agreement to synchronise the rules for objection in both the electricity and gas markets. As the proposals are currently being voted on, Ofgem has included them in this draft of the standard licence conditions. However, like the proposed modifications to the marketing condition, if the proposals are not accepted, Ofgem will default to the existing provisions.

¹³ Removing a supplier's right to object to customer transfer on the grounds of insufficient notice – A consultation document, March 2000

Alignment of customer protection obligations

- 6.19 As stated in the DTI's October 1999 paper, "A Fair Deal for Consumers: Modernising the Framework for Utility Regulation, The Future of Gas and Electricity Regulation, The Government's Proposals for Legislation", the government proposed the alignment of electricity and gas regulation, except where there exist genuine differences between the two sources of energy or the structure of the markets. Alignment of the two fuels where appropriate is an underlying principle of the Utilities Act.
- 6.20 One of the areas where alignment seems appropriate is in the supplier's relationships with domestic customers. This will help customers better understand their rights and obligations under the licence or any contract they enter into with a licensee. It also makes sense in the context of an increasing dual fuel market, where licensees often hold licences to supply both fuels and customers often obtain both fuels from the same supplier.
- 6.21 A number of Ofgem's consultations have sought the alignment of certain customer protection provisions, like the consultation on the marketing condition or the Social Action Plan consultation on the conditions that refer to the social obligations. However, there are a number of conditions that refer to domestic supply contracts that were not aligned in the February drafts. In those drafts, these conditions were: Duty to supply Domestic Customers, Information given to Domestic Customers, Terms for Supply Incompatible with Licence Conditions, Domestic Supply Contracts, Notification of Terms, Termination of Contracts on Notice and Termination of Contracts in Specified Circumstances.

Respondents' views

- 6.22 A number of respondents suggested the full alignment of these conditions. The views were generally in favour of alignment with the electricity provisions.

Ofgem's views

- 6.23 Now that the Act has Royal Assent, and in the light of responses, Ofgem considers it appropriate to further align the provisions in the licences as part of the consultation, in each case aligning to the better practice and taking into account comments received and

our duties. The October drafts of the standard licence conditions include Ofgem's proposals for alignment between the conditions referred to in paragraph 6.22. In its proposals, Ofgem seeks to balance its new principal objective of protecting the interest of customers with the need to take account of the licensee's rights. Ofgem believes that the proposals put forward in the draft gas and electricity supply licences achieve that balance.

- 6.24 The nature of the existing provisions was already similar, if not exactly the same, in most cases. The amendments made have generally been limited to repositioning similar provisions in the same conditions for gas and electricity and to aligning the wording. In other cases, the provisions themselves have been aligned, usually following the electricity model. The alignment has not included different provisions that are specific to each fuel or each market structure.
- 6.25 In the condition, "Duty to supply Domestic Customers", the gas licence has been amended to follow the electricity model. The duty to supply has been changed to a duty to offer terms, therefore making the duty to supply subject to the domestic customer accepting the terms offered. We have also introduced in gas supply some of the exceptions to the duty to offer terms to supply that appear in the electricity supply licence, while keeping the exceptions that are specific to gas. In doing so, the exceptions to the duty to offer terms in gas supply have become less specific. Mirroring the electricity arrangements, we have included an exception of where it is not reasonable in all the circumstances for the licensee to be required to supply gas. For this reason, we have proposed the introduction of a power for the Authority to determine on any question as to whether the circumstances are reasonable.
- 6.26 The condition, "Termination of Contracts in Specified Circumstances", has also been amended in gas supply to follow the electricity model. The time periods for notices have been aligned. The 48 hours notice that the customer has to give to end the contract when he ceases to own or occupy domestic premises has been aligned to two working days. Similarly, the time periods for the termination of the contract when the customer has ceased to own or occupy domestic premises without giving this notice have been aligned, and has been amended from 28 days after the customer gives notice to two working days.

- 6.27 In the condition relating to information to be given to domestic customers, we have extended some of the provisions in gas supply to electricity supply. For example, providing details with or on each bill shall be deemed to be sufficient compliance with the obligation to keep domestic customers informed of the quantity of energy used. We have also added the obligation to inform domestic customers of the most recent meter reading if requested. References to the Authority in electricity supply have been deleted, as the Consumer Council will be the first port of call in the new regime in relation to complaints.
- 6.28 In the condition about the terms of supply being incompatible with the conditions, the existing paragraph 2 in electricity supply has been replaced with the equivalent paragraph in gas supply. The word "breach" as used in electricity would not capture the situation where a term was included in the supply contract that did not fall within the spirit of the condition but was not, strictly speaking, a breach of the condition.
- 6.29 In the Gas Act, section 7A, paragraphs 9 and 10, there are provisions which require the licensee to ensure continuity of supply on similar terms where the licensee wishes to revoke or restrict its licence. This provision applies to all customers. Now that the Utilities Act has received Royal Assent, Ofgem has reviewed the provisions in the draft licences and has included a draft standard licence condition in electricity supply which mirrors the provisions in gas.
- 6.30 Ofgem has also clarified the use of the term "contract".

Non-discrimination

- 6.31 In July 2000, Ofgem issued a consultation, "Gas and electricity supply licences, Proposals for standard non-discrimination licence conditions", which proposed removing these conditions from all gas and electricity supply licences, when the new licences are implemented by the Secretary of State for Trade and Industry as part of the implementation of the Utilities Act 2000. Ofgem believed that the removal of the supply non-discrimination licence conditions was the best way to better co-ordinate gas and electricity regulation, and to protect the interests of consumers and promote effective competition in gas and electricity supply activities.

6.32 Ofgem considered three options as part of its review of the supply non-discrimination licence conditions. These were:

- the retention of the current non-discrimination conditions, unamended;
- amending the current non-discrimination conditions, to take account of recent market developments and differences between the current gas and electricity conditions; and
- removing the current non-discrimination conditions and using the Competition Act 1998 to address anti-competitive behaviour in the gas and electricity supply markets.

6.33 In assessing the options, Ofgem considered its primary duty under the Utilities Act 2000 to protect the interests of consumers, where possible by promoting effective competition, and the government's objective to better align regulation of the gas and electricity industries. As the removal of price controls indicated, Ofgem believed that, as competition develops, the most effective way to regulate the gas and electricity supply markets to secure effective competition and to protect consumers, is to move from reliance on specific *ex ante* constraints on behaviour, to an approach based upon the general prohibition of conduct that has damaging effects. More specifically, since effective competition is likely to be the best means of protecting consumers' interests, Ofgem was of the view that what should be prohibited is conduct that prevents, restricts or distorts competition.

6.34 Following from this, Ofgem assessed each option against the following factors:

- the best use of Ofgem's powers under sector specific legislation and competition legislation to address anti-competitive behaviour in the gas and electricity supply markets;
- the most efficient use of Ofgem's resources to address anti-competitive behaviour in the gas and electricity supply markets;
- minimising the regulatory burden on gas and electricity suppliers; and
- ensuring that Ofgem's approach to address anti-competitive behaviour in the gas and electricity supply markets reflects the development of competition so far, and the prospects for its future development.

6.35 After evaluating each of the options against these factors we proposed to remove the supply non-discrimination conditions from the gas and electricity supply licences. Ofgem believed that its approach of moving from *ex ante* to *ex post* regulation as competition developed should lead to customers benefiting more quickly from suppliers' innovations and allow Ofgem to focus its resources on market developments that have anti-competitive effects. Ofgem believed that the Competition Act 1998 could address anti-competitive behaviour that will cause appreciable harm to customers and competitors in the gas and electricity supply markets. Ofgem received twenty five responses to the consultation, of which twenty two made substantive comments on the proposals. The responses are summarised and respondents listed in Appendix 2.

Ofgem's views

6.36 As explained in the consultation document, Ofgem developed the factors it used to evaluate the three options to ensure that it reflected its duty to protect the interests of consumers, where possible by promoting effective competition. Ofgem was particularly concerned to ensure that consumers continued to be protected from anti-competitive behaviour, while enjoying the benefits of a developing competitive market.

Option 1 – Retaining the current conditions, unamended

6.37 As set out in the consultation document, Ofgem agrees with respondents that this option is not the best way to protect customers and competitors from anti-competitive behaviour in supply markets, as the current conditions do not take account of recent market developments, and it does not achieve the government's aim of better aligning gas and electricity regulation. Ofgem agrees that the advance notice requirement in electricity can delay the introduction of electricity offers compared to gas.

Option 2 – Amending the current conditions to take account of recent market developments and to achieve better alignment between the gas and electricity conditions

6.38 Ofgem believes that the Competition Act 1998 will allow Ofgem to address all anti-competitive behaviour that is likely to have an adverse effect on customers and competition in supply. We also believe that the deterrent effect of fines under the Competition Act 1998 and the interim measures powers will allow Ofgem to tackle anti-competitive that is causing serious harm quickly. Although all suppliers may face similar compliance costs, duplication of powers may act to increase prices for customers because of the extra expense for all suppliers.

6.39 Ofgem believes that the advance notice requirement delays the introduction of pro-competitive offers in electricity to the disadvantage of customers. This also acts to distort the development of supply competition. Ofgem believes that the resources it uses to consider offers under this mechanism can be used more effectively to address anti-competitive behaviour.

Option 3 – removing the non-discrimination conditions and using the Competition Act 1998 to address anti-competitive behaviour

6.40 Ofgem continues to believe that this option is the best way to protect customers from anti-competitive behaviour in supply markets and to better align gas and electricity regulation. Ofgem believes that competition is continuing to develop well in the gas and electricity markets, and that as competition develops it is appropriate in supply markets to rely on competition law, rather than sector specific legislation. Ofgem believes that the Competition Act 1998 can address all anti-competitive behaviour that will have an adverse effect on customers and competition, that is covered by the non-discrimination conditions.

6.41 Ofgem believes that the removal of the non-discrimination conditions will reduce compliance costs by removing duplication. We recognise that companies are familiarising themselves with the Competition Act 1998, but a lot of information has already been produced by OFT and the sector regulators to assist in understanding how the Act will be interpreted. This information should also help customers and their representatives understand the provisions of the Competition Act 1998.

6.42 Ofgem recognises that there are differences between the approaches for taking action against anti-competitive behaviour under the Competition Act 1998 and the sector specific legislation. However, Ofgem believes that combined with the deterrent effect of financial penalties under the Competition Act 1998, the interim measures powers provide sufficient protection for customers and competitors against the possibility of behaviour causing substantial harm being allowed to continue while an investigation takes place.

The application of the Competition Act 1998 to the energy sector

- 6.43 Ofgem is currently considering the responses to the formal May 2000 Ofgem and OFT consultation, "Competition Act 1998, Formal consultation draft, Application to the Energy Sectors" on the energy guidelines and expects to publish the final guideline in November. Ofgem believes that the energy guideline along with the other guidelines produced by OFT and the sector regulators provides extensive guidance on the application of the Competition Act 1998.
- 6.44 The respondents to the consultation are correct that formal guidance or decisions will not be given under the Competition Act 1998, unless the agreement or conduct has been introduced. This requirement, along with the fees for guidance or decisions, are intended to deter companies from making requests for guidance or decisions unless they have a clear intention of introducing the agreement or conduct. However, if companies approach Ofgem for informal guidance on a proposed agreement or conduct, Ofgem will endeavour to assist the company as far as possible, although any guidance would not have the legal status of formal guidance or decisions.
- 6.45 Ofgem has agreed the process for accepting fees for guidance or decisions with OFT and the other sector regulators, in accordance with the Competition Act 1998. The requirement to pay a fee for guidance or a decision has no effect on whether the guidance or decision will be favourable to the applicant. The fee is intended to deter companies from making frivolous applications for guidance or decisions.

The consistency of Ofgem's approach to the regulation of supply and generation activities

- 6.46 As is discussed in Ofgem's second submission to the Competition Commission in June 2000, "Introduction of the market abuse condition into the licences of certain generators, Ofgem's second submission to the Competition Commission", Ofgem believes that it should be able to tackle all cases of anti-competitive behaviour in the gas and electricity markets. The energy guideline explains the approach Ofgem intends to take when exercising its powers under the Competition Act 1998. However, section 60 of the Competition Act 1998 requires Ofgem, in exercising its powers under the Act, to ensure that it acts in a manner that is, as far as possible, consistent with current EC and UK jurisprudence. In Ofgem's second submission, Ofgem's explains how current jurisprudence on, for example, the ability to define temporally transitory markets and the importance of market shares for assessing dominance is likely to prevent certain anti-

competitive behaviour, such as some abuse in the wholesale electricity market, from falling within the scope of the Competition Act 1998.

- 6.47 It is because current jurisprudence on the areas outlined above is likely to prevent Ofgem from using its powers under the Competition Act 1998 to tackle potential abuses in wholesale market that Ofgem has sought to include market abuse conditions in generators' licences. As relevant case law develops and the boundaries of the Competition Act 1998 shifts to incorporate potential abuse of this kind, the licence condition will be scaled back or removed altogether. Ofgem does not believe that current jurisprudence will constrain the application of the Competition Act 1998 to anti-competitive behaviour in supply markets, therefore, a similar market abuse condition is not required.
- 6.48 Ofgem has considered the comments set out above and continues to believe that removing the supply non-discrimination conditions and using the Competition Act 1998, is the best way to protect customers and competitors from anti-competitive behaviour in supply markets and to achieve a better alignment of gas and electricity regulation. Ofgem believes that as competition develops *ex post* prohibition of anti-competitive behaviour is better than *ex ante* regulation. In particular, *ex post* regulation should ensure that pro-competitive offers are not delayed from coming to market to benefit customers. Also, the ending of the duplication of powers to tackle anti-competitive behaviour should reduce the regulatory burden on suppliers.
- 6.49 Ofgem believes that the Competition Act 1998 can address all anti-competitive behaviour that will have an adverse effect on customers and competition in supply markets. Ofgem has the power under the Competition Act 1998 to set penalties of up to 10% of UK turnover for each year of a breach up to a maximum of three years. Ofgem can also take interim measures to address behaviour that is causing serious and irreparable damage to a particular person or category of persons or to protect the public interest. Interim measures can allow anti-competitive behaviour to be addressed quickly. The Competition Act 1998 also provides suppliers with the opportunity to seek guidance or a decision as to whether agreements or conduct would breach the prohibitions of the Act. Suppliers have to pay a fee for guidance or a decision, which deters suppliers from seeking guidance or a decision unless they believe there is a serious risk that their behaviour may be anti-competitive or they are investing a large amount of money.

Provision of services in electricity

6.50 In earlier consultations, Ofgem proposed that there should be additional obligations on ex-PES suppliers given their position in the market. The conditions regarding Top up and Standby Supplies, Exempt Supply Services and Prepayment Meter Services (PPM) embody these additional services.

Respondents' views

6.51 The PESs felt that these obligations go beyond what is reasonable, as there is sufficient competition within the market for Top up or Standby Supplies and Exempt Supply Services. They believed that no supplier should be under a duty to provide Top up or Standby Supplies and Exempt Supply Services and that Ofgem's powers and jurisdiction under the Competition Act 1998 should be adequate protection against abuses of position by dominant ex-PESs.

6.52 Responses to conditions 56, 56A, 56B and 56C (Top-up and Standby, Exempt Supply Services and PPM) from ex-PES suppliers indicated that they did not consider it necessary for the extra obligations to be placed upon them. Whilst most appear to accept that there is a requirement and a case for ex-PESs to continue to be obliged to provide PPM services, there was scepticism with regard to the other requirements. Most companies were of the view that competition or other provisions already offer much of the protection that these conditions seek to cover.

6.53 Companies expressed concern about the additional obligation on the ex-PES supplier to offer terms to other electricity suppliers for access to their PPM infrastructure in their Supply Services Area (existing authorised area). They claimed that this would maintain the status quo and not lead to competition in the provision of prepayment meter services. They also argued that if the burden falls upon suppliers it could lead to distortions in competition in supply because of the information received by a former PES supply business about its competitors.

6.54 Whilst the PESs accepted the need to retain an obligation in relation to PPM services, they argued for a flexible sunset provision for all of these ex-PES obligations, should they remain as standard licence conditions.

6.56 The ability to disapply the PPM obligation in the future can be achieved by including PPM services in condition 57 (Duration of condition 56B), which already gives the Authority the ability to disapply the requirement to offer terms for Top-up, Standby and Exempt Supply Services if a company were to request such a disapplication. The condition would make it clear that no disapplication would be given if the provision of PPM Services by other suppliers in the Supply Services Area was deemed insufficient.

6.57 Companies have also expressed concern about the minimum 24-month period between when the disapplication request is made by the Licensee and the disapplication date. While they understand that the Authority needs to have sufficient time to investigate whether the conditions of the market allow for the relevant part of condition 56B to be disappplied, and whether or not to refer the matter to the Competition Commission, they believe this can be done in a shorter time.

6.58 There was disquiet over the inclusion of the Authority's veto over any charging disputes and the need for consultation in condition 56, as it was proposed that this would place a heavy burden on the licensee; most industry respondents deemed it unnecessary.

Ofgem's views

6.59 Ofgem understands companies' concerns about the provision of these services. However, having carefully considered the comments put forward, Ofgem remains of the view that the ex-PES supplier is best placed to meet these obligations particularly as it is likely that the number of exempt suppliers will increase with changes to supply exemptions. When there is evidence that these services are being provided by competitors, Ofgem will review the need for the continuation of these licence obligations.

6.60 However, Ofgem has retained the condition which allows the licensee to request that these obligations be disappplied. Whilst Ofgem needs to ensure that PPM customers are provided, and continue to be provided, with the necessary infrastructure, it also needs to provide for market changes and the possibility of other companies entering the market. Therefore, Ofgem might want to be able to disapply the PPM obligation from ex-PES suppliers in the future, subject to ensuring that these services were being provided by

another or other companies. The PPM obligations have therefore been included in the disapplication condition, although the disapplication process is more restrictive than the process for the other obligations given the different nature of the service being provided.

- 6.61 The veto on charging statements and the requirement to consult were introduced as part of the alignment with gas. Ofgem has reconsidered this aspect given the strong views put forward. Whilst there is some merit in alignment here, Ofgem has decided that the existing provisions be retained and any further alignment considered at a later date. These provisions have, therefore, been removed.

7. Distribution licences

- 7.1 As stated in Chapter 1, the Act requires that the activity of distribution be authorised, by either licence or exemption. Ofgem is consulting, on behalf of DTI, on the standard licence conditions it deems appropriate for the new distribution licence. DTI have consulted already on "Exemptions from the requirement for a licence to distribute electricity" in March 2000. Ofgem expects that DTI will be consulting shortly, for a second time, on the criteria that might be necessary for granting an exemption to an electricity network operator. The distribution licence obligations may need to be revised following the outcome of this review.

Duty to connect

- 7.2 Ofgem included obligations regarding connections in the February version of the standard distribution licence. In particular, the obligation to retain an established connection was retained as Ofgem, at that time, was uncertain as to the level of the detail that would be set out in the Utilities Act.

Respondents' views

- 7.3 One industry player felt that the distribution licence should include a section on connection agreements and that these should include responsibilities and rights at any boundary between adjacent licensed and unlicensed networks, transmission systems and customers.
- 7.4 Three industry respondents argued that new entrants will need the powers conferred under Schedules 3 and 4 to comply with their duty to connect, but one did not think that having the powers should mean that an unlimited duty to connect obligation is imposed on new entrants. These powers, if granted, allow a distributor to compulsorily purchase land and dig up roads if either of these prove to be necessary in relation to connection work. One respondent felt that there should be a level playing field between gas and electricity, so that if a gas transporter already has these powers, he should also be given these powers for electricity distribution should he enter that market. PESs wanted these powers to be linked to their network and not just their Distribution Services Area.

Ofgem's views

- 7.5 The Utilities Act encompasses the duty to connect for distributors, but this duty will not arise in circumstances where a distributor would need Schedule 3 and 4 powers to be able to make a connection and does not have them by virtue of its licence. It is open for distributors other than ex-PES distributors to make a case to have these powers. If such a case is successful, Ofgem will use the flexibility in the application conditions to switch on these particular conditions for any such distributor. Ofgem will also link these powers for ex-PES distributors to their network whilst ensuring that they still apply within their Distribution Services Area so that at least one distributor has the duty to connect in each part of Great Britain.

Charging statements

- 7.6 Ofgem included a requirement for distributors to consult with other parties when proposing to revise their charging statements for use of system and connections in the last drafts of the standard licence conditions. Also included was an ability for the Authority to veto any such proposed revisions. Both of these provisions were copied from gas as part of the process of alignment wherever appropriate.

Respondents' views

- 7.7 The general view of industry respondents was that the proposed introduction of a new procedure requiring licensees to consult with the users of connection and use of system services before revising their charges is not required. It was suggested that it does not offer any new protection not already afforded by the current arrangements and that this could entail having to consult a huge number of people, which would be onerous and impractical. It was proposed that it would be more practical to oblige distributors to ensure adequate publicity and only send information to those who request it.
- 7.8 Respondents were not clear as to the proposals for consultation on the statements, which provide the basis for connection or use of system charges. That is, it was unclear whether the consultation process (which includes 28-day periods for representations or objections) is intended to precede or can run in parallel with the five month notice period (system tariffs) specified in condition 5 (Use of system and connection to system)

of the distribution licence. It was suggested that if all consultations had to be concluded prior to the five-month notice, the consultation process would take six months to complete. Consequently, tariffs would need to be set early, which could result in misleading indications to suppliers.

- 7.9 One respondent believed that the new requirements, such as the consultation process, in condition 5 were covered by the existing arrangements. That is, anyone that wishes to make representations to the regulator about the licensee's proposals can already do so and the new arrangements would remove the current flexibility. Another respondent observed that the existing arrangements were quite adequate to protect suppliers' interests.
- 7.10 There were questions over the proposals (in condition 5B) to remove the PES licence requirement to offer to enter into agreements to provide connections, whilst maintaining the requirement to offer to enter into agreements to retain established connections. It was also suggested that, on the basis that having only one route to connections would be both more appropriate and more effective, condition 5B should be modified to remove the obligation to retain a connection. This would mean that the role of condition 5B (in respect of connections) would then be to constrain the licensee's performance of its statutory connection duties so as to secure consistency with the statement of the basis of charges to be prepared and published by the licensee under condition 5.
- 7.11 There was confusion as to why one of the specified considerations (in condition 5C) had been removed. This related to the regulator having regard, when settling disputes under the condition, to the fact that the other party to a dispute should pay the whole (or appropriate proportion) of the determined costs.

Ofgem's views

- 7.12 Given the industry's strong representations regarding the two proposed new provisions on the consultation and the Authority's right to veto, Ofgem has reconsidered its position and has removed these specific provisions from all electricity conditions in which they appeared.
- 7.13 Now that the Act has received Royal Assent, Ofgem has also reviewed the statutory duty to connect and has reinserted the provisions from the existing condition that were

missing in the February draft. These include the detailed provisions to be included in any offer by a licensee with regard to connections, the charges to be paid including the principle that no charge should normally be levied for works that do not increase the load requirement by more than 25 per cent of the existing effective capacity, and the existing timescales in which to carry out works. Ofgem considers that a specific reference to the retention of an existing connection is required. This is to ensure that existing connections as well as new ones are maintained.

Restrictions relating to embedded generation

7.14 Ofgem included this restriction in the draft distribution licence in February as part of the policy of separating monopoly networks from non-monopoly competitive areas.

Respondents' views

7.15 PESs were opposed to the imposition of this condition as a standard licence condition. They questioned whether it followed from the separation of distribution and supply in the Utilities Act or from government policy on alignment. They believed it could adversely affect renewable obligations and the development of competition in embedded generation. They also pointed out that it does not apply to all PESs at the moment. They believed that they could reduce operating or network costs by using embedded generation, improve the quality of supply and avoid potentially controversial overhead circuit construction.

7.16 They believed it was not necessary to have such a restriction, particularly as the Utilities Act will place in statute a requirement on distribution companies to facilitate competition in generation and supply. In addition, there will be separation of the distribution business from any other business within the group. One PES suggested that if it remains, it should be a special condition, whilst another believed that the criteria for giving approval should be set out.

7.17 The Scottish companies were particularly concerned given the large amount of renewable energy which is or could be produced in this way. They would also require derogations for their existing embedded generation.

Ofgem's views

7.18 Ofgem has reviewed this proposed condition in the light of responses received and other provisions. Given the proposed provisions with regard to ringfencing, non-discrimination in connections, the prohibition on cross subsidies, and the provisions with regard to the statutory duty to facilitate competition in supply and generation and the Competition Act, Ofgem considers that such a restriction is no longer required. The above mentioned provisions should ensure that distributors should act on an arms length basis between themselves and any affiliated generation company and in a non-discriminatory manner to any person seeking connection.

Long Term Development Statement

7.19 Ofgem included a standard licence condition in the distribution licence in February which would require distributors to produce a statement indicating what work they are planning to carry out on their networks over a set period of time. This work could relate to reinforcement or other modification and the statement would provide transparency for customers who might be considering connecting to the distributor's network. This obligation was introduced as part of the alignment with obligations on gas network licence holders.

Respondents' views

7.20 There appeared to be a general view amongst PESs that the obligation to produce a five year statement was inappropriate as it was not a direct consequence of the Utilities Act. They felt it would prove to be costly whilst the benefits of such a statement remained unclear. There was concern that the cost of producing such a document had not been taken into consideration during the recent price review. Another respondent was concerned about the introduction of this requirement, which it believes is likely to be onerous to produce, of limited use and might compromise company confidentiality. It believed the alignment of gas and electricity in this instance did not make sense, due to the different structure of the industries.

7.21 PESs believed that this condition should be consulted on separately and should reflect the results of the DTI/Ofgem working group on embedded generation.

- 7.22 It was suggested that a long term development statement would not offer the customer any further information not already covered by the current obligations in the existing PES licences. There was a belief that the localised reports already produced are more customer focused.
- 7.23 The main concerns referred to the level of detail and the period of time specified. The companies did not see any benefit in providing details for the network under 33 kV, as this network is very dynamic and has planning periods of 12 to 18 months. The statement would become outdated very quickly, and the extent of the network would make it an extremely costly and time consuming exercise. Generally, the issue of a statement for the lower voltage levels appeared to cause some concern.
- 7.24 Two respondents supported the introduction of this condition, which they believed would promote embedded generation and allow the derivation of demand information. One company believed the statement should include the nature and cost of the distributor's investment plans for the network together with their demand controlled areas.

Ofgem's views

- 7.25 Ofgem has carefully considered the views expressed about this condition, but remains of the view that the information in such a statement will be of use to embedded generators and other potential customers of the distributor. Ofgem has made revisions to the condition, for example, a caveat in the licensee's favour has been introduced such that information to be provided under the statement need only be information that it is reasonably practicable for the licensee to provide. Ofgem believes this will address the concerns expressed by PESs regarding the need to make the statement a "high level" document and to avoid any requirement to provide unnecessary and unhelpful detail. In view of this amendment, our position remains that it is inappropriate to add a voltage limitation, as the licensee will have adequate protection from the "reasonably practicable" wording. Ofgem, as and when requested, will also give advice on what information should be provided.

- 7.26 With regard to the cost of producing such a statement, Ofgem expects this to be at a minimum as PESs already have systems which incorporate data on their networks. It is envisaged that much of the scope of information required under the draft licence condition will be no greater than that which was produced by Area Boards prior to 1990 for the electricity supply industry use.
- 7.27 With regard to the argument that some of the information is available on request under existing obligations, our difficulty with this argument is that a person may not be aware of the specific information which he should ask for pursuant to the existing obligation without first having obtained the more general information to be provided under this condition. The existing condition does not provide the longer term view which is important for planning purposes for any person considering a connection.
- 7.28 The proposed standard licence condition has been brought to the attention of the working group on embedded generation.

Master Registration Agreement

- 7.29 The February distribution licence contained an obligation on all licensed distributors to comply with the Master Registration Agreement (MRA).

Respondents' views

- 7.30 One respondent was concerned about the need for non-PES licensed distributors to invest in the systems required to fulfil obligations under the condition which requires compliance with the MRA. A company expressed concerns about the cost of providing these services to private networks, and wanted to pass these costs onto them. They believed private distributors should then recharge suppliers as part of their access charges.

Ofgem's views

- 7.31 Decisions here depend on the level of distribution exemptions still to be set. This matter is in hand with the DTI and Ofgem expects a second consultation to be issued shortly. Subject to the outcome of that consultation, Ofgem is of the view that compliance should

not require significant investment as the systems are already in place. Provision has been made as to the recharging of suppliers as above.

Data Transfer Service

7.32 The obligation to establish a Data Transfer Service was contained in Section C of the distribution licence (and mirrored in gas transportation) in February.

Respondents' views

7.33 One company expressed its intention to charge private distributors for the service. Another voiced concerns about the fact that any entrant to the market would be required to use the Electronic Service, with the associated costs of installing and operating the link, and about how the costs should be defrayed. One licensee pointed out that a single service provider would have enormous market power, which might damage competition.

Ofgem's views

7.34 Again, much depends on the level of distribution exemptions. Ofgem has noted the concern expressed about the costs of compliance, however, compliance applies to ex-PES distributors in the first instance. It is not Ofgem's intention to introduce this obligation to any other licensed distributor and so the condition sits within Section C.

Information and incentives project

7.35 Ofgem published final proposals in September 2000, "Information and incentive project, Output measures and monitoring delivery between reviews, Final proposals", as part of the Information and Incentives Project (IIP), setting out details for collecting output measures and monitoring delivery between reviews. It is Ofgem's intention to put in place a specific licence condition for the collection of information under the IIP and for arrangements relating to the audit of that information. Ofgem considers that a specific licence condition will provide comfort to the distribution businesses about the type of information which will be collected, the audit arrangements and the process for making changes over time. This is intended to reduce the perception of regulatory risk.

- 7.36 A draft of the licence modification was included in Appendix 6 of the IIP proposals. The process for consultation and implementation were also outlined. Subject to agreement, the licence condition will initially be included in the PES licence.
- 7.37 The IIP licence condition which is introduced into the PES licence will subsequently be inserted in Section C of the standard distribution licence. This means that it will apply only to the ex-PES distribution businesses and not to other holders of a distribution licence.

8. Transportation licences

Removal of geographic exclusivity

8.1 Obligations were incorporated in the draft transportation licence to facilitate the removal of geographic exclusivity in gas transportation. Certain obligations about information provision and notification were proposed to apply to all transporters whilst a Designated Registrar of Pipes (DRP), who would maintain records on all mains, could be designated for any area.

Respondents' views

8.2 Respondents agreed that safeguards must be put in place to ensure that the removal of geographical exclusivity does not cause practical problems, increased costs or safety risks. It was suggested by one industry player that the function of the DRP will be immensely important as they will have to confirm that information is accurate and will have to provide information in emergency situations. Another was concerned about the potential liabilities regarding the provision and recording of information.

8.3 One licensee stated that gas transportation systems charges are based on investment criteria which reflect the planned usage of the network and believed that the removal of geographic exclusivity might threaten these criteria. Transportation prices must not rise unduly to reflect this.

8.4 Licensees were concerned that the requirement to maintain huge quantities of information, including the establishment of the DRP would lead to significant administrative costs. They suggested that the current proposals were unworkable and that there should be a separate consultation.

8.5 One respondent was adamant that only one DRP should be appointed, he should be given powers to assist the Authority and should be accountable to the Authority to ensure that there is no confusion or possible complications, especially in relation to boundaries. Alternatively, if there was to be more than one, there should be a duty to consult with one another.

Ofgem's views

- 8.6 Ofgem remains of the view that these provisions are necessary to ensure stability and safety of the gas network. However, Ofgem has revised the conditions having taken into account suggestions received from one respondent and the Health and Safety Executive. Ofgem has also confirmed that these provisions will not be switched on without a separate consultation taking place and is open to be persuaded of an industry alternative. Until such an alternative is put forward, with Ofgem being satisfied as to its effectiveness, the conditions will remain as proposed in the standard licence conditions.

Supply point administration and data transfer

- 8.7 The standard licence conditions issued in February 2000 included obligations on gas transporters to provide a supply point administration service (SPA) and a data transfer service. These obligations were introduced to align gas with electricity, as provided for in the Utilities Act.

Respondents' views

- 8.8 Most industry respondents who mentioned the relevant conditions supported the principles behind the obligations, with the exception of one company which saw both conditions as unnecessary. However, some respondents have argued that changes are needed to ensure that the differences between gas and electricity are adequately reflected in the conditions. For instance, they have argued that making a transporter responsible for registering supply points in its specified area does not make sense now that geographical exclusivity has been removed. One respondent argued that requiring transporters to register information about meters was unnecessary and might adversely affect the introduction of metering competition. The same respondent also argued that the requirement to respond to queries from industry players and customers was too wide ranging.
- 8.9 One respondent stated that the new requirement to have a SPA system in gas is wider than the existing requirement. They were concerned that having to agree an alternative approach will incur costs and will require a transitional period. They suggested that all transporters should meet and agree an industry standard approach.

- 8.10 Some industry respondents have argued that the obligation to set up a data transfer service could impose high costs on those who have to use it. However, respondents have also highlighted the need for some form of standardisation in formats used between transporters and shippers.
- 8.11 A customer representative proposed that conditions requiring the set up of a data transfer service should also include duties of accuracy and confidentiality, with financial penalties for mistakes.
- 8.12 One company believed that one body should be set up to provide these services in gas in much the same way as has happened in electricity and that the link between the two obligations should be made clearer.

Ofgem's views

- 8.13 Ofgem accepts the argument that there are differences between gas and electricity that make it unhelpful to fully align the obligations to provide supply point administration services and data transfer services. This does not mean, however, that these obligations should not be aligned in so far as it is both practical and desirable. We propose two main changes to these conditions.
- 8.14 The condition requiring provision of supply point administration services has been moved to Section B. This means that it now applies to all transporters, not only to those licensees who receive a direction from Ofgem so specifying. Each transporter will be responsible for the supply points connected to its pipelines. This addresses the concerns raised by the removal of geographical exclusivity whilst ensuring that all supply points are registered. Ofgem agrees that the licensee should be allowed to procure the service if it so wishes. The condition has been changed accordingly.
- 8.15 Ofgem has noted the concerns expressed about the costs of introducing a data transfer service. However, we believe that there is a need for a file format system available to all transporters and shippers. This will make it easier for shippers to interact with a number of different transporters and thus remove a potential barrier to competition in these areas. We have noted that recently there has been some considerable debate about whether file formats developed by a transporter should be made available to others. Ofgem therefore

considers that the minimum requirement is that dominant transporters should make available to others, free of charge, any file formats used to send data for purposes specified in the network code. The standard licence condition has been changed accordingly.

9. Transmission licences

Structure of the transmission licence

9.1 Ofgem had proposed a Great Britain wide transmission licence following the policy of standardising conditions as far as possible across Great Britain. The February draft of the transmission licence was structured in such a way that conditions that could apply to all three transmission companies were included in section B. Supplementary sections dealt with those standard conditions that applied in England and Wales or Scotland only.

Respondents' views

9.2 The three transmission companies all pointed out certain conditions which needed to be treated as supplementary or special conditions because they had individual application either in England and Wales or in Scotland, or for an individual licensee.

Ofgem's views

9.3 Having considered the views put forward, Ofgem has restructured the draft transmission licence so that those conditions which apply to a licensee because of the location in which they transmit electricity, have been moved to the appropriate section, that is, England & Wales or Scotland. Where an obligation applies to a licensee because of their special circumstances, this will become a special condition applying only to that licensee eg Hydro Benefit provisions.

Connection and use of system code

9.4 The February consultation on standard licence conditions referred to the Connection and Use of System Code (CUSC) but the draft did not include any modifications. Modifications in respect of CUSC were proposed in March 2000.

Respondents' views

- 9.5 One licensee made suggestions about possible amendments to the existing condition 10 with some of these suggestions being as a result of alignment between gas and electricity.

Ofgem's views

- 9.6 The suggestions made are being considered separately as part of an on going Ofgem/DTI consultation. The following consultation documents have been published during this process: NGC System Operator Incentives, Transmission Access and Losses under NETA, an Ofgem consultation document, December 1999; NGC's connection and use of system code, an Ofgem/DTI consultation on the scope and content of the connection and use of system code, March 2000; Connection and use of system code, proposed changes to the National Grid Company's licence, an Ofgem/DTI consultation document, June 2000; NGC's connection and use of system code, scope content and licence changes, an Ofgem/DTI final proposals document, August 2000. This consultation process will provide a new contractual framework, replacing the existing Master Connection and Use of System Agreement (MCUSA) for connection to, and use of, NGC's high voltage transmission system in England and Wales. The main objectives of the CUSC are twofold. First, to improve the governance to increase the flexibility of the arrangements for connection and use of NGC's transmission system. Second, to clarify procedures relating to the resolution of disputes relating to these arrangements. These changes will enable the introduction of new transmission access arrangements required under NETA and the longer term development of the arrangements in line with market developments.
- 9.7 In summary, the proposed condition will place obligations on NGC to establish a connection and use of system code and to establish and operate procedures for amendments to the CUSC. It is proposed that this obligation will be accompanied by a new licence condition in the licences of generators, suppliers and distributors obliging the licensees to be party to and comply with the CUSC.
- 9.8 The new conditions, C8 to C8G, replace the existing conditions 10 -10C of NGC's licence and will provide for greater transparency of NGC's charges and for formal consultation on changes to its charges and the principles underlying those charges. It will also enable greater scrutiny of NGC's charges by the Authority. The consultation on

these proposed licence conditions is still underway and further consultation papers will be published by Ofgem/DTI in November, December (2000) and January 2001.

- 9.9 Following a full consultation on the final proposals to modify NGC's licence, it is proposed that these conditions will be designated by the Secretary of State using the power granted to him under the Utilities Act 2000 to amend licence conditions where he considers it to be necessary and expedient for the purposes of implementing or facilitating the operation of NETA.
- 9.10 Subject to this designation, it is envisaged that these new conditions will come into effect in early 2001.

10. Generation licences

Market abuse licence condition

10.1 Given the ongoing referral to the Competition Commission regarding this issue, Ofgem feels that it is inappropriate to comment on the market abuse licence condition at this time.

Generating unit availability

10.2 The February draft of this licence condition was a switch on/off condition which Ofgem intended would only apply, in the first instance, to generators depending on their market position. A NETA policy statement was also included to this effect, advising that the condition required some amendment to reflect the introduction of NETA and outlining the purpose of the condition.

Respondents' views

10.3 One industry respondent suggested that the notice period for any 'material' reduction in the capacity of a power station could be three months rather than 6 months, whilst another felt that the condition might inhibit business decisions on the use of generating plant as it presents a substantial regulatory burden. It was also suggested that the Competition Act 1998, the introduction of NETA and the market abuse licence condition (if applied to all licensees) would make this condition unnecessary.

Ofgem's views

10.4 Ofgem proposes to include this condition as a standard licence condition in generation but with switch on/off provisions. Ofgem has also redrafted the condition to simplify the information requirements. Generators already provide NGC with outage information under the provisions of the Grid Code and Ofgem will only require to be informed of any discrepancies, and the reasons behind these, between a generator's forecast to NGC of its outage and its actual outage.

Use of licensee's lines

10.5 In February, conditions relating to the generator providing third party access were reinstated in the draft generation licence in response to comments received from the earlier consultation.

Respondents' views

10.6 One respondent believed that one of these conditions, which refers to the planning standard, is not meaningful or enforceable, as ER P2/5 is difficult to interpret and out of date in respect of generation technologies. The respondent also notes that Guidance Note 1 in the Distribution Code says that ER P2/5 does not apply to customer connections but only to distribution networks.

Ofgem's views

10.7 The ER P2/5 does need to be updated and is being dealt with by the joint Ofgem/DTI working group on embedded generation. However, Ofgem does not believe that the wording of the condition needs to be updated.

10.8 In any case, this condition and the two conditions which relate to the use of the licensee's lines have been removed from the generation licence. Subject to the level of the distribution exemption, generators who distribute on site either will fall within the exemption level or will need to apply for a distribution licence. As such, it is not appropriate to continue to have these provisions in the generation licence.

Individual switch on conditions

10.9 The February generation draft licence contained a number of conditions which contain individual switch on mechanisms within the conditions themselves.

Respondents' views

10.10 Respondents were concerned about how these conditions would be applied and the use of the phrase "such other matters as the Authority thinks fit".

Ofgem's views

10.11 Ofgem will apply these conditions, in the first instance, only to those generators who currently have them in their existing licences. Ofgem has removed the drafting mentioned in paragraph 10.10.

11. Shippers licences

- 11.1 Very few changes have been made to the gas shippers' licence since the February version. The main changes mirror those that are common across all licences such as the removal of duplicate provisions, although some minor drafting changes have also been made.

12. Stakeholders

Introduction

- 12.1 Whilst the standard licence conditions have implications for many stakeholders, the greatest impact is necessarily on licence holders and potential licence holders. Customers, too, can be affected in terms of the service they receive. Ofgem and the DTI are therefore keen to have comments on this consultation from a wide range of organisations. In this section of the paper, we have set out whom we regard as the principal stakeholders, and where appropriate, we have highlighted specific points on which it would be helpful to have comments from particular organisations.
- 12.2 Ofgem is committed to an open, consultative style of regulation. A press release will accompany the publication of this consultation paper, and we should welcome comments from any individual or organisation on the issues discussed here.

The gas and electricity industries

- 12.3 We are seeking views from transmission licensees, generators, PESs, second tier electricity suppliers, gas transporters, gas shippers and gas suppliers (both domestic and non-domestic).
- 12.4 We should be interested to receive the views of industry players on the final proposals in this document, and particularly on the alignment of obligations across gas and electricity.

Consumer representatives

- 12.5 The customer perspective is a key element in the decision making process. Energy consumer representation is going through transition with the GECC due to be established shortly. We are consulting with the Gas Consumers Council, the electricity consumers' committees, and the Chair Designate of the GECC.

12.6 We should welcome comments from consumer bodies on the alignment of the customer protection provisions between gas and electricity and on the split of the Social Action Plan obligations between supply and distribution/transportation.

13. Next steps

- 13.1 Ofgem and DTI will consider the responses received and amend the standard licence conditions accordingly. The final versions of the new standard licence conditions will be available in January 2001 for determination thereafter by the Secretary of State.
- 13.2 The deadline for responses to this consultation is Friday, 8 December 2000.

Responses should be sent to:

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Appendix 1 – Responses to Ofgem’s consultation on the categories of gas and electricity customers who should continue to benefit from certain regulatory safeguards (“small customer” consultation)

- 1.1 Ofgem received thirty nine responses to its “small customer” consultation. Generally, respondents agreed that the definition of small customer should be the same in gas and electricity, although one respondent was opposed both to the alignment of gas and electricity in relation to the definition of small customers and to the removal of consumption thresholds. Thirty one of the respondents considered that the definition of the customers who should benefit from certain regulatory safeguards should be “domestic customers”, or a subset of this. Eight considered that small business customers should be included in the definition.
- 1.2 The thirty one respondents who supported Ofgem’s proposal included both industry players and consumer bodies. All of the responses received from companies active in the gas and electricity markets expressed support for the proposal to adopt a new “domestic premises” based definition. The proposed definition was also supported by some consumer representatives.
- 1.3 Two of those respondents went further and suggested that the definition of “small customers” could be limited to a sub-set of domestic customers. It was suggested that only those customers to whom supply price controls apply, or those customers below a certain domestic consumption threshold should receive additional regulatory protection.
- 1.4 The eight respondents who did not support Ofgem’s proposals included six of the electricity consumer committees, one trade association and the Energy Savings Trust.
- 1.5 The Energy Savings Trust was opposed to the proposed definition on the basis that it would deprive small businesses of their right to free energy efficiency advice. Energy efficiency advice is available only to domestic customers in gas at present, but is available to all customers in electricity. Other responses suggested that business customers need more technical information, not appropriate to domestic customers, which cannot be easily dealt with in a code of practice. Industrial and commercial suppliers in gas could argue that extending regulation in this area might give rise to

additional costs, but there may be benefit in extending this to all customers in gas given our environmental responsibilities.

- 1.6 Several of those who did not support the proposal made suggestions for a revised definition of small customers. The suggestions included the adoption of a consumption threshold in electricity which could then be used to determine whether a customer would be a 'domestic customer' for both gas and electricity. However, this would require a link between gas and electricity registration systems. It was also suggested that adoption of the definition used by Customs and Excise to identify customers paying VAT on energy at 5% would ensure that the additional safeguards continue to apply to very small businesses.
- 1.7 Two of the electricity consumer committees maintained that consumption based definitions should be adopted in both electricity and gas. Such an approach would, of course, maintain the existing unsatisfactory position where a customer could receive additional protection in respect of one fuel but not the other.
- 1.8 One trade association considered that small businesses still needed protection and suggested that the proposed definition of "small customers" is amended as follows: "premises occupied **or able** to be occupied wholly or mainly for domestic purposes".
- 1.9 The consultation document also invited views on whether maximum resale prices for gas and electricity should be set for all customers or should be limited to a category of customers. At present, maximum resale prices are set in gas for all customers and in electricity for "designated customers". The current electricity arrangements require an actual price to be fixed through a determination, these prices vary across the regions as they are tied to the local PES tariff and must be amended each time the tariff changes. The current arrangements in gas are that the maximum resale price is related to the cost paid by the landlord. The current electricity arrangements must be replaced due to the abolition of the PESs and their tariffs. The Utilities Act 2000 has copied the current gas provisions into electricity and therefore the maximum resale price in both gas and electricity could be tied to the landlord's costs, if desired.
- 1.10 The consultation paper proposed that the application of maximum resale price should be limited to domestic customers. Those respondents who provided views agreed that the

maximum resale price should only apply to domestic customers. However, this will result in small businesses losing protection against the maximum price that their landlord can charge for the energy they consume.

- 1.11 The majority of respondents recognised that it would be necessary to make some system changes to take account of any new definition and that changes may also be necessary to existing industry agreements. It was generally recognised that changes would be required to the registration systems of the gas transporters, to enable them to identify “domestic customers”.
- 1.12 Three of the respondents who are active in the gas market indicated that the proposed definition would require major changes to be made to IT systems, processes and existing industry agreements. In particular, it was indicated that major changes would need to be made by gas transporters. Two stated that the high number of IT and system changes resulting from initiatives such as the climate change levy, meter unbundling and NETA mean that implementation would not be possible within the proposed timescale. One respondent suggested that the changes could not be made before 2002 at the earliest.
- 1.13 Transporters have indicated that the levels of changes that may be required would make the early 2001 deadline feasible. One transporter did however state that its ability to meet timescales was dependent on receiving early notification of the final requirements and also on the relative priority that Ofgem attaches to the project. Some changes may be required to existing gas industry agreements, but many of the respondents did not expect this to be an unduly onerous task. Gas suppliers will have to provide transporters with data on which sites are domestic, but suppliers already have this information.
- 1.14 In their responses, the PES supply and/or distribution businesses indicate that the proposed definition could be introduced, in electricity, in early 2001. They do not anticipate that any major changes will be required to their registration systems or to existing industry agreements. However, these statements have been made on the assumption that the current 01 and 02 profiling mechanisms will be used in electricity.

Appendix 2 – Responses to Ofgem’s consultation on the non-discrimination provisions in the gas and electricity supply licences

- 2.1 Respondents generally agreed with the factors Ofgem had considered when assessing the options for the non-discrimination conditions. Two consumer representatives were concerned that Ofgem’s criteria did not specifically consider the interests of customers, while specifically considering the regulatory burden faced by suppliers.
- 2.2 No respondent specifically supported the option of retaining the current conditions, unamended. Respondents were concerned that this option would delay pro-competitive offers to customers being brought to market in electricity, thereby restricting competition and innovation. One respondent was concerned that the presence of an advance notice requirement in electricity would disadvantage PESs offering “dual fuel” as compared to BGT in gas. Two respondents were concerned that this option would create confusion between the use of Competition Act 1998 and sector specific powers.
- 2.3 The second option considered in the consultation paper was to amend the current conditions to take account of recent market developments and to achieve better alignment between the gas and electricity conditions. Seven respondents believed that this was the best option for the future non-discrimination conditions. These respondents believed the licence conditions were more flexible and easier to enforce than the Competition Act 1998. Also, respondents believed that sector specific legislation allowed quicker action against anti-competitive behaviour than the Competition Act 1998. The conditions would also be more appropriate to the energy sector than general competition law, which applies to the whole economy. One respondent believed that the duplication of powers was not an important issue, as all suppliers would face the same level of compliance costs.
- 2.4 Generally the respondents supporting the second option agreed with the amendments to the current conditions suggested by Ofgem if this option was followed. However, one respondent did not believe that the advance notice requirement in the electricity condition should be removed as it stopped anti-competitive offers from being brought to market. One respondent was concerned that Ofgem should continue to be pro-active in monitoring supply markets and not rely only on complaints, as customers may not always be sufficiently informed to complain.

- 2.5 The respondents opposing this option did not believe that it provided Ofgem with any additional powers to address anti-competitive behaviour. Respondents believed that amending the conditions and potentially updating them in the future to take account of market developments would be onerous for Ofgem.
- 2.6 The third option consulted on was to remove the non-discrimination conditions from the supply licences, and rely on the powers granted by the Competition Act 1998 to address anti-competitive behaviour. Fifteen respondents believed that this was the best option. These respondents believed that the Competition Act 1998 was adequate to address anti-competitive behaviour, and that this option would allow companies to introduce innovations more quickly, would reduce confusion and inconsistency when both sector specific and competition law potentially apply, would reduce compliance costs for suppliers, and would recognise the convergence of the gas and electricity supply markets. Respondents cautioned that initially the removal of the non-discrimination condition would not reduce the regulatory burden because of the need to understand the Competition Act 1998, which is relatively new. One respondent was concerned that domestic customers would not understand the Competition Act 1998 as well as the non-discrimination conditions, which would affect their ability to submit complaints.
- 2.7 Seven respondents opposed the third option, arguing that competition was not sufficiently developed to rely on the Competition Act 1998. Two respondents did not support relying on the Competition Act 1998 unless Ofgem could confirm that it covered all the behaviour covered by the non-discrimination conditions. Two respondents were particularly concerned that Ofgem would not be able to address anti-competitive behaviour in supply markets as quickly under the Competition Act 1998 as sector specific legislation.
- 2.8 One respondent suggested that the reduction in the number of competitors in the gas and electricity markets showed that competition was not developing well. Respondents were concerned that dominant suppliers still abused their market position and believed that the existing licence conditions provided protection for customers.
- 2.9 In respect of the application of the Competition Act 1998 to the energy sector, five respondents requested more detailed guidance from Ofgem on the application of the Competition Act 1998 to supply markets. One respondent also requested that Ofgem

publish the final energy guidelines by October to allow suppliers to plan for the removal of the non-discrimination conditions.

- 2.10 Two respondents requested clarification on Ofgem's statement in the consultation document that companies could seek guidance or a decision as to whether agreements or conduct would breach either of the prohibitions of the Competition Act 1998 before the agreement or conduct had been introduced. The respondents believed that Ofgem's statement was inconsistent with the guideline, "The Major Provisions"¹.
- 2.11 Two respondents expressed concern that Ofgem would require fees to be paid for guidance or decisions. One of these respondents believed that the acceptance of payments by Ofgem to approve agreements or conduct could be considered to be a bribe.
- 2.12 Four respondents expressed concern that Ofgem's proposals to remove the supply non-discrimination conditions was inconsistent with its introduction of a "market abuse" licence condition to certain generators' licences to prevent the abuse of substantial market power. Respondents were not clear why it was appropriate to introduce additional regulation to the generation market while removing regulation from the supply market. One respondent suggested that Ofgem should introduce a market abuse condition for BGT in the gas supply market.

¹ The Major Provisions, OFT 400, March 1999

Appendix 2 – List of respondents to the consultation on supply non-discrimination conditions

Accord Energy
Amerada Hess Gas
Aquila Energy
British Energy
British Gas Trading
Consumers' Association
Eastern Energy/Norweb Energi
Enron Direct
Gas Transportation Company
Health and Safety Executive
London Electricity
National Consumers Council
National Electricity Consumers Committee
National Energy Action
North East Electricity Consumers Committee
Northern Electric
Npower
Office of Fair Trading
Scottish and Southern Energy
Scottish Power
South West Electricity Consumers Committee
Strathclyde and Central Energy Advice Centres
Seaboard
V-is-on Gas
Yorkshire Electricity

Appendix 3 - List of respondents to consultation on standard licence conditions

1. Amerada
2. Association of Electricity Producers
3. BNFL Magnox
4. British Energy
5. British Gas Connections
6. British Gas Trading
7. Electricity Consumers Committee (South West)
8. Electricity Consumers Committee (Yorkshire)
9. Elf Connect
10. Elf Pipelines
11. Gas Consumers Council
12. Gas Supply Company
13. Gas Transportation Company
14. GPU Power
15. London Electricity
16. Major Energy Users Council
17. MRA Service Company Limited
18. National Electricity Consumers Committee
19. National Grid Company
20. North West Electricity Consumers Committee
21. Northern Electric and Gas
22. Norweb
23. nPower
24. PESs
25. Powergen
26. Scottish and Southern
27. Scottish Power
28. Seeboard
29. Slough Heat and Power
30. Transco
31. Unit Energy
32. Western Power Distribution
33. Yorkshire Electricity