

Wednesday, 24 May 2006

Attention: Heather Glass

Ofgem
9 Millbank
London SW1P 3GE

Cc: distributionpolicy@ofgem.gov.uk

Dear Heather,

Regulation of Independent Electricity Distributors: Consultation on Implications of Licence Applications from Affiliates of Existing Licensees

Thank you for the opportunity to comment on the options set out in your letter of 13 April.

Laing Energy is strongly opposed to the licensing of affiliates of distribution network operators (DNOs) who are contemplating in-area work. There appears to be little obvious purpose for agreeing to this other than to compete with independent DNOs (IDNOs) but doing so by loading costs onto the parents' main licensed business creating an obvious cross subsidy that will increase total costs to consumers. Permitting affiliates to compete for work with IDNOs could also have significant competitive detriments, especially given the early state of competition in this new and evolving market.

Of the options outlined, the only ones that we consider viable are either:

- to refuse to grant a licence; or
- to restrict any licence to exclude an affiliate DNO's host area.

We are surprised that, given the implications for competition, Ofgem may be contemplating an alternative way forward. The competitive detriments of the alternatives are clear and already referenced in the open letter, and include:

- preferential treatment by the DNO to its affiliate relative to other developers;
- better access to sensitive and planning information; and
- fewer and lesser incentives to provide enhanced service levels to customers by the affiliate if the proposal is awarded to them.

Over time, a DNO with an affiliate who cherry picks low cost sites can be expected to see its average costs rise enabling the affiliate to charge higher prices than would otherwise be the case. Furthermore, we believe the surveillance burden on Ofgem of enforcing fair competition between an affiliate and competing IDNOs in this area is probably excessive, and it is unclear what off-setting consumer benefits are likely to arise, up and above those enabled through permitting the IDNO to compete against the DNO. We consider that Ofgem's resources would be better targeted if it were to

facilitate further evolution of the framework to enable IDNOs to enter the market, ensuring that the regulation required to facilitate this is kept to the minimum and delivering its intended benefits.

Looking at the other options set out in the letter, it would seem illogical and inequitable to us to treat affiliates in the same way as other IDNOs. Further we do not understand how the third option (“grant licence, with modifications to provide additional protection for consumers”) would work, nor what is meant by option 4 (“modify the DNO’s licence and/or price control.”). In both cases, much more definition of the mechanics is required before these can be properly evaluated, and significant changes to the ring-fencing and disclosure arrangements operated by the DNO would be required as a minimum if either of these options were to be implemented.

Please let me know if you require any further comments or clarification of our views.

Yours sincerely,

Darren Grundy
Business Leader
Laing Energy Ltd