



## **Briefing Document for the Committee of Public Accounts**

**Thursday 17 January 2013**

**Re: Commission for Energy Regulation  
Annual Report and Financial Statements 2011**

## **1. Introduction**

In accordance with the Committee's invitation to examine the Commission for Energy Regulation (CER) Annual Report and Financial Statements for 2011 (the Report), this briefing document has been prepared to provide supplementary information on the Report under review and to give an update on the key developments since its publication including an expenditure update for 2012.

This briefing paper focuses on our principal activities, duties and functions, key tasks for 2011 to 2013, a commentary on financial and operating performance plus a brief outline of corporate governance arrangements.

## **2. Principal Activities**

The CER is the independent body responsible for regulating the natural gas and electricity markets in Ireland as well as aspects of safety in the upstream and downstream energy sectors. The CER's role is to ensure a safe, secure & competitive supply of natural gas & electricity to customers in Ireland. In a world where energy supply and prices are highly volatile, the over-riding mission of the CER, acting in the interests of consumers, is to ensure that:

- the lights stay on,
- the gas continues to flow,
- the prices charged are fair and reasonable,
- the environment is protected, and
- energy is supplied safely.

CER is committed to carrying out its functions in a fair, impartial, balanced and transparent manner. We provide a professional and efficient service to all our stakeholders and act with integrity and impartiality at all times. The CER's Strategic Plan 2010 - 2014 focuses on achieving the five main aspects of our Mission Statement as published on the CER website<sup>1</sup>.

### **2.1 Duties and Functions**

The CER was established under the provisions of the Electricity Regulation Act, 1999, and has taken on significant additional responsibilities since then under various pieces of legislation. Responsibility for the regulation of the natural gas market was conferred upon the CER under the Gas (Interim) Regulation Act, 2002. The Energy (Miscellaneous Provisions) Act 2006 added to the role and functions of the CER, including providing for additional responsibilities in gas and electrical safety. The Electricity Regulation Amendment (SEM) Act, 2007 outlined the CER's functions in relation to the Single Electricity Market (SEM) for the island of Ireland. Uniquely this market is regulated by the CER and the Northern Ireland Authority for Utility Regulation (the Utility Regulator). More recently, the Petroleum

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<sup>1</sup> <http://www.cer.ie/en/about-us-strategic-plan.aspx>



(Exploration and Extraction) Safety Act, 2010 also has given the CER significant new and important functions in the area of petroleum exploration and extraction safety.

The CER's statutory duties include promoting: competition in gas and electricity markets; safety on the part of electricity and natural gas undertakings; the continuity, security and quality of supplies of electricity and natural gas; and renewable, sustainable or alternative forms of energy. The CER must also take account of the need to: protect the environment; encourage efficient use and production of electricity; and take account of the needs of customers, the disadvantaged and the elderly.

## **2.2 Work Programme for 2011 to 2013**

### **2.2.1 Work Programme for 2011**

The 2011 Report provides an overview of the CER's key work items and achievements in the year. The main focus of the report is on the "8 Key Tasks" for 2011 which were viewed as being the CER's most important strategic tasks for the year. These key tasks were spread across the CER's main business areas. They are to help drive forward the market reform agenda in Ireland, taking into account the three pillars of sustainability of supplies, security of supplies and competitiveness of supplies. The CER's strategy in delivering these key objectives (as well as all of our other on-going work tasks) was framed against the Government's energy policy objectives. The tasks are as follows, with full details provided in the 2011 Report;

- Key Task 1: Retail Price De-regulation and Customer Protection
- Key Task 2: Progress all-island Common Arrangements for Gas (CAG)
- Key Task 3: Progress Smart Metering
- Key Task 4: Single Electricity Market (SEM) Development
- Key Task 5: Review of Bord Gáis Networks' Transmission and Distribution Revenue
- Key Task 6: Safety
- Key Task 7: Monitor Gate 3 Connection Offers and Review Uptake of Gate 3
- Key Task 8: Input to EU Framework Guidelines and Implement "Third Package" requirements in electricity/ gas.

The 2011 Report informs on the outcomes against "Key Performance Indicators" (KPI's) which were agreed with the Department of Communications, Energy and Natural Resources as part of the Department of the Taoiseach's "Better Regulation" drive.

### **2.2.2 Work programmes for 2012 and 2013**

The year 2012 saw many policy developments from the CER. These included setting out the revenue for Bord Gáis Networks from 2012 to 2017, with a key objective being "value for money" for the gas customer. We also, together with Government, decided on a national roll-out of smart energy meters to homes across the country. Working with our partners in the Northern Ireland Utility Regulator, we continued to progress the integration of the wholesale

electricity market into the EU-wide electricity target model. We also finalised the high-level design of the new petroleum safety framework.

The CER work programme for 2013 plans to, further progress these areas and to commence other work. In particular, we plan to manage four major projects simultaneously next year, covering both our economic and safety functions, namely (i) the continued integration of the SEM into Europe; (ii) developing the roll-out for energy smart metering; (iii) implementation of the petroleum safety framework; and, (iv) creating an economic framework for water regulation (subject to legislation). Given the importance of these projects, there will be a significant increase in expenditure in order to fulfil these duties but every effort will continue to be made to ensure that such increases are kept as low as possible.

Looking first at projects related to our economic energy role; in 2013 the CER and the Utility Regulator will work on integrating the SEM into the emerging pan-European electricity market. This is in order to promote cross-border competition and to meet Ireland's commitment to be part of Europe's emerging internal electricity market, referred to as the "target model", by 2016. In 2013 the Regulatory Authorities plan to publically consult and decide on any changes to the high-level design of SEM that will be made in order to facilitate the integration of SEM into the target model. We encourage all interested parties to fully engage in this important consultative phase. In early 2013 the CER will also decide on the next steps in relation to all-island gas arrangements, following the completion of an analysis of all-island gas balancing and a cost-benefit study.

The CER's smart metering roll-out programme is an important national energy infrastructure initiative and the focus of 2013 will be on firming-up on the high-level design and requirements for a roll-out programme, with the involvement of all relevant stakeholders. The current plan is for a national roll-out of smart meters to commence from 2015.

Turning to the petroleum safety project, in 2013 the CER will develop the detailed policies, procedures and guidelines which underpin the petroleum safety framework, with public consultations and decisions in areas such as safety case guidelines and compliance procedures. Based on this, the CER expects the framework to come into full effect in November 2013, an important milestone from when onwards the CER will be in a position to assess petroleum exploration and extraction safety cases from a safety perspective.

The CER's role will expand significantly this year when, following the passing of legislation, the CER is appointed as Ireland's economic water regulator. Creating an economic framework for regulating Ireland's public and waste water system will be an important project for the organisation in 2013, with a view to developing a high-quality, cost-efficient, and economically-sustainable water system.

In addition to these projects, in 2013 the CER will keep moving forward with key operational work. On economic matters this includes retail monitoring and customer protection so that energy customers can get the most out of retail competition. We are also working to ensure



that any disconnection moves by suppliers are strictly a last resort. On networks, we are progressing work-streams to help facilitate the increased connection of renewable generators (typically wind farms) in Ireland, already ahead of many EU countries at circa 20% of electricity consumption. More broadly, active engagement in European economic regulatory matters is becoming increasingly important for the organisation's work, covering issues such as ACER Framework Guidelines and Network Codes, all of which have the potential to impact on the Irish energy sector. In relation to safety, in addition to the petroleum project, the CER will continue to implement our operational downstream functions in gas and electrical safety, with a priority on enforcing the gas safety framework and safety regime for electrical contractors.

### **3. Financial and Operating Performance**

#### **3.1 Funding by Levy on Industry**

The CER is not funded by the Exchequer, the Electricity Regulation Act, 1999 (as amended) confers on the CER the power, to make regulations prescribing an annual Industry Funding Levy to be paid by regulated gas and electricity industry participants to the CER.

Initially the proposed principles for administration of the levies for the relevant calendar year and subsequent years were communicated to all market participants through a consultation process. The CER prepares an annual estimate of operating and capital expenditure required for the subsequent year by sector. The Commissioners review the annual capital and operating budgets, work programme, procurement plan, management accounts, key project business plans, and banking arrangements. The main purposes of this budgeting process relate to planning and control, and supporting the achievement of strategic plans. This process also defines the annual funding required which sets the amounts to be recovered from Industry participants i.e. Levy Orders issued by Statutory Instrument.

In order to determine the amount that must actually be collected from industry, an annual adjustment is made for any under/over recovery of costs in the prior year. In previous years, the Commission had offset significant cumulative operating surpluses on an annual basis against the Gas and Electricity Levy Orders to be recovered. This resulted in a substantial reduction in the levy income recovered for the applicable accounting periods, 2009 to 2011.

In 2011, our income was €9.09million. The levy recovered from respective sectors is outlined below;

- The electricity levy at €6.240million equates to 69% of the total levy. The relevant undertakings that are liable to pay the levy are any person engaged in performing the function of generation, transmission, distribution and supply of electricity.
- The gas levy at €2.804million equates to 31% of the total levy, the relevant natural gas undertakings that are liable to pay the levy are any person engaged in transmission, distribution or supply of natural gas in Ireland.

Pending designation of petroleum activities and implementation of the safety framework for levy purposes, the CER have secured a short term commercial loan facility to fund petroleum safety activities, as consented to by Ministerial approval. The CER intends to recover the costs of its activities on petroleum safety, in accordance with Section 20 of the Electricity Regulation Act 1999 as amended by the Petroleum (Exploration and Extraction) Safety Act 2010. The CER will publish its decision on how it will levy the petroleum industry in Q1 of 2013.

In 2012, the levy recovered from respective industry participants is outlined below;

- The electricity levy at €6.76million equates to 68% of the total levy,
- The gas levy at €3.26million equates to 32% of the total levy.

### 3.2 Expenditure

Total operating expenditure in 2011 was €9.756million - a decrease of 2% on the previous year's expenditure. The new regulatory function of Petroleum Safety amounted to €1.12million (11.47%) of the overall total. Of this overall total, 92% went on the three main categories of spend; staff costs- payroll plus non-payroll (59%), office accommodation (10%) plus project fees (24%). Costs directly incurred by each sector are recorded in the separate accounts of the electricity, gas and petroleum sectors. Shared costs are allocated to each sector in proportion to the staff numbers engaged in the relevant sector. The table below illustrates annual expenditure trends per sector, during the five year period 2008 to 2012;

Function	Year 2008 Actual €'000's	Year 2009 Actual €'000's	Year 2010 Actual €'000's	Year 2011 Actual €'000's	Year 2012 Estimate €'000's
Electricity	6,778	7,025	6,911	5,574	5,427
Gas	4,036	3,408	2,579	3,063	4,050
Petroleum Safety	0	0	441	1,119	1,636
<b>Overall Total</b>	<b>10,814</b>	<b>10,433</b>	<b>9,931</b>	<b>9,756</b>	<b>11,112</b>

Appendix A, attached, provides details of expenditure for 2011 as extracted from the Report and the expected outturn for 2012 in respect of staff costs, overheads and project costs. It should be noted that the estimated out-turn for 2012 is provisional and subject to audit by the Office of the Comptroller and Auditor General. Additionally the schedule excludes year-end adjustments in respect of the re-statement of pension costs in line with FRS17 requirements. For comparative purposes, the 2011 totals exclude the FRS17 pension adjustment.

#### 3.2.1 Procurement

CER have continued to focus on managing our costs. Procurement spend analysis is performed on an annual basis. The main aim of the planning process is to support the achievement of the CER's key objectives and allow concentration of more resources both financial and staff time, on delivering core tasks. This is done by securing best value for money, reducing or managing risk and modernising related business processes by adopting best practice procurement techniques for all bought-in external goods and services. The plan aims to meet the obligations of the public procurement policy framework and in doing so



reinforce the Commission's commitment to effective and efficient resource allocation and service provision.

The annual procurement plan is underpinned by an analysis of expenditure on goods and services per category and the procurement and purchasing structures which have been well established in CER. The plan sets out practical and strategic aims and objectives for improved procurement outcomes and appropriate measures to achieve these aims. This plan builds on the recommendations set out in the previous procurement plans as prepared annually since 2009. In addition to compliance with legislative requirements, the procurement function supports the Commission's business objectives and is focused on delivering the optimal outcome to tendering processes issued on behalf of the organisation. To ensure the CER is focused on delivering value for money outcomes the procurement processes and staff capabilities are reviewed annually to ensure purchasing personnel, have the necessary capacity to operate in line with best practice.

### **3.3 Human Resources**

The CER currently has 73 employees (70.6 FTE's) out of an approved total figure of 81 (2012). It is envisaged that this will grow to 85 FTEs in 2013 as the petroleum, safety framework is finalised. The CER is currently in discussion with the Department of Environment, Community and Local Government as well as the Department of Public Expenditure and Reform about the level of resources needed to fulfil the function of being the economic regulator for water. The current positions are split between Economic and Safety Regulation. The HR Department is responsible for implementing and complying with best HR practise across the organisation and is also responsible for Recruitment, Training & Development, Absenteeism, Health & Safety, Risk Management, Pensions Administration and Facilities Management.

Examples of these activities include;

#### *Performance Management:*

A PMDS has operated in CER since the establishment of the organisation. Individuals are set yearly objectives based upon the organisations business plan with reference to our Five Year Strategic Plan. The PMDS is currently being reviewed and updated in line with newly published DPER guidelines.

#### *Croke Park Agreement:*

The CER remains committed to implementing a number of initiatives under the Croke Park Agreement. These include better human resources management, better business processes and improved customer service.

#### *Work Force Planning:*

This piece of work was carried out in 2012 as required by DPER. It examined the work demands on the organisation and the levels and expertise of the staff required to achieve organisation objectives. The CER has commenced the implementation of its recommendations.

### **3.4 Corporate Governance Arrangements**

The updated Code of Practice for the Governance of State Bodies (the Code) issued by the Department of Finance in 2009, sets out a corporate governance best practice framework which State Bodies are required to adopt. In the interests of transparency and accountability, the CER has incorporated the recommendations into its organisational structure and reporting mechanisms. The Commission as a non-commercial State Body has noted that some aspects of the Code of Practice are not “appropriate” or fully “relevant” to the Commission’s circumstances as per Section 1.1 of the Code. The CER has agreed with the Department of Communications, Energy and Natural Resources on the extent to which requirements are adapted to the CER. The Statement of Best Practice in the 2011 CER Annual Report refers to the Commission’s overall compliance with the Code. A brief update on internal audit plus Audit Committee output in 2012 is outlined below.

#### **3.4.1 Internal Audit**

The CER has an internal audit function, which operates in accordance with the Framework Codes of Best Practice set out in the Code. The work of internal audit is informed by analysis of the risk to which the CER is exposed, and annual internal audit plans are based on this analysis. The analysis of risk and the internal audit plans are endorsed by the Audit Committee and approved by the Commission.

#### **3.4.2 Audit Committee**

The Audit Committee members at the end of December, 2012 are Mr. Tom O’Higgins (Chairperson – external), Commissioner Garrett Blaney, Dr. Paul McGowan and Mr. Tom Mason (external). The Committee’s main functions are to advise on how the Commission is managing key financial and operational risks, to evaluate the effectiveness of internal financial controls, to appraise value for money issues and to monitor implementation of Commission decisions arising from Audit Committee recommendations. During 2012, the Audit Committee met on four occasions and carried out the following functions;

- The Committee reviewed and approved for submission to the Commission Internal Audit Reports on Internal Financial Control, Carbon Revenue Levy Financial Administration, Review of Project Management, a Review of IT General Controls; and a Follow-up review on recommendations per 2011 reports.
- The Committee monitored policy and practice enhancement work by the Commission in relation to IT; and
- The Committee liaised regularly with management in relation to the conduct of risk management and mitigation work within the Commission.



## Appendix A: CER Expenditure for 2011 plus Estimated Expenditure for 2012

### CER INCOME AND EXPENDITURE ACCOUNT (EXTRACT)

	Notes	2011 Total Euro (Audited)	2012 Total Euro (Estimate)
<b>Operating Expenditure</b>			
Direct Wages & Salaries		5,014,968	5,070,825
Pension Costs	1	981,416	1,012,486
Recruitment and Training		72,495	156,548
Travel & Subsistence		122,378	134,190
Office Accommodation Expenses		837,226	874,459
IT & Communications		324,573	343,549
Office Service Costs		33,745	35,286
Insurance Premiums		58,640	103,653
Advertising		115,128	70,325
Consultancy, Professional & Legal Fees		2,268,388	2,812,102
Audit fees plus Internal Audit Fees		36,433	43,357
Other Expenses		69,357	67,540
Interest Payable		33,307	127,434
Depreciation		258,955	260,538
		<b>10,227,010</b>	<b>11,112,293</b>
<b>Capital Expenditure</b>		<b>57,878</b>	<b>50,047</b>

Note: The schedule presented for CER Expenditure for 2012 gives the Commission's interim expenditure as extracted from the CER Management Accounts which are prepared within 5 working days of the month end. The amounts presented are provisional and may be subject to change as adjustments may be required to finalise the Income and Expenditure Account resulting from the analytical review of the interim and final accounts by senior management. Additionally the schedule excludes year-end adjustments in respect of re-statement of pension costs in line with FRS17 requirements<sup>2</sup>. All 2012 figures are provisional and are subject to audit by the Office of the Comptroller and Auditor General.

<sup>2</sup> Schedule Note 1: For comparative purposes, the 2011 totals exclude the FRS17 pension adjustment.