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Dear Andy

Ofgem's Five-Year Strategy 2006–2011

I refer to Sir John Mogg's letter dated 12 August 2005. EDF Energy is pleased to have the opportunity to contribute to the development of Ofgem's strategy for the next five years.

Recent developments in the direction of Ofgem, cited by Sir John, are impressive and we largely support them, while noting that it is important for the organisation to continue to focus at all levels on maintaining a high quality and reasonable process of regulation. We remain to be convinced that the RPI–3 cost reduction target is sufficiently demanding, and we have some differences of emphasis (which we amplify below) in relation to metering policy and network regulation.

It is also clearly imperative that Ofgem should work more closely with the DTI to develop a coherent environmental strategy for the energy sector. This must be a strategy which transcends the current piecemeal and fragmented approach and is able to reconcile the underlying tensions between what is economically efficient and what is politically desirable.

With those caveats, however, we would broadly expect Ofgem's strategy over the next five years to be one of consolidating on the developments cited by Sir John against the background of the principles of best regulatory practice, as recently entrenched in statute. We believe that such consolidation will need to be accompanied by clear and compelling evidence of a strong contribution by Ofgem to the real and sustainable reduction demanded by the government in the regulatory burden faced by British industry.

Indeed, one of the tests of success for Ofgem's supply licence review project, in which we intend to play a full and proactive part, will be the extent to which it can light a deregulatory beacon for other utility regulators by showing that reducing the burdens imposed by the stock of existing regulation can actually increase the quality and effectiveness of regulation overall.

Turning now to (1) metering policy and (2) network regulation:

1. We are concerned that Sir John's reference to further evolution in metering policy might mean that Ofgem is contemplating fresh initiatives in metering following a prolonged period of major upheaval for the industry. It is clear that a number of difficult and sometimes intractable metering-related issues remain outstanding. They include the potential customer impact of supplier or agent failure, the problems of compliance with the RGMA baseline, the implications of Transco's continuing dominance in the provision of gas metering services, the lack of a governance framework for IGTs, and the future provision of post-emergency metering arrangements.

All of these issues have substantial implications for the development of the energy industry's most fundamental customer-facing service. We believe that Ofgem must focus urgently, and with a more robust emphasis than before on its principal statutory objective to enhance consumer benefit, on working with the industry to resolve these issues. This work area should feature strongly in the new five-year plan, as should a clear commitment by Ofgem to formulate a comprehensive smart metering strategy. We see this as essential to enable the energy industry to achieve the long overdue modernisation of this neglected element of national infrastructure.

2. We accept Sir John's injunction to network operators to take full account of the needs and requirements of their customers. However, Ofgem itself also needs to build on the work undertaken as part of the last price control review to develop a better understanding of customers' interests with regard to regulated networks (i.e. where customers are unable to express a preference through competitive choice).

In particular, it is to be expected that the impact of regulatory incentives on outputs and efficiency will ensure that the most cost-effective gains are achieved first, potentially leaving behind prospective improvements that have increasingly higher marginal costs (for example, the fundamental changes to network architecture that may be necessary to achieve further gains in system reliability). It is therefore essential that Ofgem develops its understanding of customers' willingness to pay for such improvements in order to be able to demonstrate that it is making effective choices on their behalf in lieu of competition, and so fulfilling its statutory duty.

There are also two issues related to the management of the network price control review process that need to be brought into the development of Ofgem's five-year strategy. The first is the need to provide for increased use of Ofgem's own technical team (rather than external consultants) to assess and form judgements on appropriate work programmes and capital allowances. The second issue is the maintenance of a sufficiently robust in-house capability for the audit of distributor accounting practices in order to ensure that the data produced for cost benchmarking and regression analysis are truly and consistently comparable.

Although not cited by Sir John, we continue to believe that Ofgem has a key role to play in the area of social policy. We are fully supportive of the government's commitment to eradicate fuel poverty. However, as Ofgem is well aware, the causes of fuel poverty are wider than just energy costs. The government must take responsibility for those causes that are related to homes, health, and income, and must co-ordinate the efforts of the energy industry, government departments, and support agencies. Ofgem, for its part, should take a key role in ensuring that increased government support and involvement will in fact happen, and in encouraging other suppliers to follow EDF Energy's lead by entering the debate on social tariffs.

We hope that all of these comments will be helpful, and we look forward to commenting on your draft strategy in due course.

Yours sincerely

A handwritten signature in black ink, appearing to read 'D. Linford', with a long horizontal flourish extending to the right.

Denis Linford
Director of Regulation