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Our ref NT/THS

Andy MacFaul  
Head of Government Affairs  
The Office of Gas & Electricity Markets  
9 Millbank  
London  
SW1P 3GE

98 Aketon Road  
Castleford WF10 5DS  
[www.ce-electricuk.com](http://www.ce-electricuk.com)

tel: 01977 605165  
fax: 01977 605944

e-mail: [tony.sharp@ce-electricuk.com](mailto:tony.sharp@ce-electricuk.com)

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Dear Andy

### **Ofgem's five-year strategy 2006 - 2011**

CE Electric UK Funding Company (CE) is the UK parent company of Northern Electric Distribution Ltd (NEDL) and Yorkshire Electricity Distribution plc (YEDL). This letter represents the response of CE, NEDL and YEDL to Ofgem's open letter on its five-year strategy 2006 – 2011.

#### Key challenges facing the industry

We believe that the key challenges facing the industry in the short to medium term are already well articulated and understood – increasing capital profiles to maintain current quality of supply standards; customers' willingness to pay for improved security of supply; connection of the required volumes of renewable generation; future arrangements for metering (not least in the light of the recent *energywatch* report); the most appropriate form of price control against which to deliver the requisite outputs; and the increasing profile and impact of European legislation. The key requirement that we see as necessary to address a number of these challenges is a fully-integrated approach to network investment and security of supply that embraces not only standards of performance and incentives but also the scope of competition.

A significant problem and risk that we perceive with the development of such an approach is that of planning horizons. The nature of the assets that we are dealing with is such that we ourselves use a rolling twenty-year horizon when planning network investment and development. Whilst we believe it is by no means inappropriate for Ofgem to employ a five-yearly cycle for reviewing monopoly price controls, we believe that it needs to extend its planning horizon significantly beyond five years in order to be able to develop a realistic and viable longer-term strategy for networks on key issues such as quality of service, storms resilience and distributed generation. We would therefore encourage and welcome the development and setting out of a long-term network strategy that complements and delivers against the government's stated energy policy and the appropriately-researched aspirations of customers.

#### Action that the Authority should take

The actions that we should like to see the Authority taking to address these issues are as follows:

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- early opening of the debate on the best way forward for DPCR5, embracing a review of the traditional approach to network utility regulation to ensure optimisation against government objectives for renewable energy, energy efficiency and security of supply: we believe it will be too late to wait until completion of the gas and electricity transmission price control reviews before turning to consideration of DPCR5;
- closer working with government to articulate how the latter's long-term policy aims in environmental, social and energy areas can best be supported via a coherent and comprehensive longer-term strategy for networks as referenced above;
- review of the new incentive schemes introduced by DPCR4 ahead of the commencement in earnest of the DPCR5 process, to assess the extent to which the much more complex incentive framework under which we now operate is resulting in expected behaviour;
- taking a more proactive role in respect of European legislative developments, to be in a position not only to influence outcomes but also to give early warning to regulated companies of the potential regulatory implications of European developments;
- greater engagement with customers and their representatives via detailed research to inform decision making as to what is or is not in customers' best interests; and
- further building on the significant improvements made to date in the processes for consulting with the industry, in terms of clarity over timescales for end-to-end consultation/decision/implementation processes, longer timescales for consultation responses in some instances and further development of the regulatory impact assessment process.

#### How the Authority should prioritise

Operating as it is under an increasing efficiency target in respect of its own activities, the Authority should, we believe, apply strict criteria to its prioritisation processes as follows:

- appropriate delivery against government energy policy (without compromising the principle of arm's-length regulation);
- pursuit of changes/developments that are demonstrably of the greatest value/importance to customers (following appropriate engagement with them); and
- concentration on delivery of the greatest beneficial impacts (as informed by rigorous regulatory impact assessments).

I hope that you will find these comments helpful, and I look forward to publication of Ofgem's proposed strategy and plan in January.

Yours sincerely,

*Tony Sharp*

**Tony Sharp**  
**Regulation Manager**