



Andy MacFaul
Head of Government Affairs
Ofgem
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3 March 2006

Dear Mr MacFaul

OFGEM'S CORPORATE STRATEGY AND PLAN 2006-11

The Energy Networks Association is funded by all of the licensed electricity and gas transmission and distribution companies in the UK.

We are pleased to have the opportunity to contribute to your five year Corporate Strategy for 2006-11. I apologise for the lateness of our response, but trust that you find the comments useful in shaping your work.

ENA's comments are confined to those themes which will directly impact on the energy networks sector, in particular that relating to regulating network monopolies.

Regulating Network Monopolies

ENA agrees that regulating energy network monopolies is a fundamental strand of Ofgem's work and recognises that Ofgem has identified the relevant issues within this theme. It is also important to recognise the important interaction between this the second of Ofgem's seven themes with the third, i.e. that related to security of Britain's energy supplies where efficient and timely investment in the networks will play an increasingly important role.

We have a number of specific comments on your theme of 'Regulating network monopolies' which are of particular importance to our members.

By their very nature, the energy network companies have to take a long term view of their businesses when planning for the future. Major investments may take years to complete and will remain in operation for tens of years. Ofgem as the regulator of these businesses' activities should therefore also be looking many

well connected

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years into the future to create the appropriate regulatory climate in which the companies will be operating and to provide clarity about its long term objectives.

The regulatory framework that is put in place by Ofgem will need to create the correct incentives on companies to deliver what is needed for the UK's networks over the longer term. This will require moving away from an emphasis on eliminating inefficiency and driving down costs, towards an increasing need for investment as it becomes apparent that the infrastructure assets are ageing and that like for like replacement will not secure the change in network capabilities that will be needed to meet rising customer expectations and changes in government objectives.

The most critical issue facing the network companies is the amount of new investment to undertake and the conclusion is that the horizon of capex spend needs to be extended beyond the current 5 year period to successfully and effectively meet a number of longer term government objectives in relation to climate change, security of supply and social access. This is not necessarily a debate about the duration of the price control but rather a reflection of some of the very long term challenges facing the industry and the investment required to support a longer term vision.

We believe therefore that Ofgem should give consideration to lengthening the time horizon of its corporate strategy to reflect more closely the time horizon of the companies it is regulating.

Financing Network Investment

We welcome the review of financing network investment that Ofgem is currently undertaking with Ofwat. Our belief is that a climate must be created which enables businesses to decide for themselves their own mixture of debt and equity. This requires investors to be sufficiently attracted to the sector, and to achieve this, two factors are especially important:

- a) The financial community requires certainty and continuity in the regulatory framework, especially since investment decisions invariably overlap a number of price control periods.
- b) There is increasing competition for capital across the world. Consequently, it will be important that the UK, and the energy sector in particular, is seen as an attractive place to invest that capital.



Price Control Reviews

During last year's consultation on the corporate strategy, ENA urged Ofgem to establish key regulatory principles for the regulation of the network companies during the forthcoming price reviews in order to ensure consistency of approach. We therefore welcome Ofgem's intention to incorporate the lessons learned during DPCR4 into the current Transmission and Gas Distribution price control reviews and agree that developing a clear and predictable approach will reduce uncertainty for our members and provide a stable framework for their long term decisions.

Security of Supply

A key question for the future development of networks is the extent to which customers will be prepared to pay for improvements to their quality of service and how these aspirations will be satisfied within the evolving regulatory framework. It will be important that Ofgem continues to canvass the views of customers in this regard to ensure that the companies have clear incentives to invest to deliver the appropriate quality of service. However the current arrangements (largely based around market research into customer's willingness to pay) do not adequately address the long term integrity and security of the network.

Europe

We are pleased that Ofgem has continued to make Europe one of its seven strategic themes and recognises that Europe will continue to become increasingly important in shaping the regulatory agenda. We agree that Ofgem has identified the relevant issues within this theme and support Ofgem's proposed approach to encouraging the enforcement of existing obligations elsewhere in Europe. It is important for investors that evolving regulation is consistent with UK regulatory policy and the operation of competitive markets. We also hope that Ofgem is able to provide an influence in a way that minimises any additional burdens on the energy industry in the UK. This would help to ensure EU regulation is proportionate and not overly interventionist.

Better Regulation

We recognise Ofgem's commitment to adopting the principles of better regulation and improving its efficiency. In particular, we welcome Ofgem setting



up a better regulation unit to take forward such issues, which should in turn lead to a reduction in regulation and also in the costs of regulation. The work on the Supply Licence Review is one such example of this desire to reduce the regulatory burden on the companies and seems to be making good progress. It is important however that great care is taken to ensure that not only customers remain protected but also that other market participants, such as the network companies, are not adversely affected by any of the amendments or removal of licence obligations without proper consideration and consultation.

We note the improvements made under Ofgem's Project Paperless initiative, however we would like to take this opportunity to reiterate the need for Ofgem to take full account of the effects on industry resources and therefore should actively monitor and manage the volume of consultations it produces. We also hope to see further development of regulatory impact assessments.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'N Goodall', with a horizontal line underneath.

Nick Goodall
Chief Executive

The Energy Networks Association is funded by the UK's electricity and gas transmission and distribution companies. Its Members and Associates are asset owners and operators including CE Electric, Central Networks, Chubu Electric, EDF Energy, ESB, Guernsey Electricity, Independent Power Networks, Jersey Electricity, Laing Energy, Manx Electricity, National Grid, Network Rail, Northern Gas Networks, Northern Ireland Electricity, Scottish & Southern Energy, Scotia Gas Networks, Scottish Power, Tepeco, United Utilities, Wales & West Utilities and Western Power Distribution.