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Ofgem's Five Year Strategy 2009 - 2014

Dear Andy,

We welcome the opportunity to respond to the recent Ofgem letter regarding your five year strategy for 2009 – 2014. We have some general comments first which reflect concerns we have with the relationship between government priorities and how they impact on the business environment and competitive markets.

In the recent past prices have been driven up by a variety of cost pressures, e.g. primary fuel costs and environmental costs. At the same time it is clear that there is a looming capacity gap. Ordinarily one would expect an increase in market wholesale prices to reflect this tightening market and provide a signal for new build. However, recent experience has shown marked political intervention in energy markets. It is unclear whether prices would be allowed to respond to tightening supply and demand conditions. If this perception is allowed to prevail it is likely to deter new entrants as well as new build from existing participants. Such an outcome would be extremely damaging and it would be helpful for Ofgem to include in its forward plan steps it will take to combat this perception as there is no prospect that the underlying pressures will go away.

We have identified the following priorities for Ofgem.

1. Creating and Sustaining Competition

Competitive markets are still the most efficient method of delivering the lowest cost products to energy market customers. We are already seeing product innovation and more interaction between suppliers and customers in an effort to mitigate the effects of the higher prices. Whilst we fully support a targeted and long term solution to those most affected by higher energy costs, political interference within the competitive markets will ultimately increase energy prices for all. Ofgem has a major role to play in this area.

We note that in your plan published in March 2008 (paragraph 1.22) that you are disappointed with the slow progress with cash-out changes. We find such a statement a little hard to understand given that Ofgem have the opportunity to participate and indicate what their concerns are. Industry is generally supportive of change where they see good reason for it.

We fully support the role you are taking in Europe to provide greater transparency

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and liberalization of the European energy markets.

2. Regulating networks effectively

The 'Regulating Networks Effectively' theme remains valid and most of the relevant issues have been identified within this theme. A key issue in the future for both electricity and gas networks will be that of connecting gas imports and more renewable and/or distributed generation that may be both intermittent and remote. We believe that there is a need for additional infrastructure as well as better utilisation of existing assets and welcome the measures set out in the final Transmission Access Review report to consider ways in which new grid infrastructure is planned and developed, including new incentives on Transmission Owners to invest ahead of full user commitment. Ofgem should develop these measures as a priority.

We will continue to support the wider initiatives undertaken as part of the Transmission Access Review and are fully committed to helping the Government meet its renewable targets. Our preference remains, however, for the development of arrangements that fit within, and complement the existing access framework. Connectees should face the costs that they impose on the system and additional costs should not be socialised.

Offshore wind generation can play a key part in meeting Government's renewable objectives. We would encourage Ofgem to finalise the regulatory and commercial framework as a matter of some urgency, given that there are still some elements of the regime yet to be decided.

3. Helping to protect the security of Britain's energy supplies

As we said in 1 above we believe that competitive markets are the most effective means of delivering security of supply.

With the requirement to invest £100bn to meet Government's renewable energy targets¹, we were disappointed when Ofgem seemed to jump on the political bandwagon that was calling for windfall taxes. That would seem to be out of scope given the scale of investment required in this industry and the stable political and regulatory environment required to deliver it. For the next 10 years we plan to invest more than we earn to invest in new, cleaner generation and would expect Ofgem to support this scale of investment that we and the rest of industry is making.

We welcome your involvement in the Energy Markets Outlook process and in closer timescales recognise the role you play in organising the summer and winter outlook seminars which are of value to all market participants.

4. A leading voice in Europe

We continue to support Ofgem's work with European regulators' groups to develop a consistent European regulatory framework and in particular the work on the regional market initiatives in electricity and gas. We agree that regional markets are a required step towards single markets in electricity and gas.

Liberalisation of the energy market has already brought benefits to UK customers. We support the aim of safeguarding against the danger that overly prescriptive European proposals might undermine these benefits. We look to Ofgem to work with Government to ensure the appropriate transposition into UK law.

However, from the perspective of better regulation, we are concerned about Ofgem having taking

¹ BERR UK Renewable Energy Strategy consultation – June 2008

measures for the sake of harmonization on gas transparency, previously considered adequate by most market participants in the UK, and the possibility of market abuse legislation for the energy sector, which given that there are not market integrity issues in the UK, is unnecessary.

5. Helping to achieve sustainable development

Helping to achieve sustainable development remains a valid theme. It is even more pertinent now given the publication of the UK Renewable Energy Strategy consultation which discusses how we will meet our share of the EU 2020 target.

We note that BERR is currently consulting on amendments to the Authority's social and environmental guidance which includes the use of the Shadow Price of Carbon in impact assessments.

We look to Ofgem to ensure that wherever possible robust market focused solutions are introduced that enable the delivery of sustainable development in the most efficient way.

6. Helping to tackle Fuel Poverty

Fuel poverty has, by all measures, risen up the political and social agenda. Suppliers have responded positively to the initiatives agreed with Ofgem and other stakeholders arising out of the fuel poverty summit. In addition, the recent proposals agreed with Government resulting in a further £910m being committed to alleviate fuel poverty over the next three years through energy efficiency measures will make a difference to eligible customers' well-being.

Suppliers will therefore continue to do all that they can to ensure customers are identified who can benefit from the considerably enhanced assistance that is and will become available in the coming months. However, as we have said before, suppliers can only do so much. Once a customer has received all the help that is available and has maximised their financial position together with ensuring they are consuming energy efficiently on the most appropriate tariff, there is little, if anything, more a supplier can do. It must be the job of Government to deal with societal related to general poverty.

7. Better Regulation

We are fully engaged in the Industry Code Governance review process but our starting point is that the codes in their present form have served the industry well over the years and therefore fundamentally they are fit for purpose. We accept that there is always room for improvement, in the codes themselves but also in the roles of industry and Ofgem in making the codes work.

If you wish to discuss any aspect of the above response, please do not hesitate to contact me. We look forward to the next stage of the process and the publication of the consultation in January 2008.

Yours sincerely

Alan McAdam
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