



ScottishPower

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Dear Andy

Ofgem Proposed Corporate Strategy and Plan 2005-2010

We are writing on behalf of ScottishPower in response to Alistair Buchanan's invitation to comment on Ofgem's Corporate Strategy and Plan for the years 2005-2010. We welcome Ofgem's recent announcement that it is submitting itself to an RPI-3 resource control and confirmation that this will apply for the five years of the plan. We are however surprised that the opportunity has not been taken to make a significant reduction in Ofgem's resource requirements in the first year of the plan in recognition of the completion of the two major projects of recent years, the Distribution Price Control Review and BETTA, which together account for over 20% of Ofgem's resource requirement in the current year. While we recognise Ofgem's desire to retain expertise we believe that core expertise could still be retained with a more significant reduction in year one and if necessary a lower reduction in subsequent years.

We agree with the retention of the seven major themes from the current Strategy and the benefits to the industry in terms of regulatory continuity and predictability of working within a stable overall regulatory framework.

Creating and sustaining competition

We recognise Ofgem's important role in creating and sustaining competition and Ofgem's differentiation between its role in markets where competition is established and markets where it is not established. Ofgem has recognised that competition has been established for some time in the GB electricity and gas consumer markets and the GB wholesale gas market and with the introduction of BETTA will be established in the GB electricity wholesale market. It is thus not clear why the resources being allocated to consumer and wholesale markets in the first year of the plan, 2005/06, are 50% higher than the resources allocated to the equivalent work areas in Ofgem's budget for the current year.

Ofgem estimates that only minimal resources will be required to monitor the GB electricity wholesale market following BETTA implementation and we agree with this estimate. BETTA this year accounted for over 30% of the resources allocated to the creating and

sustaining competition work area and the freeing of this resource should have enabled a more substantial reduction to have been made in resource requirements while still having the resources to undertake the important projects in this area.

We agree that an important area of work for Ofgem is to ensure that the UK is not being disadvantaged through artificial restrictions on the availability of gas to the British market and recognise the benefits of Ofgem working with the European Commission and other national regulators to ensure that capacity on European pipeline networks is available to companies wishing to export gas to the UK.

Ofgem will from 2005 be required to take account of the new rights of appeal to the Competition Commission when making decisions on modifications to the industry agreements underpinning the gas and electricity markets. We believe that this should lead to a reduction in the occasions when Ofgem makes decisions which are opposed by a significant number of industry participants and thus should result in a reduced workload for Ofgem and the industry and in Ofgem recognising the need to move to 'lighter touch' regulation.

We do not believe there is a need for a major review of retail competition in either the domestic or non-domestic gas or electricity supply sectors. Ofgem has recently concluded that competition is continuing to develop and deliver benefits to domestic customers in all demographic groups and that the non-domestic supply sectors are also competitive. The GB retail energy markets are more competitive than many other consumer markets which are not subject to ongoing major reviews and we do not believe there is justification for significant Ofgem resources to be tied up in this area of work.

We welcome Ofgem's review of the supply licences with a view to removing any conditions which are no longer necessary in a competitive market and the simplification of those which remain. However, given that supply licences were reviewed and simplified in 2001 following the Utilities Act we do not believe that a major review lasting more than 1 year is required.

As regards the connections market, ScottishPower's electricity distribution businesses continue to support the development of competition in this area, and to work co-operatively with Ofgem to this end.

Regulating network monopolies

We agree with Ofgem's statement that 'ensuring that network users pay charges that reflect the costs they impose on the system is an important principle that underlies Ofgem's approach to network charging arrangements'. We do not believe that the recently approved GB electricity transmission charging arrangements satisfy this criteria. An important task for Ofgem in 2005 will be to review aspects of these arrangements and ensure they are amended as soon as possible to be proportionate and non-discriminatory and do not result in market participants facing volatile changes in their costs.

It is important that shippers, suppliers and customers realise the benefits estimated by Ofgem from the sale of the local gas distribution network businesses through comparative regulation at future price controls. The sale has been justified on these benefits being realised from the 2008 price control onwards. Ofgem has retained comparative regulation expertise from the recently completed distribution price control review and this expertise should be able to be used both on the 2007 transmission gas and electricity price control reviews and also on the 2008 gas distribution price control.

Following the Distribution Price Control Review, there are a number of new and revised incentive arrangements, such as for distributed generation, that we will be managing in our two operational areas over the next five years. We will work with Ofgem to help identify any aspects of these arrangements that are not working as intended, in order that changes can be made where appropriate in due course.

We will also work with Ofgem to implement the new arrangements for funding transmission investment for renewable generation. In addition, the forthcoming full Transmission Price Control Review is expected to require the commitment of significant resources on our part.

We believe that implementation of these new incentives and institutional arrangements, including BETTA go-live, should now be allowed to take its course. Significant further policy initiatives should be limited until enough time has elapsed to allow an assessment of performance under the new arrangements. This would help to ensure that policy decisions are based on sound, well-researched analysis, and would also help companies to manage their resources in dealing with the workloads involved.

We note that Ofgem believes that each of the three transmission licensees should have new incentives to promote the efficient network reinforcement necessary to accommodate the growing level of renewable generation. We look forward to Ofgem's proposals. We do not however believe that there has been inefficient investment in the past and we are eager to see the justification for these new incentives. Investment for renewables has been pushed by the licensees for some years now and is an extremely important aspect of the forthcoming review. We have previously stated, and still hold the view, that for incentives to work they must be simple and have reasonably predictable outcomes. We do not believe that the deep system operator gas entry capacity scheme satisfies these criteria.

Following the recent introduction of relative price regulation for independent gas transporter sites it is important that Ofgem acts to ensure that all such sites implement relative pricing as soon as possible to ensure that suppliers do not continue to face increased costs.

Helping protect the security of Britain's energy supplies

Ofgem has an important role to play in conjunction with DTI in assessing supply security and publishing forward-looking indicators. We believe that the current market arrangements may not be sufficient to avoid future security of supply problems and that there may be a need for a market mechanism to ensure sufficient generation capacity remains available. While there are some indications that the market is starting to respond to higher anticipated prices we believe it is too soon to be confident that sufficient new conventional plant will be built.

A leading voice in Europe

We agree that European energy markets and EU regulatory policy have an important influence on energy markets in Britain and that Ofgem should, in conjunction with DTI, work with the Commission and national regulators to promote full and effective liberalisation of the European energy markets and to shape the regulatory agenda going forward. It is also important to harmonise arrangements between GB and the rest of Europe to ensure a level playing field in a competitive market. Important in this regard is the harmonisation of transmission charging arrangements and in particular the proportion of transmission charges to be paid by generators.

Helping to protect the environment

We agree that Ofgem's work on the environment should be integrated throughout the work of the organisation and aimed at assisting the gas and electricity markets and industry to achieve environmental improvement as efficiently as possible. While Ofgem does have a new duty to contribute to sustainable development Ofgem must recognise in exercising this duty that the leading role will be taken by Government departments with more direct environmental responsibilities.

We are concerned that Ofgem is increasing the resources it is allocating to administering the Government's environmental programmes. We do not believe that Ofgem should be diverted from its key priority tasks by administrative work which could be carried out by industry bodies. Ofgem's budget for 2005/06 on renewables is almost twice the level of the current year. Much of the work Ofgem currently carries out in relation to Renewables Obligation Certificates and Levy Exemption Certificates could be carried out by industry bodies such as the Non-Fossil Fuel Purchasing Agency allowing Ofgem to concentrate on its core tasks.

Helping to tackle fuel poverty

Ofgem recognises the challenge faced by the Government in its aim to eliminate fuel poverty among vulnerable households by 2010 given the recent rises in fuel prices and upward cost pressures from low carbon measures such as the Renewables Obligation, the Energy Efficiency Commitment and Carbon Trading.

We share Ofgem's concerns in relation to the implications of rising fuel prices on the fuel poor. For this reason we have invested very significantly in assisting these customers, both through the Energy Efficiency Commitment's Priority Group and also using specific ScottishPower initiatives.

We are currently engaged with the other major domestic energy suppliers, through the Energy Retail Association in assessing how best to maximise benefits from existing schemes. This exercise will feed into discussions with the Energy Minister, in determining how industry and Government can work together to alleviate fuel poverty in line with Government targets.

We continue to monitor the measures that we have in place to help the fuel poor and vulnerable customers to ensure maximum benefit for the funding employed. We also remain committed to working with Ofgem in this area.

Improving Ofgem's efficiency and effectiveness

We welcome Ofgem's RPI-3 resource control to operate for the five years of the plan. We believe, however, that the opportunity should have been taken to make a more significant reduction in Ofgem's resource requirements in the first year of the plan in recognition of the completion of the two major projects of recent years, the Distribution Price Control Review and BETTA, which together account for over 20% of Ofgem's resource requirement in the current year.

We also see a case for Ofgem to review the effectiveness of its website as a resource for customers and regulated companies. While we find it generally a very helpful source of information, there are some surprising gaps. For example most licences are not currently

available on the site and there is also no comprehensive archive of determinations available.

We hope that this is helpful and look forward to publication of the final Strategy and Plan.

Yours sincerely

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