

ANNUAL REPORT 2006/07



niaer

**Northern Ireland Authority
for Energy Regulation**



ANNUAL REPORT 2006/07

of Northern Ireland Authority
for Energy Regulation

Laid before the Northern Ireland Assembly in accordance
with Article 6 (5)(a) of the Energy (Northern Ireland) Order
2003 by the Department of Enterprise, Trade and Investment

niaer

Northern Ireland Authority for Energy Regulation



CONT

Chapter 1

Chairman's Report

4

Chapter 2

Chief Executive's Report

6

Chapter 3

Forward Work Plan 2006/07

9

Chapter 4

Electricity Industry

17

Chapter 5

Gas Industry

21

Chapter 6

Water Industry

26

Chapter 7

Energy Efficiency, Alleviating Fuel Poverty and Reducing Emissions

28

Chapter 8

Corporate Affairs

30

ents





1

Chairman's Report

This report covers my first year as Chairman of the Board of the Northern Ireland Authority for Energy Regulation (the 'Authority'). During this year we made a number of fresh starts, laying foundations for future achievement.

We work hard to ensure openness and transparency of our decision-making processes. We aim for an approach where all key stakeholders understand the process by which we will take a decision; know how they will be consulted; and understand the basis for our decisions. Stakeholders might not agree with us... but there should be no surprises.



This is particularly important in the context of the restoration of devolved government in Northern Ireland. As a non-Ministerial government department, we provide a resource to the whole Executive and indeed to the whole of Northern Ireland society. We offer an independent centre of expertise, solely focused on promoting consumers' long and short-term interests.

During 2006/07 we put in place a new top team in the Authority, with new Board members and a new Chief Executive. This team pools decades of experience: as senior managers within utility companies; as regulators; as non-executive directors in private, public and third sectors; as operators in the Republic of Ireland, GB, the rest of Europe, and around the world.

This experience is a particularly valuable resource as Northern Ireland's utility industries face a period of rapid change. Promoting competitive energy markets, securing public support for efficient water investment, and re-orienting the utilities to develop sustainably are enormous challenges. Northern Ireland will need to harness all available expertise to meet these challenges, and innovative policy approaches will be required.

As the UK's only multi-utility regulator, we see great scope for creative cross-fertilisation between different industry traditions. We look forward to harnessing these lessons, learning together with the Executive and Ministerial departments, for instance, as we use public consultation to consider the case for universal water metering.

We are greatly assisted by our developing relationships with other regulators and agencies. In particular, our collaboration with the Commission for Energy Regulation to develop the Single Electricity Market has been a flagship project for the year. We look forward to harnessing the momentum of collaboration to address gas and other projects in the coming years.

I would like to finish by paying tribute to the hard-working and able staff of the Authority. The substantial achievements laid out in this report were enabled by many individuals' very hard work and creativity. A year of change brings upheavals, and it is to the great credit of our colleagues – both those who have been with us for some time, and new arrivals – that the organisation has maintained its focus on consumer benefit and delivery.

In 2007-08 there will be further change as the Authority assumes regulatory responsibility for Northern Ireland's water and sewerage service. To mark this further development, the Authority will, from 1 April 2007, become the Northern Ireland Authority for Utility Regulation (the Utility Regulator).

Peter Matthews
Chairman, Northern Ireland Authority for
Energy Regulation





2

Chief Executive's Report

Northern Ireland's utility sector is changing faster now than for many years, and the pace of change seems likely to continue. This has meant an exciting and busy year for the Authority.

We see, for instance, new ownership structures. With Arcapita's purchase of the Viridian Group, private equity owners have come to play a larger role in Northern Ireland utilities than in the rest of the UK.



As regulator, we have maintained a fundamentally “ownership blind” stance. We inserted an effective ring-fence into Northern Ireland Electricity’s (NIE) licence while it was still owned by a publicly quoted company, and the Arcapita takeover led us to make only minor changes. We have also worked effectively with Terra Firma, the owners of Phoenix Natural Gas. Our November 2006 agreement with Phoenix established a long-term framework for that company’s financing, and so laid a sound platform for continued expansion of the gas industry around Greater Belfast.

The November agreement also foresaw the transfer of Phoenix’s transmission assets to a low-cost financing structure. This kind of mutualisation continues to serve NI consumers well in reducing the costs of the Moyle interconnector and Scotland to Northern Ireland pipeline (SNIP), and we will continue to ensure effective regulation and governance of mutual structures.

We do, however, expect ownership and management structures to be compatible with competitive energy markets. During the year we confirmed, along with the Department for Enterprise, Trade and Investment (DETI), our expectation that the electricity system operator System Operator of Northern Ireland (SONI) would be divested and not be in common ownership with players in the competitive sectors. We would expect to maintain this stance in the future. We have also implemented legal and managerial unbundling in all the energy companies.

In addition, the year saw the creation of a government-owned water company. This is a new structure for Northern Ireland, and we look forward to the Executive’s consideration of the Hillyard Review as to whether it is recommended as a long-term option. In the meantime, we are concentrating our efforts on developing the building-blocks of effective regulation that will be applicable whatever ownership or funding structures are adopted. This means base-lining the company’s strategic business plan to ensure it is acceptably ambitious, and can be effectively monitored. It means preparing enforceable customer service standards, and effective enforcement of all of Northern Ireland Water’s licence obligations. It means assessing what sustainability means in the water and sewerage context, and in particular considering the case progressive tariffs, to protect vulnerable customers and create appropriate demand signals.

Not only is ownership changing, but so too are the market structures for utility companies. Market opening continued during the year and will be complete by the end of 2007. The Single Electricity Market (SEM) programme is essential to enable market entry by new generators and suppliers. We hope that in coming years we will see increasing levels of competition for all customers, an aspiration that was at the core of March’s Memorandum of Understanding (MoU) with the Commission for Energy Regulation (CER). That MoU also stressed the importance of competitive market structures and the continued reduction of dominant market shares; and committed both regulators to developing a transparent, consistent and harmonised approach to wholesale and retail markets in a manner which supports effective competition.

Meanwhile, Phoenix and particularly Firmus are bringing gas to new areas, which offers a triple benefit: economic, environmental and in reducing fuel poverty.



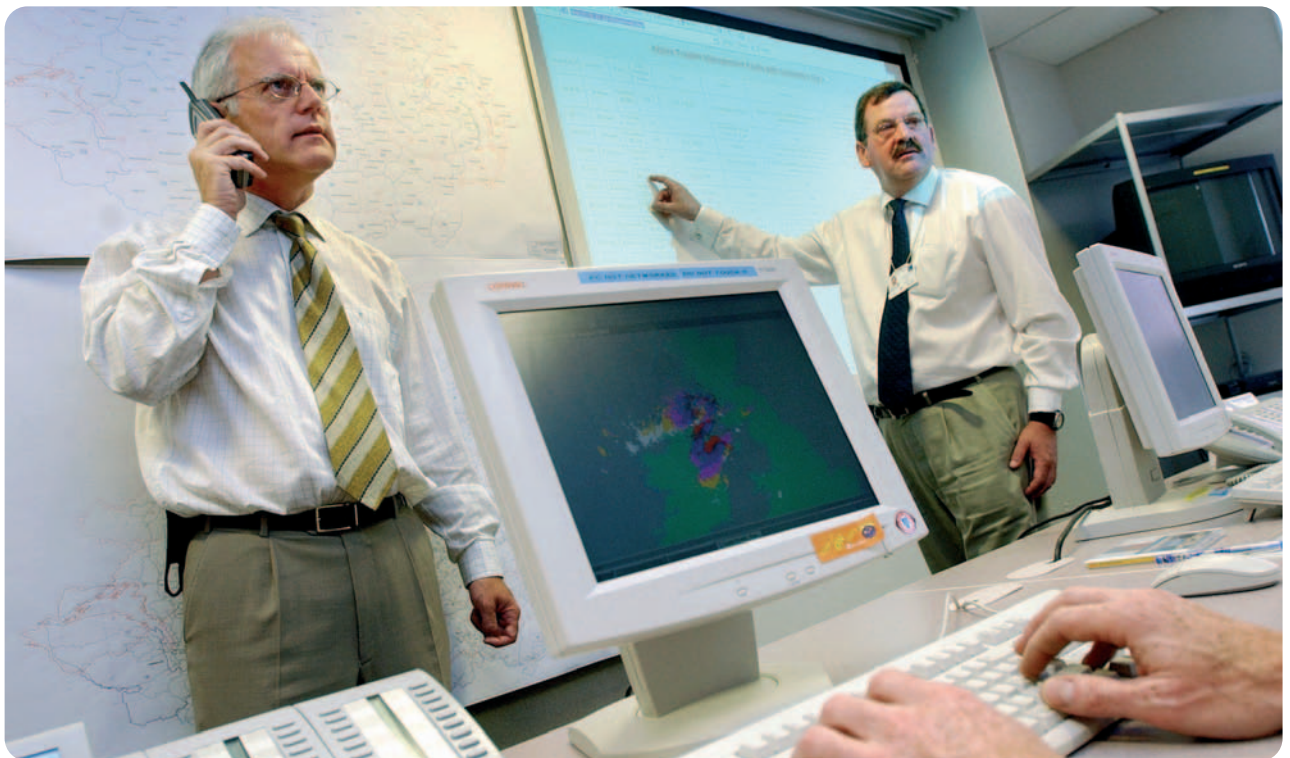
Further extension of the gas network seems to be one of NI's best options to reduce our carbon emissions. As regulator, we devoted considerable attention during the year to simplification of NI network arrangements, and this is an agenda we will continue to pursue on an all-island basis with CER.

This pace of market change creates substantial new challenges for the regulator. During the year, the Department of Finance and Personnel (DFP) undertook an independent review of our required staffing level. The review underlined the need an increase in staffing to meet the range of regulatory responsibilities. We have been recruiting these staff not only from the NI civil service, but also from the private sector. In addition to our existing experienced staff (who aside from our finance team were almost all economists) we have recruited accountants, engineers and people with a business background, bringing in staff who understand the utility sectors and so have a much shorter "learning curve".

The pace of expansion means the Authority of today is a rather different organisation from the Ofreg which began the 2006-07 year. We are looking forward, during 2007/08 to becoming the Utility Regulator, with a new responsibility for regulating water and sewerage services. We are also looking forward to completing our recruitment phase and a period of consolidation at least in Human Resource terms – although I doubt that the pace of industry change will slow.

2006-07 was a year of solid achievements that lay a foundation for the future. I would like to add my thanks to Peter's to the staff who have made this possible. I have greatly enjoyed working with them during the last year, and admire the energy and creativity they bring to our work. Thanks also to our board who provide us with energising leadership.

Iain Osborne
Chief Executive, Northern Ireland Authority for Energy Regulation





3

Forward Work Plan 2006/07

The table overleaf details the targets as set out in our Forward Work Plan for 2006/07 and includes a brief commentary.



Electricity

Project Summary	Outcome/Target	Timescale	Commentary
General			
Regulate and enforce licences	Ensure licence compliance	Ongoing	
Increase the transparency by which costs are reflected in tariffs	Consultation exercise undertaken	February 2007	Achieved
Oversee the Moyle interconnector contracts	Interconnector auctions held	Ongoing	Achieved
Continue to explore the options for the future role of Kilroot Power-Station	Options explored	Ongoing	No progress on Power Purchase Agreement extension
Transmission and Distribution			
Facilitate the separation of the combined Public Electricity Supply, Transmission and Distribution licence held by NIE to comply with EU directive.	New licences granted by DETI	3 July 2007	On target
Agree the functions which SONI will undertake in the SEM as Single Market Operator	Industry contracts to be finalised	31 October 2007	On target
Issue a licence to SONI to comply with EU Directives and its SEM role.	SONI Licence issued	1 July 2007	On target
Facilitate the ongoing work into the connection from Rathlin Island to the mainland.	Approval for expenditure given	31 March 2007	Connection to be completed in Summer 2007
Supply			
Facilitate the opening of the electricity market to all customers by 31 July 2007. This will include, inter alia, approval of programme structure with industry, approving the detailed market design and expenditure by industry participants. Formulating policy where necessary.	Retail market opening to be achieved by target date	1 November 2007	On target



Project Summary	Outcome/Target	Timescale	Commentary
Formulation of a metering policy and programme for Northern Ireland	New policy in place	During 2008	Work postponed until retail market opening achieved
Oversee and maximise the return for customers on the sale of spare inter-connector capacity and review the terms of interconnector trading	Interconnector capacity auctions	Ongoing	Achieved - monthly auctions held
Amend the regulations on meter certifications to reflect updated programme.	Regulations amended	31 March 2007	Achieved - new programme of meter and certification approved
Price Control			
To put in place a new PPB Price Control	Current price control extended	31 March 2007	Achieved - new price control to be set for SEM
To put in place a new SONI Price Control	Current price control extended	31 March 2007	Achieved - new price control to be set for SEM
To establish a price control for the Northern Ireland responsibilities of the Single Market Operator	Establish price control	July 2007	On target
To put in place a new Transmission and Distribution Price Control	New Transmission price control	November 2006	Achieved
To put in place a new NIE Supply Price Control	Current price control extended	31 March 2007	Achieved - new price control to be set for SEM
Single Electricity Market			
Design and create a new single market for the wholesale trading of electricity that is beneficial to Northern Ireland consumers	SEM Go Active	1 July 2007	On target
	SEM Go Live	1 November 2007	On target
Ensure value for money in the procurement and use of external advice to the SEM project	Keep to agreed consultancy budget	31 March 2008	On target
Legislation			
Ensure that appropriate legislation is in place to deliver a competitive wholesale electricity market	Legislation required for Go Active	1 July 2007	Achieved - SEM Legislation passed in Parliament March 2007
	Legislation required for Go Live	1 November 2007	On target



Project Summary	Outcome/Target	Timescale	Commentary
Establish a decision making body that will oversee the regulation of the wholesale electricity market	SEM Committee to be established by legislation	1 November 2007	Power to establish SEM Committee included in legislation
Modeling			
Complete a Cost Benefit Analysis of the impact of new wholesale market on the island of Ireland	Cost Benefit analysis completed	31 March 2007	Achieved - included in NERA Consultants Report published November 2006
Determine the distributional effects of impact of the wholesale electricity market on Northern Ireland	Distributional effects determined	31 March 2007	Included in NERA Report
Publish results of modeling of the potential market outcomes from the new market design	Results of modelling and potential market outcome published	31 March 2007	Included in NERA Report
Capacity Payment Mechanism			
Design an appropriate capacity payment mechanism (CPM) to be included as part of the wholesale electricity market	Appropriate CPM included	31 March 2007	Achieved - decision paper December 2006. CPM design included in March 2007 TSC.
Work with relevant parties to create a Generation Security Standard (GSS) that is compatible with all island market.	GSS created	Ongoing	Ongoing discussions with System Operators on GSS for CPM purposes
Work with relevant parties to determine a methodology to deliver an overall sum of money to be allocated in the capacity payment mechanism	Methodology determined with relevant parties	Ongoing	On target - indicative capacity sum for 2007 published February 2007
Market Power			
Develop market power arrangements that mitigate the impact of market power on the island of Ireland	Arrangements to mitigate impact of market power developed	1 November 2007	On target - directed contracts price, form and allocation – Decision November 2006 Directed contracts quantification methodology- Decision December 2006



Project Summary	Outcome/Target	Timescale	Commentary
Undertake a review of generation ring fencing arrangements	Review to be undertaken	31 March 2007	Review not undertaken accepted NERA report from 2006 for market power purposes
Agree bidding principles and local market power mitigation strategy	Principles and strategy achieved	Completed	Achieved - decision paper September 2006
Establish a Market Monitoring Unit	Fully functional MMU by Go Live	1 November 2007	Decision paper on MMU in SEM December 2006
Trading and Settlement Code			
Finalise a Trading and Settlement Code that will deliver the wholesale electricity market.	Go Live version of code designated by 3 July 2007	3 July 2007	On target TSC version 1.3 – final consultation document published March 2007
Renewable energy and Carbon			
Ensure that the design of the wholesale trading arrangements does not conflict with existing measure to promote the development of renewables	Suitable arrangements to be put in place by 1 November	Ongoing DETI in lead	NIRO legislation to be amended to ensure compatibility
Ensure that carbon emissions are controlled in a manner that is beneficial to Northern Ireland	NI energy industry continues to contribute to Government targets on carbon emissions	Ongoing	NIAER has continued to promote energy efficiency and low carbon energy
Demand Side Management			
Explore the feasibility of demand management schemes in the wholesale electricity market	Feasibility of schemes assessed	31 October 2008	On target - interim decision to run with existing arrangements. SOs to bring forward plans for an integrated all-island approach
Generation Issues			
Issue amended licences for generation.	Amended licences issued	3 July 2007	On target - enduring conditions apply from 1 November 2007



Project Summary	Outcome/Target	Timescale	Commentary
Ensure that the appropriate changes are made to contracts to allow the introduction of the new wholesale electricity market	Contracts to be amended and agreed ongoing	31 October 2007	On target - ongoing work to ensure that the contracts are fully updated
Participant Readiness			
Ensure that market participants are ready to participate in the wholesale electricity market	Multiple work streams monitoring to ensure market readiness	5 October 2007 Self Certification Statements	On target - Go live criteria published in March 2007

Gas

Project Summary	Outcome/Target	Timescale	Commentary
Natural Gas			
To regulate and enforce gas licences to meet our statutory duties.	Meeting statutory duties	31 March 2007	Ongoing
To progress and finalise the Phoenix Transmission and Distribution price controls and decide on the way forward in terms of the Supply business price control.	Finalising price controls and decision on supply business control	31 March 2007	This exercise continues to progress but completion has been delayed until the last quarter of 2007
To ensure appropriate unbundling and business separation is in place for the Phoenix licensed entities.	Unbundling and business separation in place	31 March 2007	On target - this exercise was progressed alongside EU Directive Implementation
To progress and finalise the modifications to the licences to implement the EU Gas Directive.	Licences modified	31 March 2007	On target - modifications successfully progressed and consulted with implementation due in the last quarter of 2007
To progress work with the Gas Market Opening Group to ensure the appropriate environment is created for effective competition to emerge.	Ensure effective competition in place	31 March 2007	Work continues to ensure competition systems in place



Project Summary	Outcome/Target	Timescale	Commentary
Natural Gas			
To review and if necessary amend the Standard Conditions of Gas licences in conjunction with DETI.	Review and amend licences if necessary	31 March 2007	Postponed until resources are available
To progress and finalise the BGE (UK) Transmission and PTL Operational Expenditure reviews.	Finalise reviews	31 March 2007	On target - (BGE (UK) review completed). PTL review to be completed
Progress licence and code modifications to ensure transmission regime continues to operate effectively.	Licence and code modifications progressed	31 March 2007	Ongoing
Finalise the BGE(UK) Transmission licence.	Finalise licence	31 March 2007	Achieved
To conclude discussions with the owners of Phoenix Natural Gas on the long term licensing arrangements.	Conclude discussions	30 June 2006	Achieved
Promotion			
Facilitate the introduction of the South North gas transmission pipeline into the NI system.	Work progressed on South-North transmission	31 March 2007	Ongoing
Work with CER to analyse the benefits to customers of an all-island gas market, including the potential of all-island Gas Capacity Statement	Progress work with CER	31 March 2007	On target - It is likely that the AIP Gas project will be progressed next year
Review rationalisation of NI operational system.	Review took place	31 March 2007	Achieved



Project Summary	Outcome/Target	Timescale	Commentary
Social Action			
Energy Efficiency Levy	To ensure the efficient use of levy funds and agree a report detailing the benefit to electricity customers	Ongoing	Ongoing
Continued development of Social Action Plans	Social Action Plans developed	31 March 2007	Rescheduled - continued to work with Fuel Poverty Advisory Group and GCC. Planned research for 07/08 year before reviewing plans.
Promotion			
To facilitate the continuing operation of a UK wide Renewable Energy Tariffs trading arrangement.	Renewable Energy Tariffs strategy arrangement in operation	Ongoing	Achieved
To administer a Renewable Electricity Guarantee of Origin Scheme	Administer Scheme	Ongoing	Achieved
To administer the Climate Change Levy Exemption Scheme on behalf of HM Customs and Excise	Administer Scheme	Ongoing	Achieved

Corporate Affairs

Project Summary	Outcome/Target	Timescale	Commentary
Social Action			
Put in place an efficient and effective risk management strategy	Risk strategy in place	31 March 2007	Target met
Ensure processes are in place to enable the delivery of a full statement of internal control in respect of the FYE 31 March 2007	Statement in place for 06/07 Resource Accounts	31 March 2007	Target met
Comply with HM Treasury initiative – “Faster Financial Closing” – in respect of annual accounts to complete, audit and publish	Resource Accounts presented on time	HMT timetable	Target met





4

Electricity Industry

Single Electricity Market (SEM)

The Single Electricity Market, the flagship project for the emerging All Island Energy Market as determined by the governments of the Republic of Ireland and the UK in December 2004, is a single set of wholesale electricity trading arrangements for the island of Ireland. This unique development combines two smaller markets to bring competition, security of supply and efficiency benefits to all electricity consumers on the island. Along with improvements in north-south and east-west electricity interconnection, the market is a sensible and practical first step toward longer term British Isles cooperation within a wider UK-Ireland-France electricity market.



The project was initially scheduled to Go-Live on 1 July 2007. Since the beginning of the project a number of key milestones have been met, including publication of the Trading and Settlement Code – the rules by which market players will trade power. During the project the complexity and detail of the issues across two jurisdictions and involving a large number of players have become clearer. The extent of the work required by all parties to deliver the SEM was also crystallised. Following consultation with the Transmission System Operators and the industry, the target date was extended by four months. This was to enable extensive market testing and implementation to run from June to November 2007. Go Active and Go Live will take place on 3 July and 1 November respectively.

The legislation providing the powers to implement the market was delivered on time in March 2007. The legislation included the ability to create a new decision making body, the SEM Committee, to oversee the new market and was underpinned by a Cost Benefit Analysis, which was provided to DETI in December 2006. The design of the Capacity Payment Mechanism for the new market was published in June 2006 with indicative figures being published in January 2007.

Retail Market Opening

The electricity trading system introduced in Northern Ireland at privatisation established NIE's Power Procurement Business (PPB) as the single buyer of electricity from the privatised generators under long-term Power Purchase Agreements (PPAs). Each year the PPB set a Bulk Supply Tariff (BST) which all supply companies, including NIE Supply and Second Tier Suppliers, were required to pay. As a result of these arrangements opportunities for customers to benefit from electricity trading were severely limited.

The situation was changed by the introduction of the EU Directive on the Internal Market for Electricity (IME) which became law in Northern Ireland in July 1999. At this point the wholesale electricity market was liberalised to the extent that the first 26.4% (by demand) of large customers obtained the right to source their wholesale energy (via a licensed Supplier) from a source other than the PPB. The Directive required further market opening to 35% by 2003, to all non-domestic customers by 2005 and for all customers by 2007.

Establishment of the new IT systems necessary to support competition for the estimated 60,000 non-domestic customers was initially planned for 2005, but was delayed until September 2006. During this delay however customer switching continued to be facilitated and all non-domestic customers were able to change supplier.

Following the completion of market opening for non-domestic customers in September 2006 the Authority immediately began work on extending the new trading arrangements to domestic customers, as well as un-metered supplies. This was due to be completed by July 2007 but due to the interactions with the SEM it was decided to postpone retail market opening to coincide with SEM go live on 1 November 2007.

Some of the key milestones that have been met include changes to the retail market procedures, Operational Framework delivery, Business Definition phase, Procurement Process completion, Implementation Partner Design appointment and Implementation and Build phases.

The Authority continues to exercise regulatory oversight over the systems and expenditure necessary to comply with the Directive. Extending real choice to customers for whom it is economic to switch supplier remains a key priority for the Authority.

Price Controls

Negotiations continued during the year on the structure of the new price control for the Transmission and Distribution (T and D) Business. The T and D business is NIE's largest regulated business.

The Authority published final proposals for the price control in a consultation paper in June 2006. These proposals were agreed with NIE and a decision paper was published in September 2006. Licence modifications were made to ensure that NIE was adequately ring-fenced and that financial safeguards reflect those of GB regulated companies.

Licence modifications were also drafted and put in place to implement the new Price Control, which is set for five years commencing April 2007. The main points of the Price control are:

- NIE network charges capped at the previous year's level (before inflation);



- A £12 million network investment programme during the 5 year price control period;
- A £13.2m reduction in what customers will pay for the required investment programme, and a £4.2m one-off cut in operating expenses during 2007-2009;
- In line with the regulatory arrangements that apply to the Distribution Network Operators in Great Britain, new protection for customers in the event of an NIE take-over i.e., tax benefits of higher debt levels will be returned to customers, and stronger protection of NIE's financial stability, regardless of ownership (the "ring fence");
- Increased SMART (Sustainable Management of Assets and Renewable Technologies) programme to boost renewables and research projects;
- £1m vulnerable customers fund to target fuel poverty, funded by NIE shareholders, not customers.

The Authority took the view that the final proposals represented a balance of between necessary investment for the long term and cost reduction for the short term. The new control will also increase customer protection at a time of unprecedented take-over action in European utilities.

The Price Controls for PPB and SONI (the System Operator of Northern Ireland) expired in March 2006. It was agreed that they should continue substantially in the same format until the start of the SEM in November 2007. The NIE Supply Price Control also expired at the end of March 2006. This was also extended until the start of the SEM, but any adjustments to the underlying revenue entitlement would be applied from April 2007.

In conjunction with CER, the Authority commenced work in establishing a price control for the Single Market Operator (SMO), which again will apply from November 2007.

Tariffs

During the period of this report, the Authority undertook a wide consultation on tariff transparency and timeliness. The tariff consultation was taken against a background of dissatisfaction from suppliers and customers with the lack of transparency in tariff formulation and the timeliness of their publication.

Many of the problems with tariffs will be solved with the advent of the SEM, including difficulties with BST and non-

BST sales, out of market legacy costs on the Public Services Obligation (PSO), Balancing Charges and the Renewable Output Factor (ROF) arrangements.

In the interim, the Authority decided that NIE must adequately demonstrate that all costs are appropriate before they can be passed on through tariffs.

The Authority also decided that it would not approve PSO charges until PPB adequately demonstrated to the industry that they are legitimate and that their calculation can be clearly understood. The Authority organised a workshop to facilitate this.

Over the past few years, the gap between make-up and spill prices has increased with the advent of secondary make-up multipliers. Many industry participants felt that the level of make-up and spill charge did not accurately reflect the true cost to PPB and sought a reduction in the spread of the prices. The Authority has acted to ensure that make-up and spill prices accurately reflected the underlying costs or avoided costs of their generation and has decided to remove secondary multipliers from balancing charges.

The ROF scheme was devised as a means of allowing small renewable generators to avoid make-up and spill charges on a daily basis thus removing short-term imbalance risk. Instead, initially, suppliers had to provide 120% of customer demand with renewable electricity, and the additional 20% was deemed to cover the costs to NIE associated with balancing this electricity in real time. The arrangements were amended in 2005 due to additional government green assistance when 'ungrandfathered' plant was subject to a new ROF factor of 60%.

Following consultation, in which the Authority received submissions from several wind generators indicating that the 60% rule makes the scheme uncompetitive and that the true cost of make-up and spill without secondary multipliers is still in the region of a 20-30% cost lift across the year, the Authority instructed NIE to revert to a 20% ROF factor for the seven months commencing 1 April 2007.

Interconnectors

Northern Ireland has two main interconnectors: one connecting it with the Republic of Ireland (the North-South Interconnector) with a tradable capacity of 330MW and one connecting it with Great Britain (the Moyle Interconnector) with a tradable capacity of 400MW. The trading direction on



the North-South Interconnectors is exclusively export (from Northern Ireland to the Republic of Ireland) while the trading direction on Moyle is predominately import (GB to Northern Ireland).

Auctions for capacity on both interconnectors, are administered by SONI in conjunction with the Authority. In November, the Authority published a consultation paper containing proposals on auction methodology, reserve prices and restrictions on capacity. A subsequent decision paper was published in December to apply for auctions from April 2007 until the start of the SEM.

Regulation of Incumbent Suppliers under SEM

In collaboration with CER, the Authority issued proposals regarding the strategy for the regulation of NIE and Electricity Supply Board (ESB) in light of the emerging market structures of the SEM.

The existing market structure will be replaced by a new licensing regime. For supply, a common form of licence will be used in each jurisdiction. However, this will include special conditions for those supply entities that continue to fulfil the role of a Public Electricity Supplier (PES). In the Republic of Ireland, ESB Customer Supply will be designated as the PES, while in Northern Ireland NIE Supply will be under similar obligations, even though the concept of a PES will be phased out.

These additional licence conditions will encompass acting as a supplier of last resort, undertaking a Universal Supply

Obligation, undertaking the purchase and sale of contracts for difference and being subject to an Economic Purchase Obligation (EPO) for wholesale electricity supplies. These supply companies will have their businesses strictly ring-fenced from related undertakings and affiliates.

European Regional Market

Regulators in UK, Ireland and France have been working closely with the aim of creating a regional electricity market. Other groups of regulators are doing the same with the long term goal of a European wide electricity market.

During the period of this report there have been consultations relating to wholesale market development, balancing arrangements and congestion management.

The Northern Ireland market is already fairly transparent in that information is freely available to participants. The balancing consultation was not relevant to Northern Ireland as the SEM will operate a day-ahead rather than a within day market. Changes need to be made to the Moyle Interconnector trading arrangements in line with congestion management, but this will be a post-SEM issue.

SONI Divestment

Research continued into the most appropriate way of divesting the SONI from the Viridian group. The SONI Price Control, once set, should give a better indication to any potential buyers as to the company's true value.





5

Gas Industry

Brief background to Northern Ireland's Natural Gas Industry and Licences

Natural gas first arrived in Northern Ireland in 1996 and has since brought considerable environmental, economic and social benefits to Northern Ireland. It is the least polluting fossil fuel and its availability in an area provides greater fuel choice for industry. Natural gas also provides domestic customers with the opportunity to convert from inefficient central heating systems to highly efficient gas condensing boilers and in due course to domestic Combined Heat and Power (CHP). There are also two gas fired power stations in Northern Ireland, Coolkeeragh Power Station in Londonderry and Ballylumford Power Station near Larne.



The broken blue lines in the above map show Northern Ireland's gas transmission infrastructure. Currently there are three Designated Pipeline Operators (DPOs) of NI's natural gas transmission infrastructure, these are:

1. Premier Transmission Limited (PTL) who operate the Scotland to Northern Ireland (SNIP) pipeline. PTL is licensed to convey gas from the low water mark at Castle Robin Bay to the pressure reduction station in Ballylumford power station. PTL is owned by Northern Ireland Energy Holdings, a not for profit company with a 100% debt finance structure.



2. Phoenix Natural Gas (PNG) who are licensed to convey gas to and within the Greater Belfast and Larne areas. They own and operate the Ballylumford to Torytown pipeline (BTP) and the Lough Crossing pipeline. The BTP runs from Ballylumford to Torytown (which is just north of Belfast) and the Lough Crossing takes the gas on to Knocknagoney in North Down. PNG is 100% owned by Kellen Acquisitions Ltd, a subsidiary of the Terra Firma private equity fund. Kellen purchased Phoenix's former owners East Surrey Holdings Ltd in October 2005.
3. Bord Gais Eireann Northern Ireland (BGE NI) who are licensed to convey gas in the North West Pipeline, which runs from Carrickfergus to Coolkeeragh Power station in the north west of the province, and the South North Pipeline which runs from Gormanstown in Co Meath to connect with the North West pipeline at Ballyalbanagh in Co Antrim. BGE NI is a subsidiary of BGE UK which is owned by Bord Gais Eireann, the state owned gas company in the Republic of Ireland.

There are two operators of the Northern Ireland gas distribution infrastructure which are;

1. PNG who, in addition to the above transmission pipelines operate the distribution network in the Greater Belfast and Larne areas; and
2. BGE NI (Distribution) Ltd known as Firmus Energy Distribution Ltd. who are licensed for the conveyance of gas within the towns along the route of the North West and South North Pipelines. Firmus Energy Distribution Ltd. is committed to the construction of distribution networks in the towns of: Ballymena, Ballymoney, Coleraine, Londonderry, Limavady, Antrim, Armagh, Banbridge, Craigavon and Newry.

In addition to this, several companies are licensed to supply gas within Northern Ireland. These include;

a) For the Power stations:

British Gas Trading (BGT), which is licensed to supply gas within Ballylumford power station. Premier Power and NIE also hold licences to supply gas within Ballylumford power station. Bord Gais Eireann Energy Supply holds a licence to supply gas within Ballylumford power station and



Coolkeeragh power station. Coolkeeragh (ESB) holds a licence to supply natural gas within Coolkeeragh Power Station.

b) For the Greater Belfast and Larne Areas

PNG's licence is a combined conveyance and supply licence which allows it to supply gas within the Greater Belfast and Larne areas (see above for details of the conveyance licence). Viridian Energy Supply Ltd. (Energia) and Firmus Energy Supply also hold licences to supply gas within the Greater Belfast and Larne areas (where PNG does not hold exclusivity).

c) For other areas within Northern Ireland

BGE Northern Ireland (Supply) Ltd, known as Firmus Energy Supply Ltd, holds a licence to supply gas within the towns along the route of the North West and South North pipelines.

Gas Transmission Developments within the Year

South North Pipeline

BGE (Northern Ireland) undertook construction of the 156km South-North pipeline (SNP) in March 2006. The pipeline was successfully commissioned on schedule in October 2006, and connects the transmission networks of the Republic of Ireland and Northern Ireland for the very first time, providing a second gas route to Northern Ireland. The pipeline runs from Gormanston in Co. Meath to Ballyclare in Co. Antrim and facilitates construction of the gas networks to seven more towns - Antrim, Armagh, Banbridge, Craigavon, Lurgan, Newry and Portadown.

Following the commissioning of the SNP, agreement was reached between Bord Gáis Éireann (BGE) and Premier Transmission Limited (PTL) to allow their interaction in the event of an emergency thus improving security of supply for Northern Ireland.

Rationalisation of Northern Ireland Transmission Arrangements

With the completion of the SNP in October 2006, the Authority identified possible opportunities to rationalize and streamline the existing arrangements in the Northern Ireland Gas Transmission Network.

The Designated Pipeline Operators (DPOs) presented to the industry their proposals for 'streamlining' and worked with industry and the Authority on the best way forward to implement these proposals in the most efficient and cost effective way. Streamlining was approved by the Authority on 30 March 2007 and saw the introduction of a single balancing zone on the Postalised Network involving free-flow at Carrickfergus which in the short-term will reduce balancing actions and increase capacity, delaying the need to book capacity for NI on the Irish interconnectors. The completion of the SNP also saw the introduction of the Lisburn offtake and the appropriate arrangements to facilitate this offtake.

Other benefits of streamlining include rationalization of shipper arrangements, increased and more competitive balancing sell options, and more effective operator-to-operator communication. The main focus going forward is for the Authority to continue to monitor potential for further rationalization that will benefit suppliers and consumers.

BGE (Northern Ireland) Price Control

The Authority began discussions in December 2006 with BGE (Northern Ireland) regarding their 2007/08 to 2011/12 Price Control, the two aims being to set their Allowed Operating Expenditure for gas year 2007/08 and the following four gas years and to set their cost of debt going forward for five years from 1 October 2007.

It is intended that the price control will be finalised in July 2007 for the purposes of determining the BGE (Northern Ireland) Forecast Required Revenue and the setting of the Postalised Tariff. The aim for the Authority will be to set a fair and reasonable position which allows BGE (Northern Ireland) to finance its regulated activities while ensuring that NI gas customers benefit from efficient financing and operations.

Mutualisation of Phoenix Natural Gas Ltd Transmission Assets

In November 2006 the Authority reached agreement in principle with Phoenix Natural Gas Ltd (Phoenix) on a new licence framework. Part of this proposed agreement was that Phoenix would sell their transmission business.



The first issue for the Authority in approving the proposed sale of the Phoenix transmission assets is to ensure that it provides measurable benefits to customers and the Utility Regulator examined all options which seek to maximise customer benefits.

One option explored by the Authority is for the new licence for the Phoenix transmission assets to reflect the principles of the Premier Transmission Limited (PTL) conveyance licence. PTL was purchased in 2005 by Northern Ireland Energy Holdings, a not-for-dividend company limited by guarantee. This purchase was 100% debt financed and the PTL licence was designed to reflect this in a number of areas including the required revenue.

The Authority's early assessment of the proposed mutualisation of the Phoenix transmission assets is that will deliver significant consumer savings.

EU Regulation

With regards to EU 1775/2005, following consultation and discussions with industry to understand their needs, to ensure DPO compliance with the regulation and to minimize costs, the Authority decided to prioritise the Transparency requirements of the Regulation. The DPOs have been in discussions with one another to agree the best way forward in order to meet these Transparency requirements and will consult with industry once a standard approach is agreed.

National Transmission System (NTS) Exit Reform

Ofgem are trying to implement reforms to National Grid's (NG) exit regime. The exit reforms propose to make rights to NTS Exit Capacity and Flow Flexibility available to all NTS exit users on a common basis. Ofgem believe that the reforms will generate better investment signals for NG by exposing users to the true costs of NTS exit capacity.

The Authority is currently working to ensure the negative impact of these reforms on Northern Ireland are minimized and have expressed concerns to Ofgem on a number of occasions.

Gas Distribution and Supply Developments within the Year

Price Controls to maximise the benefit to gas customers

The Authority continues to work with PNG Distribution on the third conveyance price control process. The Authority is also undertaking the first ever supply price control. Throughout this process the Authority will seek to ensure that the costs incurred in conveying gas are minimized and that the most efficient business model is adopted by PNG so that costs to consumers are kept as low as possible.

Work also continues with the Firmus Energy conveyance price control. This again will ensure that distribution charges to consumers in the towns along the NW and SN pipelines are kept to a minimum. This will be done through a rigorous assessment of Firmus Energy's planned capital and operational expenditure as well as a detailed examination of its proposed network development.

Gas price reductions

Phoenix made a commitment in October 2006 to review their gas price at the end of the winter 2007 and in March 2007 they announced a 14.6% reduction in their tariffs¹. Phoenix stated the price cut was due to the fall in the wholesale cost of gas over the winter period. Phoenix has made a further commitment to review prices again at the end of summer 2007. The Utility Regulator is satisfied that the reduction announced by Phoenix in March 2007 represents a reasonable adjustment in the light of falling wholesale costs.

Although gas prices in Northern Ireland remain higher than gas prices in Great Britain there are many reasons for this differential including the method and stage of development, size of market and interconnector costs. Gas prices in Northern Ireland compare favourably with those in the Republic of Ireland and are lower in some cases.



New licence granted to Phoenix Supply

On 19 December 2006, Phoenix Supply was granted a new gas supply licence. The granting of the new gas supply licence to Phoenix Supply formed part of the business separation process required to ensure full compliance with the Gas Directive 2003/55/EC.

EU Regulation – Gas Transmission, and Distribution

The publication of Gas Directive 2003/55/EC by the European Commission will have considerable impact on the transmission and distribution of gas in Northern Ireland.

Gas Directive 2003/55/EC allows all gas and electricity consumers to shop around for their supplier meaning their current supplier no longer has to be their only choice. The gas supply market in Northern Ireland was opened on 1 July 2006 for the remaining non-domestic consumers and for

domestic consumers on 1 January 2007. As a result of this, consumers were able to choose an alternative gas supplier from these dates and in 2006/2007 the first non-domestic consumer switched supplier.

DETI enacted on 1 October 2006 the regulations to implement the Gas Directive 2003/55/EC and the Utility Regulator will proceed with the licence modifications in 2006/2007.

Gas Market Opening Group

The Authority has established a Gas Market Opening Group (GMOG) to identify and deal with barriers to competition in the Greater Belfast area gas market². The GMOG continues to work to ensure that the appropriate systems and processes are in place so that the transition to full competition runs as smoothly as possible.



¹ The lower rates were applicable from 31 March.

² Firmus Energy Supply Ltd., have exclusive rights for the supply of gas within the towns along the route of the North West and South North Pipelines.





6

Water Industry

Throughout the year, active preparation was under way for the reform of Northern Ireland's water and sewerage industry. Ministers decided as part of this reform that the Utility Regulator would be appointed as regulator for these industries in addition to our long-standing role in energy. This change was in fact made in the Water and Sewerage Services (Northern Ireland) Order 2006, and the new water powers and duties were due to come into effect on 1 April 2007.



Although we had no statutory water role until the end of the year, we provided advice throughout the year on a consultancy basis to the Department of Regional Development. This role was of particular importance during the elaboration of the new licence for Northern Ireland Water. This licence, in combination with the Order, sets out an extensive regulatory regime providing a range of consumer protections similar to, but more extensive than, the equivalent in England and Wales. In addition, the Authority's Chief Executive issued a personal letter which set out his own expectations about how the new water regulator would use these powers.

Following the passage of the Order, we have recruited a number of staff to undertake water regulation. We have recruited people with water experience from the Department, from Northern Ireland Water, and from the private sector. Mrs Jo Aston was appointed as Director of Water, after a recruitment competition, and was due to commence her role with the Authority from May 2007.





Energy Efficiency, Alleviating Fuel Poverty and Reducing Emissions

Energy Efficiency Levy Programme

Regulatory energy efficiency programmes have been running successfully in Northern Ireland since 1997/8 when the Office for the Regulation of Electricity and Gas introduced the Energy Efficiency Levy Programme (EEL). As initially conceived the EEL was introduced to implement energy efficiency schemes for domestic consumers with the aim of reducing carbon emissions. However with the eradication of fuel poverty steadily moving up the ladder of Government priorities, and as a result of a consultative process in Northern Ireland, it was decided that the majority of levy funding (80%) would be targeted at helping to alleviate fuel poverty by improving poorly heated and inadequately insulated properties i.e. “fuel poverty proofing”. The remaining 20% is available for energy efficiency and emission reducing projects in the domestic and business sectors.



A report is produced annually (available from NIE and on our website – www.niaur.gov.uk) setting out the annual achievements of the levy programme in terms of energy saved, customer benefits, and carbon savings. A report for 2006/07 will be published on our website as soon as it is available.

The types of schemes supported in 2006/07 were:

- Cosy Homes
- Small Business Energy Efficiency Scheme
- Help the Aged
- Age Concern
- Critical Care Scheme
- NiEA Lighting Scheme
- Phoenix Free Boiler and Insulation Scheme
- Fuelstretcher Schools and Sheltered

In addition to the Energy Efficiency Programme, NIE Supply has successfully delivered £16m of lifetime savings to customers through stimulating additional investment in energy efficiency in 06/07. NIE has also successfully achieved the challenging target of supporting 1000 micro renewable installations by March 07.

NIE's renewable energy tariff continues to grow, with approximately 21,500 customers opting for this tariff by March 2007.

Reducing Emissions

Most energy used in Northern Ireland is produced from fossil fuels which release the most harmful emissions. In delivering its objectives the Authority is required by legislation to have regard to protection of the environment. The Authority has sought to fulfill its responsibilities in relation to emissions through a number of initiatives.

The SMART (Sustainable management of Assets and Renewable Technology) programme was developed by NIE in response to a regulatory initiative whereby NIE Transmission and Distribution is encouraged to seek alternatives to the conventional methods of managing and developing the electricity network in NI. Already this initiative has led to the development and full operation in 2005/06 of a major biomass project in Northern Ireland which displaces carbon producing fossil fuel with environmentally friendly renewably generated electricity. In addition, as a by-product, this project has now introduced a new indigenous neutral fuel source into the Northern Ireland energy scene through the annual production of 50,000 tonnes of wood pellets which are in the course of displacing equivalent fossil fuels usage.

Furthermore the SMART programme in 2006/07 supported communities, businesses, schools and a range of other organisations to make a significant contribution to renewable generation and carbon saving with assistance in installing micro renewables in Northern Ireland.

The Northern Ireland Renewable Obligation

This has been the second year of operation of the Northern Ireland Renewable Obligation (NIRO). 2006/07 has seen a significant increase in interest in renewable generation, both large and small scale with many projects coming on line. The NIRO was introduced by the Department of Enterprise Trade and Investment to encourage renewable generation.

The NIRO is managed by the Authority although administered by our sister organisation Ofgem, London, via an Agency Services Agreement between both parties. The reason for this modus operandi is cost and the maintenance of a seamless UK Renewable Obligation. Full details of the second year of operation of the NIRO (i.e. ROCs generated, value of ROCs, ROCs traded, distribution of buy-out fund etc) is available from Ofgem's website (www.ofgem.gov.uk).





8

Corporate Affairs

The 2006-07 year was notable for the preparations for the regulation of the Northern Ireland water and sewerage industries from 1 April 2007 and the emergence of the Single Electricity Market from 1 November 2007.



Appeals, Complaints and Disputes

Consumer protection is a prime responsibility of regulation which is underpinned by legislation in the Electricity, Water and Gas Orders.

Whilst robust price control is an important feature of economic regulation, it is also important that when things go wrong that the customer has redress through an agreed set of procedures that are simple, transparent and fair with a right of appeal.

During 2006-07 specialist staff in the Authority's office worked with colleagues in the new emerging water company, Northern Ireland Water Limited (NIW), and the Consumer Council for Northern Ireland (CCNI) to develop systems, procedures and leaflets to provide an agreed level of consumer protection and information given the planned creation of NIW on 1 April 2007.

By 31 March 2007 systems and procedures were in place to assist customers who wished to formally complain about the level of service that the new emerging water company was delivering.

In addition to dealing with unresolved electricity disputes passed to the Northern Ireland Authority for Energy Regulation from the Consumer Council, the Authority has been working with the Northern Ireland electricity industry on, amongst other aspects of regulation, consumer interests and protection as the industry faces major change from 1 November 2007. In conjunction with NIE and the Consumer Council, the Authority has been looking at the need for revised Codes of Practice for consumers and possible new or revised Guaranteed and Overall Standards of Performance for the significant change that will occur in the electricity market post 1 November 2007.

Resources

Administration

The Energy (NI) Order 2003 ('The Order') established the NIAER ('the Authority') from 1 April 2003 and at the same time abolished the offices of Director General of Electricity Supply and Director General of Gas for Northern Ireland. The Order amended the Electricity (NI) Order 1992 and the Gas (NI) Order 1996 and transferred most of the functions described in those Orders to the Authority. The Order put consumers at the heart of regulation by placing on the Authority one principle objective for Electricity and one

principle objective for Gas. The principle objective for electricity is set out in Article 12(1) of the Energy Order and the principle objective for gas is set out in Article 14(1). In addition the Order transferred the assets and liabilities of the Directors General to the Authority.

Board

The Authority's Board, which was almost entirely replaced during the year under review, is made up of the Chairman, the Non-Executive Directors and the Chief Executive.

Following the retirement of Mr Douglas McIlldoon as Chairman on 31 March 2006 and in line with the decision by the Minister that the role of Executive Chairman would be split into a non executive (part-time) Chairman and full time Chief Executive, DETI appointed Dr Peter Matthews as Chairman of the Authority with effect from 1 April 2006. The Authority subsequently appointed Mr Iain Osborne as its Chief Executive and he assumed his position on 15 June 2006.

As of 31 March 2007, the Board comprised:

Peter Matthews, Chairman
Etain Doyle
Clive Elphick
John Gilliland
Philip Johnston
Christopher Le Fevre
James Oatridge
Iain Osborne, Chief Executive

Recruitment, Training and Development

The Authority members are recruited by DETI on merit through fair and open competition. This ensures opportunities for employment regardless of race, sex, physical disability, religion, or marital status. Most staff are loaned from either DETI or DFP where recruitment activities are carried out by NI Civil Service Commission and/or Departmental Personnel Divisions. Following the completion of the staffing review carried out by DFP, external recruitment competitions were developed. During the course of 2006/07 the Authority ran recruitment competitions for a number of staff, employed directly by the Authority.

Staff training and development needs are agreed with their line manager, and are then reflected in Personal



Development Plans. There was continuing emphasis on the development of necessary specialist skills, for example in the regulatory economics field, and on financial management and IT skills.

Finance and Funding

Resource Accounts

As a non-ministerial Government Department the Authority's funds are voted by Parliament and accounted for on an annual basis through the Resource Account. The published accounts are available from The Stationery Office or can be downloaded from our website (www.niaur.gov.uk).

The net operating cost (see Table 1 below) of running the Authority in the financial year ended 31 March 2007 amounted to £2,590,000 against the Authority's original resource budget as per spring supplementary estimate position of £2,756,000. This resulted in a saving against estimate of £166,000.

The Operating Cost Statement shows that salary costs rose in line with inflation from the previous year - £1,444,000 for 2006/07 against £1,005,000 for 2005/06. The rise in salary costs also reflects an increase in staff numbers.

The percentage of staff costs to total costs has risen slightly from 32% in 2005/06 to 35% in 2006/07 – this is mainly due to the increase in staff resources in the SEM team.

The significant change in other current expenditure is the increase in consultancy costs from £1,500,000 in 2005/06 to £2,071,000 in 2006/07. This can be accounted for by costs associated with the development of the SEM and the significant requirement for technical support to enable the project to be completed within the agreed time frame set by ministers in both jurisdictions.

The Authority's gross expenditure in pursuit of its objectives as detailed in the Statement of Operating Costs by Departmental Aim and Objectives (see Table 2 opposite) was as follows: - £3,352,000 (£2,310,000 in 2005/06) for Objective A - Electricity and £704,000 (£756,000 in 2005/06) for Objective B – Gas. The significant rise in costs for Objective A is due mainly to increased costs associated with the continuing development of the Single Electricity Market.

More detailed financial information on costs can be found in the Authority's Resource Accounts.

The Operating Cost Statement (the public sector equivalent of a profit and loss account) and a schedule setting out our financial performance in pursuit of objectives are shown below.

Operating Cost Statement – Table 1

	2006-07	2005-06
	£000	£000
Administration Costs		
Staff Costs	1444	1005
Other non-staff Costs	2612	2061
Total Costs	4,056	3,066
Operating Income	(1,466)	(1,545)
NET OPERATING COST	2,590	1,521



Costs by NIAER Aims and Objectives – Table 2

	2006-07			2005-06		
	Gross	Income	Net	Gross	Income	Net
	£000	£000	£000	£000	£000	£000
<i>for the year ended 31 March 2007</i>						
Objective (A) To promote competition in the generation and supply of Electricity and to protect the interests of electricity consumers with regard to price and quality of service	3,352	(763)	2,589	2,310	(992)	1,318
Objective (B) To promote the development and maintenance of an efficient, economic and co-ordinated gas industry and to protect the interests of gas consumers with regard to price and quality of service	704	(703)	1	756	(553)	203
TOTAL	4,056	(1,466)	2,590	3,066	(1,545)	1,521

Licence Fees

The Authority's costs are recouped primarily from the annual fee paid by electricity and gas licensees. From 1 April 1998 the fees were reclassified as Accruing Resources and to give effect to the re-classification DETI gave the Authority permission to collect electricity licence fees on its behalf. No change was required to the arrangement for gas licence fees which were already being collected by the Authority.

Electricity licence fees are calculated on the basis of a determination made by the Authority in respect of the identifiable costs of electricity regulation which stipulates that one third of the total fees due should be charged to the holders of generation licences, one third to transmission and distribution licensees and one third to those engaged in supply.

Gas licence fees are calculated on the basis of a Determination made by the Authority in respect of identifiable costs of gas regulation and will be apportioned

between the holders of gas conveyance and gas supply licences on the basis of 80% to the holders of conveyance licences and 20% to the holders of supply licences.

- Conveyance licence holders also engaged in distribution activities will pay a premium of £50,000. In addition the balance of costs to be charged to conveyance licenses will be apportioned on the basis of volumes conveyed in the previous year.
- Holders of gas supply licences will be required to pay a minimum fee each year of £1,000. In addition the balance of the costs to be charged to gas supply licensees will be apportioned on the basis of volumes supplied in the previous year.

The electricity licence fees in respect of the financial year ended 31 March 2007 totalled £763,000 whilst the gas licence fees in respect of the financial year ended 31 March 2007 totalled £703,000.



The costs of the CCNI in carrying out the duties assigned to it by the Order are collected by the Authority from Electricity and Gas Licence holders. CCNI costs for the Financial Year ended 31 March 2007 totalled £324,875 of which £185,463 was attributed to electricity work and £139,232 was attributed to gas work.

Central Government Financing

An amount of £2,590,000 in respect of the financial year end 31 March 2007 were borne by central government in respect of expenditure on areas not covered by current licences such as the Single Electricity Market, management on behalf of HM Customs and Excise of the Climate Change Levy Exemption scheme, the Electricity (Guarantees of Origin of Electricity Produced from Renewable Energy Sources) scheme and the Renewables Order (Northern Ireland) 2005 scheme.

Accounting System

The Accounting system was further enhanced over the past financial year by the addition of report writing software which allows Finance Section to produce resource accounts in a more effective and timely manner – meeting the Treasury's faster financial closing targets before they become statutory. The updated system will continue to be used to enhance the financial and management information available to staff throughout the Authority.

Audit

External Audit

The statutory annual accounts are audited by the Northern Ireland Audit Office (NIAO), whose staff work with the Authority Finance Section staff from submission of the draft accounts through to final publication. The 2006/07 Accounts were given an unqualified certificate by the NIAO.

Internal Audit

The Internal Audit of the Authority is carried out on a contract basis. Following a tender exercise, a local company of professional accountants and auditors HELM were successful and carry out the Internal Audit function. The Internal Audit report for the Financial Year ended 31 March 2007 gave limited assurance. The Authority will seek to address areas for improvement during 2007/08.

Audit Committee

As per Her Majesty's Treasury guidelines an Authority Audit Committee was established and met on three times during 2006/07 in order to provide additional assurance to the Accounting Officer that the system of internal controls are operating effectively. Until November, the Committee was chaired by John Gilliland with Joan Whiteside as the additional member. Subsequently, the chair passed to James Oatridge and he and Clive Elphick made up the remainder of the committee. The Committee has been involved in the following areas:-

- Approval of Accountant's Project Plan to ensure the Treasury's Faster Financial Closing targets are met;
- Meeting with Internal Audit manager to approve the Internal Audit plan;
- Meeting with NIAO Audit Manager to discuss financial audit process and timetable;
- Review of management responses and implementation of both external and internal audit recommendations over the past year;
- Financial and Qualitative review of NIAER consultancies;
- Development and review of the risk register;
- Development of management and financial information;
- Development and approval of the Accounting Officer's Statement of Internal Control.

Corporate Governance

Corporate Governance has been strengthened, since the inception of the Authority, by the increased frequency of audit committee meetings, the implementation of External and Internal Audit recommendations, the development and formal review of a corporate risk strategy and register and the incorporation of risk management more fully into corporate planning and decision making. These developments assisted in giving the Accounting Officer greater assurance that the Authority is maintaining a sound system of internal control that supports the achievement of the Authority's aims and objectives.





In addition to the work undertaken by the Audit Committee, a Remuneration Committee has been established to manage and approve recommendations regarding the remuneration of the Chief Executive Officer and senior staff. The Committee will also contribute to wider pay policy issues affecting all staff.

Business Advisory Groups (BAGs) have been established for Water and Energy (covering Electricity and Gas). The membership of these BAGs is made up of non executive directors, with relevant utility experience, and senior staff working in the utilities. They are designed to provide detailed scrutiny of key policy issues in support of the decision making processes at Board level.

Payment Policy

The Authority complies with prompt payment guidelines set out by Government which specifies payment within 30 working days. The Authority endeavours to pay all undisputed invoices within 30 working day from receipt of invoice. During the financial year, 2006-2007, 97% of the Authority's creditors were paid within 30 working days.

Equality Scheme and Equality Impact Assessments

The Authority's Equality Scheme and Equality Implementation Plan were reviewed during the year to

ensure its commitment to the fulfilment of the obligations in Section 75 of the NI Act 1998 is maintained. The obligations concern the promotion of equality of opportunity between the groups identified by the Act as relevant for NI purposes and promoting good relations between persons of different religious belief, political opinion or racial group.

In line with the implementation plan the following areas were addressed: -

- A review of the Equality Scheme was prepared and submitted to the Equality Commission in February 2007;
- Development of relevant training programmes;
- Screening of Authority policies in order to ascertain should Equality Impact Assessments be carried out.

Publicity and Communications

The Authority's Freedom of Information Scheme was approved on 12 November 2002. The Scheme can be viewed on our website and sets out, among other things, the classes of information publicly available without the need for a specific request. An in-year review was carried out to ascertain what additional responsibilities the scheme will impose from 2006 regarding the supply of information in response to individual requests.



Publications, consultation papers and press releases are routinely made available on the website. The Authority continues to engage with the media on public relations activities.

In the past year we have continuously improved and updated our website in order to inform and consult stakeholders in a user friendly and informative manner.

Details of all Electricity and Gas licences and any modifications, revocations, directions, consents or determinations relating to them are contained in their respective public registers, which are held in the Authority's office at Queens House, 14 Queen Street, Belfast. Each can be viewed by the public, for a fee of £1.00, from 10.00am to 4.00pm Monday to Friday.

Copies of licences and related documents are available for sale or may be viewed or downloaded (free) from our website – www.niaur.gov.uk

Land Bank

Belfast West Power Station

Belfast West Power Station (BWPS) was handed back to the Landbank in 2003 by AES. Landbank is managed by NIE behalf of customers under a condition in its licence. Following an appraisal of BWPS, validated by the Authority's consultants, on the assessment of the risk presented by its disuse, it was agreed that prompt dismantling and demolition would be the safest course of action. The level of risk posed by the site in its current status is of concern. This relates chiefly to the release of asbestos and contamination of the local environment. Technical and Environmental reports have set out the basic strategy required to achieve the controlled, safe dismantling and demolition of the station. Prices for the work have been sought to assist in setting budgets.

The Authority has developed a memorandum of understanding with NIE in order to encapsulate the high-level strategy, roles and responsibilities of taking forward the work associated with the demolition of BWPS.

As NIE PBB do not have the resources required to manage and deliver the demolition and clearance of the BWPS site they have tendered for and established a dedicated Project Management Team (PMT) who will be responsible for the procurement of the necessary resources to complete this project.

There has been significant progress at Belfast West Power Station completing pre-demolition enabling works, conducting discussions with stakeholders and statutory authorities and in the tender competition for the main demolition contract.

NIE is managing the site to ensure that all prevailing risks are mitigated as cost effectively as possible, but in full compliance with Health & Safety, environmental and other relevant legislation. As part of this process we have ensured that NIE have been maintaining regular contact with statutory authorities including EHS, HSENI and the Northern Ireland Fire Brigade (NIFB). These parties have all offered advice and made recommendations with respect to specific actions that have been required. We will continue to liaise with these authorities and take on board any further recommendations they make with respect to managing the site.

The Authority receives a monthly report on costs by category of expenditure and an analysis of any significant variances against the agreed and approved budget. The Authority have liaised with NIE in order to establish the process of moving us towards a point where the Authority should be able to consent with reasonable confidence, when formally requested, to the expenditure which NIE expect to incur on the demolition project. The Authority has taken steps to ensure that NIE are handling the demolition process in an economic and effective way which takes properly into account the risks and liabilities involved. The consultants employed by the Authority are Mott MacDonald.

Coolkeeragh Power Station (CPS)

During the year the Authority issued a direction to NIE to commence work on the project management of CPS. Following a tender exercise, carried out in conjunction with NIAER, NIE confirmed that Jacobs Babbie had been appointed as Project Manager for the decommissioning, asbestos removal, demolition and remediation of Coolkeeragh Oil Fired Power Station with effect from 4 May 2006.

Single Electricity Market

The Authority's Finance team have been working jointly with CER on developing the financial and administrative structures to support the teams working on the SEM.



This has resulted in the implementation of an account payable system developed in conjunction with the finance team in CER. A number of consultancy tender exercises have also been developed and run in conjunction with CER.

Licensing

All the information required to obtain a licence in NI including a specimen application form is now available on our website. During the year 2006 - 2007 a number of new wind farm generation licences were issued and a number of gas supply licences including a new gas supply licence to Phoenix. Discussions are continuing with DETI, to finalise a standard bespoke wind farm generation licence.

Climate Change Levy Administration

The Finance Act 2000 introduced the CCL and gave the Authority responsibility for accrediting renewable generators, administering and monitoring the exemptions claimed and issuing Levy Exemption Certificates. As the legislation did not provide any finance to the Authority the cost of administering this scheme is recouped from central government.

Consumer Representation

The Energy Order transferred responsibility for looking after the interests of consumers of electricity and gas to the CCNI. The Order also abolished the Northern Ireland Consumer Committee for Electricity (NICCE) and the Group established by the CCNI in connection with the exercise of its functions in relation to the supply of energy (excluding electricity) and replace both organisations with one group dealing with energy.

The Authority collected and passed on to the CCNI the sum of £324,875 being the estimated amount required by the CCNI for the year ended 31 March 2007 to carry out its functions under the Order.

The Authority has retained responsibility for making determinations, for making and setting Overall Standards and Guaranteed Standards, conditions dealing with resale of electricity, approving Codes of Practice and publishing a report on NIE's performance in meeting its standards.



