



Andy MacFaul
Head of Government Affairs
Ofgem
9 Millbank
London
SW1P 3GE

Direct lines:
Tel: 020 7257 0132
Fax: 020 7257 0101
Tanya.Morrison@shell.com

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Dear Andy

Ofgem's three year strategy 2005-8

I refer to the letter from Sir John Mogg seeking views on the key challenges faced by the gas and electricity industries in the short to medium term; the action the Authority should consider taking to respond to these challenges and what priorities should be chosen. Shell Gas Direct (SGD) is a licensed shipper and a supplier to non-domestic gas customers; our comments therefore focus on issues relating to downstream gas industry issues.

Priorities and pace of industry change

SGD welcomes the introduction of an RPI-3 cost reduction target for Ofgem. We consider this a necessary check to ensure that the scope of regulatory activities does not grow. However, as we set in previous years, we continue to consider that Ofgem is too large given that there are competitive supply markets and well established approaches to regulating the natural monopolies. The indirect costs of Ofgem are significantly higher than direct costs and can lead to inefficient allocation of industry resources.

The key challenge that we continue to face as an industry is the level and pace of change. While some is driven by external events, the past 18 months has seen the implementation of RGMA and the changes required for Ofgem to permit National Grid to sell four of its distribution networks (DNs). We do not consider that sufficient effort was made by Ofgem to decrease or reprioritise workload from other sections while this work has been taken forward. Indeed, Ofgem staff appear unaware that there are overlapping requests for data, consultations, and implementation periods and the impact these have on both suppliers and on our customers. We would have expected Ofgem to prioritise security of supply earlier this year and remain concerned that work to overcome barriers to demand side management for the coming winter were given lower priority than work related to the DN Sale and to changing the cashout arrangements.

In our response last year, we expressed our concerns that Ofgem was establishing too many workgroups and that their work was difficult for all to follow. We continue to consider that further transparency could be achieved, perhaps by Ofgem establishing regular events for the industry, perhaps once per quarter, where overviews of progress in the various areas of work can be presented at one time. It will then be possible to see how the various initiatives fit together.

Regulation of natural monopolies.

We consider that the RPI-X formulation with regular, eg five-yearly, reviews is a good approach to regulating the revenue of natural monopolies. RPI-X provides a simple, clear and transparent incentive based approach which provides the stability to the competitive market to allow it to take forward investment and develop service offerings to the benefit of consumers.

Ofgem's effectiveness

While we welcome statements confirming Ofgem's commitment the principles of best regulatory practice., the task now must be to show that Ofgem is put these principles into action. We would also welcome an independent review of Ofgem's impact assessments. While we acknowledge that an internal review was carried out, a review taking into account the views of affected parties by an organisation not related to Ofgem would demonstrate accountability.

We are concerned that areas of work are re-initiated and then implemented based on the premise that Ofgem has "long wanted" such change. However, while the subject of proposed change remains consistent, the reasons given by Ofgem, the description of the change required can alter radically over the years. We consider that much more emphasis needs to be placed on Ofgem demonstrating that it has addressed issues and concerns raised previously by industry participants. It would be welcome if minutes of the Authority meetings and other documentation demonstrated that that Authority has been given clear, objective information on why the industry has not followed the suggested course of action, including outlines of outstanding issues that we had expected Ofgem to address.

We note that there Ofgem will be attempting to streamline and improve the quality of the processes for consultation. This should not undermine the requirement to properly consult the industry. Ofgem staff should also try to gain a better understanding of the system impacts of the changes they are proposing and the ability of the industry to absorb many over-lapping changes at once. In particular, Ofgem should refrain from starting up new areas of work until projects are fully implemented and "bedded down".

A practical approach to improving communications would be to ensure that the website is both up to date and user-friendly. The diary appears to be used only infrequently used giving little indication of upcoming publications. It is difficult to find documents and work areas and information sites are incomplete and out of date. Ofgem staff often recommend using Google to find documents on the site; this is helpful for single documents but not for finding areas of work. Ofgem e-mailed notifications would be more useful if the subject or title of the document being published was included in the subject header.

Conclusion

Shell Gas Direct welcomes opportunities to work with Ofgem. With competitive supply markets now established, Ofgem's priority should be to withdraw from proactive involvement in the industry, its structures and governance as much as possible. If a "light touch" regulatory approach is implemented, this will provide evidence that the market is working.

Yours sincerely

Tanya Morrison
Regulatory Affairs Manager