EDISON MISSION ENERGY
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Ofgem's three year strategy 2004-7

Edison Mission Energy is a worldwide operator of independent power plants. In the United Kingdom EME owns and operates the pumped storage power stations at Dinorwig and Ffestiniog owned by EME's subsidiary First Hydro. It also operates and has a third share in the Derwent co-generation plant at Derby. It has also previously owned other coal and gas fired generating plant.

As an independent generator operating in the competitive wholesale electricity market and without access to our own supply business, the main concerns we would like to see Ofgem addressing over the next three years are set out below:

Market structure. The market is becoming progressively dominated by vertically integrated generation and retail businesses. Those companies are less exposed to the pressures of a competitive generation market than independent generators because they have retained a significant proportion of their old 'franchise' customers at tariffs above the competitive market rate. This customer inertia is likely to be a long term feature of the market. Independent generators may be progressively squeezed out of the market. The more so because it will only be the vertically integrated companies that will be prepared to take on the risk of new investment. Competition will be damaged to the detriment of customers. An early investigation of the impact of vertical integration using Enterprise Act powers should be an Ofgem priority.

Market signals. Current trading arrangements do not give clear price signals at times of system stress. As a result security of supply is put at risk. Longer term price signals which should incentivise new investment are largely absent from the market. We have proposed and will continue to propose BSC modifications to improve these signals and to support other proposals which have the same objective. It should be an Ofgem priority to support changes which result in improved price signals and incentivise the use of existing capacity and, as necessary, new investment. Those changes will affect short term price signals but the longer term incentives are not yet being addressed. It is unlikely that adequate and timely new investment will be forthcoming without some financial reward for making capacity available in addition to payment for energy when generated. Ofgem should review the stance it has taken against any form of capacity payment.

Market governance. The interaction between the various industry codes governing generation is a mess. Changes which impact on commercial decisions may be taken in the BSC, CUSC, Grid Code or NGC procedures and changes in one area often require consequential amendment in another. This leads to multiple scrutiny which is a regulatory burden for firms and also consumes additional Ofgem resource. <u>It should be an Ofgem priority to review these interactions and propose a simpler unified approach.</u>

<u>**Ofgem resources**</u>. Ofgem's £36 million budget is very large. Nearly two thirds of this is devoted to activities under the broad heading of promotion of competition. That is very surprising and suggests that there is far too much regulation of activities which should broadly be subject only to general competition laws. It is a general feature of UK policy that the promotion of competition has in many areas been accompanied by an extension of regulation. <u>Ofgem should make it a priority to review its activities in competitive parts of the energy market and reduce the scale of its detailed involvement.</u>