

Mr A. MacFaul  
Head of Government Affairs  
Ofgem  
9 Millbank  
London  
SW1P 3GE

2<sup>nd</sup> March 2005

Dear Andrew

### **Ofgem Proposed Corporate Strategy and Plan 2005-2010**

The Energy Saving Trust (EST) welcomes the opportunity to respond to Ofgem's consultation on its proposed Corporate Strategy and Plan 2005-2010. This submission should not be taken as representing the views of individual members of EST.

EST was established as part of the Government's action plan in response to the 1992 Earth Summit in Rio de Janeiro, which addressed worldwide concerns on sustainable development issues. We are the UK's leading organisation working through partnerships towards the sustainable and efficient use of energy by households, communities and the road transport sector and one of the key delivery agents for the Government's climate change objectives. Our response focuses on the key areas of EST's activities and related issues. We do not attempt to answer questions outside of our area of expertise.

EST welcomes the proposed Corporate Strategy and Plan 2005-10 and is pleased that Environment again forms one of Ofgem's key themes for the period 2005 -2010 along with the new duty to contribute to sustainable development. Currently much of Ofgem's efforts in these areas relate to administration duties and in our opinion Ofgem does not yet appear to be as proactive in these areas as in others. Environmental and sustainable development issues need to be mainstreamed into Ofgem's strategic activities and in our opinion, Ofgem needs to strengthen its Corporate Strategy and Plan in these areas accordingly.

We believe that Ofgem has a real opportunity to help shape markets that can deliver a low carbon economy, which would be beneficial to consumers through reduced energy demand (and hence lower prices) in a more secure and less polluting environment. A good starting point would be to formally support the Government's domestic target to reduce CO2 emissions by 20 percent by 2010 and the Housing Act 2004 target for a 20% increase in residential energy efficiency by 2010 from a 2000 baseline.

In this respect, greater emphasis should be placed on energy efficiency and distributed generation related strategies moving forward, particularly in relation to the future of the Energy Efficiency Commitment (EEC), the proposed Low Carbon Buildings Programme (LCBP), the potential impact of the current Energy Efficiency Innovation Review and European initiatives. EST would welcome the opportunity to continue to work closely with Ofgem on these and other issues of mutual importance e.g. enhancing Energy Smart through utilisation of the existing EST infrastructure and expertise.

We have identified the following additional key issues that we believe should receive greater Ofgem priority during the next five years. Some of these are under Ofgem's full control whilst others would require Ofgem to influence Government accordingly.

### **Markets Policy**

- Refinement of EEC to a more market-based approach including non-supplier programmes and a "buy-out" provision akin to the RO to improve cost-effectiveness. This would allow future targets to be strengthened accordingly.
- Encouragement for the improved integration of EEC with fuel poverty instruments.
- Proactive consideration of the benefits of energy efficiency or "white certificate" trading.
- Facilitate the development of energy services companies.

### **Distribution and security of supply**

- Further support to the development of distributed generation to allow the full project benefits to be realised by developers, including the refinement of the Renewables Obligation (RO) support mechanism to make it easier for micro-generation to gain RO Certificates (ROCs).
- Greater recognition of the role of biomass and energy efficiency (through demand reduction) in enhancing security of supply.

### **Consumer Policy**

- Improvements to the level and consistency of billing information.
- Encouragement for the development of smart metering and data systems.

### **Enforcement**

- Development of mechanisms to ensure compliance with green certificate guidelines, e.g. accreditation schemes, and to promote the uptake of green tariffs.
- Greater involvement in the development of energy efficiency related European legislation, e.g. the proposed energy services directive and product standards etc.

In addition, EST would also like to make some specific comments on the consultation document and attach these accordingly.

Yours sincerely

**Brian Samuel**  
**Head of Policy and Research**

## **Energy Saving Trust's specific comments on Ofgem Proposed Corporate Strategy and Plan 2005-2010**

### **Section 2. Ofgem's developing role over the next 5 years**

#### **Paragraph 2.2**

We agree that it is important for Ofgem to take account of the environmental impacts of its decision-making and to help Government deliver its carbon saving targets in the most cost effective way. Ofgem's policies need to be designed to assist Government in meeting its targets.

#### **Paragraph 2.4**

We welcome the new duty to contribute to sustainable development. In particular, we would like to see energy efficiency and distributed generation become more integrated into Ofgem's mainstream work with energy suppliers and their advice to consumers.

#### **Paragraph 2.11**

We are pleased that Ofgem recognises the important role of network operators in developing efficient and innovative solutions to the application of new technologies. We believe that this is especially important at the micro-generation level and that both Ofgem and the network operators take account of the different requirements of micro-generators compared to other network users.

#### **Paragraph 2.16**

We would like to see reference given to the role of energy efficiency in improving security of supply by reducing demand. In particular, increased levels of insulation will help reduce peak winter demands. Distributed generation can also assist in enhancing security of supply. We note the comments in relation to wind power and believe that greater attention should be paid to encouraging biomass generation, which can provide renewable baseload power.

#### **Paragraph 2.18 (and Section 6. A leading voice in Europe)**

We are disappointed that Ofgem does not recognise the opportunities that strengthening European legislation on energy efficiency could provide. Ofgem should be encouraging the development of tighter appliance and product standards that would reduce energy consumption and supporting energy performance improvement targets under the proposed Directive on Energy Services.

We believe that Ofgem's new duty to contribute to sustainable development requires greater involvement and support to environmental issues at the European level, which must include energy efficiency.

In our opinion EEC has the potential to deliver the greatest short and medium term contribution to reducing household carbon reductions. It is therefore important to ensure that future European legislation would not prevent the strengthening of future EECs.

### **Paragraph 2.19**

International emissions trading may offer industrial consumers the best prospect of achieving value for money in securing environmental improvement, but energy efficiency offers the best prospect for households. It is important to develop mechanisms that allow all consumers to take advantage of energy efficiency through reduced costs and improved comfort, whilst reducing emissions. Because of the level of market failure in investment in cost effective energy efficiency by smaller consumers, a single carbon trading system is **not** the most cost effective carbon emissions reduction policy.

### **Paragraph 2.20**

We are disappointed that no reference is made to the benefits and cost-effectiveness of energy efficiency under the heading of Environment.

### **Paragraph 2.21**

We welcome the recognition given to energy efficiency in reducing fuel poverty. Distributed generation and renewable heat technologies can also make a major contribution to reducing fuel poverty, especially in off gas network areas. It would be helpful if this was also recognised.

## **Section 3. Creating and sustaining competition**

### **Paragraph 3.30 (and 7.14)**

We agree that further action is required to develop competition in connections, particularly given the planned expansion of distributed generation and new housing developments.

In our opinion, work is required to improve the level and consistency of information provided on bills. Currently it is difficult to compare and understand consumption patterns, which makes it difficult for consumers to link the impact of their behaviour to energy usage and to understand how energy efficiency measures might benefit them. Introducing a billing code of practice would be helpful in this respect and need not constrain suppliers from offering innovative products.

## **Section 4. Regulating Network Monopolies**

### **Paragraphs 4.7 and 4.15 - 4.19**

We welcome Ofgem's commitment to ensure network operators are capable of connecting distributed generation, specifically renewables. This must be undertaken in a timely and efficient manner and at low cost. We believe that the Innovation Funding Incentive and Registered Power Zones initiatives will be helpful in this respect. The effectiveness of the reform of distribution charges needs to be monitored and assessed with a view to improving where necessary.

## **Section 6. A leading voice in Europe**

Please see our comments made in relation to paragraph 2.16.

## **Section 7. Helping to Protect the Environment**

We support the efforts that Ofgem is beginning to make in helping deliver a low carbon future but believe that Ofgem needs to strengthen its activities in this area. In particular, we believe it would be helpful if Ofgem would formally support Government's domestic target to reduce CO2 emissions by 20 percent by 2010 and the Housing Act 2004 target for a 20% increase in residential energy efficiency by 2010 from a 2000 baseline.

### **Paragraph 7.8**

As part of this review, we suggest it might be helpful if Ofgem could also consider the application of trading schemes in other activities e.g. merits of introducing a "white certificates" or energy efficiency trading scheme as being considered by France and Italy.

### **Paragraphs 7.12 – 7.14**

We are disappointed that these paragraphs focus on past initiatives rather than moving forward to 2010. In particular, we are disappointed at the lack of strategic focus on EEC3 and subsequent instruments. In our opinion the fact that improving energy efficiency will reduce consumer's bills and therefore in the interests of consumers, has been understated.

### **Paragraph 7.12**

The EEC is the single most important residential measure for the short and medium term. We believe that Ofgem needs to start considering the future role of EEC3 now and within the timeframe of the strategic plan; consideration will also need to be given to the future of EECs post 2011. In our view, EEC should be switched to a more market-based approach including non-supplier programmes and a "buy-out" provision akin to the RO to improve cost-effectiveness. The introduction of the requirement to produce an energy report as part of the Home Condition Report (or the Scottish equivalent) under the Energy Performance in Buildings Directive (EPiB) upon sale or change of tenancy will also facilitate the uptake of household energy efficiency measures; as it is easier to install energy efficiency products such as insulation and heating controls at this time.

This would allow the EEC for the period 2008-11 to be expanded to roughly triple that of EEC1 along with a reduction in the minimum percentage of measures delivered to the priority group.

### **Energy efficiency or "white certificate" trading**

Currently a non-energy supplier, e.g. insulation provider, white goods manufacturer etc, can only extract value from delivering EEC through a prior arrangement with an energy supplier under an Ofgem approved programme. Direct accreditation of third party schemes by Ofgem would allow a more diverse range of participants with additional cost effective energy efficiency projects. Accredited third party activity would require a standard format to allow trading with suppliers and demonstrate compliance with EEC,

i.e. a ‘white certificate’. This approach should improve cost-effectiveness and the range of projects by increasing market liquidity although a range of issues would need to be considered including the legal basis, property rights, accreditation, transaction costs, costs to consumers, impact on priority group, supplier market power, settlement periods, market deadweight. This approach is already being progressed in France and Italy.

### Energy efficiency obligation

Under the current system, energy suppliers are required to fulfil their entire obligation, unlike the RO, which includes a buy out option. Under the existing EEC approach, Government has to set the obligation at a level lower than suppliers can reasonably be expected to deliver whereas with a buy-out the obligation has to be set at a higher level than Government wants delivered otherwise as the obligation level is reached, the white certificate value falls to zero and any incentive to deliver disappears. We therefore believe that a buy-out provision would allow higher EEC targets to be set. Recycling of buy-out revenues back to suppliers could be done in proportion to energy efficiency delivered (as with the RO), which would create an additional incentive to deliver energy efficiency. Again a range of issues would need to be considered including the legal basis, costs to consumers, impact on priority group, market deadweight, level of the buy-out price etc.

### Interaction between other instruments

Ofgem already recognises that energy efficiency can also help alleviate fuel poverty. We believe that Ofgem should be encouraging improvements in the interaction between EEC and the existing fuel poverty programmes, such as Warm Front, Warm Deal, Welsh Home Energy Efficiency Scheme (HEES), Scottish Heating Grant Scheme and the Scottish Housing Quality Standard (SHQS). We note that the Fuel Poverty Action Plan states that programme managers of these schemes will be encouraged to work more closely in partnership with other energy efficiency schemes, such as EEC. We believe this could include the use of EST’s Home Energy Efficiency Database (HEED<sup>1</sup>) as an information repository to achieve better co-ordination. A more radical approach might be to totally focus the EEC on reducing carbon and developing existing or additional measures to address fuel poverty.

### **Paragraph 7.13**

We welcome the trial removal of the 28 day rule, which should help facilitate the development of energy service companies. We believe Ofgem should be proactively encouraging energy suppliers to develop energy efficiency services including distributed generation technologies.

### **Paragraph 7.14**

We agree that further work is required to improve information provided on bills. Currently it is difficult to compare and understand consumption patterns, which makes it

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<sup>1</sup> HEED has been developed by the on behalf of Government and records energy efficiency installations, as well as survey data on a property-by-property basis. A key advantage of HEED is that it uses data from a wide variety of sources including energy suppliers, government scheme managing agents, local authorities as well as EST programmes. HEED is purposely designed to; build up a picture of progress on energy efficiency over time and by area; help local authorities with their reporting under the Home Energy Conservation Act; and facilitate the planning and efficient targeting of energy efficiency initiatives

difficult for consumers to link the impact of their behaviour to energy usage and to understand how energy efficiency measures might benefit them. Introducing a billing code of practice would be helpful in this respect and need not constrain suppliers from offering innovative products. We would also welcome initiatives to encourage the development of smart metering, which has the potential to facilitate energy management and energy efficiency thereby reducing costs to consumers and note that Italy is currently implementing improved metering systems.

### **Paragraph 7.15**

We would welcome reference to the EST's activities in promoting energy efficiency activities in the household sector and look forward to working with Ofgem in delivering major carbon reductions. This is especially pertinent given that EST launched a £3m EEC campaign on 14<sup>th</sup> February to raise awareness of EEC amongst consumers.

### **Helping deliver the true benefits to distributed generators**

There are still significant barriers to the development of a market for small scale distributed generation, including difficulties in obtaining the true value of distributed benefits and a lack of consumer awareness. We believe that Ofgem has a responsibility to help overcome these.

EST welcomes that small generators (up to 50kW declared net capacity) are able to claim ROCs on an annual basis. However, we are disappointed that it has not proved possible to allow greater flexibility in claiming ROCs on either an annual or monthly basis. We believe that it is important for Ofgem to develop its procedures to allow generators to gain ROCs without incurring excessive cost and to be able to easily aggregate annual generation. In this respect we believe that:

- All small scale renewable generation, including on-site use, should be eligible for ROCs.
- Eligibility should not be dependent on having sale/buyback contracts in place.
- Type approval accreditation schemes for meters should be developed.
- The RO framework should be modified to enable small generators to obtain ROCs on a monthly basis if they so desire.

We believe that more needs to be done by Government and Regulators to allow distributed generators to realise a more favourable share of the true benefits i.e. ROCs benefits, Levy Exemption Certificate (LEC) benefits and supplier cost avoidance i.e. the avoidance of distribution and transmission losses, the avoidance of distribution and transmission charges by suppliers, the avoidance of Balancing and Settlement Code (BSC) and Elexon charges etc. We would welcome recognition of this in Ofgem's Corporate Strategy and Plan.

We welcome the current work being undertaken through the DTT's New and Renewable Energy Programme and its Distributed Generation Programme including the development of a guide for distributed generators, which should focus primarily on the requirements of small scale generators who typically don't have the resources and expertise to fully address the wide-ranging issues. We believe that it would be helpful if Ofgem supported the development of this guide and should consider assuming responsibility for supporting its future maintenance in respect of any regulatory change.

## **Proposed Low Carbon Buildings Programme**

We support the DTP's proposed LCBP to increase the use of building integrated renewables and distributed generation, as advocated in the Renewables Innovation review. The LCBP would deliver low carbon buildings in the future by incorporating support for emerging technology and best practice in both energy efficiency and renewables. We believe Ofgem needs to consider how it can effectively facilitate the aims of the programme once it has been established.

## **Energy Efficiency Innovation Review**

We also believe that Ofgem will need to consider the potential impact of the current Energy Efficiency Innovation Review in its future activities.

## **Accreditation for green tariffs**

With the demise of Future Energy, the UK green tariff accreditation scheme, following the introduction of the RO consumers are faced with an increasingly confusing array of tariffs branded as "green". This market has already suffered, for example previously 'gaming' between suppliers seeking a high rank in the Friends of the Earth green tariff league table. This led to a series of meetings during 2004, between suppliers EST, DTI, Ofgem and energywatch, which resulted in a proposed framework for auditing green tariffs and the planned revision of Ofgem guidelines for Green Supply Offerings, which is due for publication in early 2005.

EST recognises the benefit of this work, but notes that there is no plan to require compliance with the guidelines or to promote green tariffs. EST believes that a national accreditation scheme for green tariffs is required in order to raise consumer awareness and stimulate renewable uptake whilst avoiding confusing and misleading claims being made to consumers that could damage the credibility of renewables. We therefore recommend that Ofgem consider how this might be implemented.

## **Section 8. Helping to tackle fuel poverty**

### **Paragraph 8.3**

We support Ofgem's willingness to deliver a more joined up approach to fuel poverty and refer to our previous comments in our response on Paragraph 7.12.

### **Paragraph 8.5**

We welcome the joint Energy Smart initiative between Ofgem and energywatch including the provision of the top 10 energy efficiency tips. It is important to recognise that consumers need to be encouraged to go to the next step in seeking advice and implementing energy efficiency measures. EST is best placed to provide this through its existing infrastructure, including its network of 52 Energy Efficiency Advisory Centres. This would ensure cost-effective delivery of consistent messages. We would welcome the opportunity to meet with Ofgem to explore how best this might be achieved.

## **Appendix 1 Corporate Plan Deliverables**

We are disappointed to see that none of the deliverables set out under “Protecting the Environment” imply Ofgem action to actively develop markets to promote the efficient use of energy or to contribute to the achievement of sustainable development. This seems to be inconsistent with Ofgem’s firm commitment to creating the conditions in which the energy industries can help deliver a low carbon economy as efficiently as possible.