

John Costyn
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Ofgem
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1st February 2007



Dear John

OFGEM'S SUSTAINABLE DEVELOPMENT REPORT 2006

We welcome the opportunity to provide feedback on the report, responding specifically to the key question of 'what further action can Ofgem take to protect the interests of future generations of energy customers'.

We agree with the selection of the five priority areas that Ofgem has identified to structure the report and find the document a very useful summary of Ofgem's policy positions. However, as we will explain below, we do believe that in some areas of policy the regulator should take a longer term view in order to genuinely embed sustainability within its regulatory approach.

Theme 1: Managing the transition to a low carbon economy

EDF Energy strongly supports the European Union Emissions Trading Scheme (EU ETS) and believes that it is an important policy measure in the battle against climate change. Its current structure however is not capable of underwriting the investment needed to significantly reduce CO2 emissions in the electricity sector.

EDF Energy welcomes Ofgem's recognition that Government should explore alternative policies that could be operated in parallel to the EU ETS in order to provide the long term price signals needed to deliver investment in low carbon technologies. We also agree with Ofgem that auctioning of carbon allowances should occur sooner rather than later.

In principle, EDF Energy supports the expansion of the sectors and types of greenhouse gases incorporated within the EU ETS where reliable measuring, reporting and verification processes can be developed. The inclusion of these sectors should proceed at a pace that does not compromise the existing scheme and allows the market to adapt to changes. We recommend the creation of 'expansion criteria' to ensure consistent principles behind the expansion of the scheme.

We support Ofgem and Government's efforts to remove the barriers, and where appropriate provide incentives, for electricity generating technologies that have the potential to reduce carbon emissions. However, we do believe that it is essential that Ofgem and Government regularly review any incentives, to ensure that they are actually delivering significant carbon savings, at an acceptable cost to the consumer.

Where changes to incentive schemes are considered, the impact on investor confidence needs to be taken fully into account to avoid constraining investment.

We welcome Ofgem's intentions to publish revised green supply guidelines and monitor the first year of electricity suppliers' fuel mix disclosure requirements. Future issues of the sustainable development report should deliver analysis on the changing nature of the UK fuel mix.

Theme 2: Eradicating fuel poverty and protecting vulnerable customers

We welcome Ofgem's acknowledgment that fuel poverty is part of a wider problem of poverty and social exclusion and that there is a limit to the role that the industry and the regulator can play.

We support Ofgem's efforts to encourage Government, the regulator, suppliers, consumer bodies and other organisations to work together to target customers most in need. However, we strongly believe that Government must lead this process

Going forward we believe that there are several other key areas where Ofgem could take further action to protect the interests of current and future energy customers;

- support separation of EEC into two distinct targets; 1) Energy Efficiency; and 2) Fuel Poverty, which would allow better targeting of measures at the fuel poor;
- support new Government money for tackling hard to treat homes, e.g. by solid wall insulation; and
- actively step up the EnergySmart campaign to improve awareness and confidence in benefits of competition amongst more vulnerable customers.

Theme 3: Promoting energy saving

We agree with Ofgem that the market should reward investment in energy saving on an equivalent basis to energy consumption. We want to work closely with the regulator to achieve this transition to an energy services market.

We welcome future debate on cap and trade type programmes and agree with Ofgem's view that there must be evidence that these lead to genuine and cost effective carbon savings.

We believe that Ofgem should promote changes to the EEC that work in support of a competitive energy market with full flexibility for suppliers to innovate, and no undue disadvantage for any supplier.

Theme 4: Ensuring a secure and reliable gas and electricity supply

Security of supply is dependent on maintaining the long term availability of expertise and knowledge within the industry. We believe that in future, the report should consider this and identify areas where Ofgem can contribute. For example, Ofgem could provide 'use it or lose it' funding (in a similar way to its innovation funding incentives) for responsible price controlled companies, like EDF Energy's electricity distribution businesses, who invest in longer-term skills development programmes.

We welcome Ofgem's involvement in the planned trial of smart metering and other consumption feedback options. We believe that these trials should be of significant scale, over an appropriate time period, with full transparency of the results.

We believe that at present the industry is in danger of talking a lot about smart metering, but not making the breakthrough that is required to achieve uptake on a significant scale. We believe that Ofgem should reconsider whether it is still wise to put metering activities entirely within competitive market, which currently leaves suppliers to make the decision as to where and when they install smart meters. An alternative would be to give the responsibility for smart meter installation to the Distribution Network Operator (DNO), with the regulator gradually increasing the number of installations that the DNOs are required to make. This would ensure that we make the breakthrough needed, but would not prevent suppliers from using smart meters to provide energy efficiency products and any other additional services.

We believe that Ofgem has a major role in monitoring the success of the new ombudsman scheme. In addition, as a result of recent proposals, it is likely that energywatch will soon cease to exist. We believe that Ofgem will need to play a strong advisory role to the various consumer protection bodies, to ensure a smooth transition to any new system, so that no customers 'fall between the cracks'.

Theme 5 – Supporting improved environmental performance

Indicator 14 discusses the environmental impacts of electricity and gas networks. The document states that Ofgem takes companies' *regulatory* environmental requirements into account in setting price controls, but perhaps implies that going beyond these regulatory requirements would have an unacceptable impact on cost to the consumer. However, we believe that it is important for Ofgem to be aware that not going beyond regulatory requirements in managing environmental performance also has a cost to the consumer of the future. This cost may be difficult to measure, but is nonetheless real. A good example could concern how the replacement of fluid filled cables may be dealt with at the next electricity distribution price control review:

- There are social and environmental costs resulting from cable leakages (ground pollution, risk to health from pollution of water courses, congestion and disruption from cable repair works etc). These costs are externalised (i.e effectively ignored) if Ofgem only considers the financial costs avoided by not accelerating cable replacement.
- There are also security of supply issues here which Ofgem needs to consider. If a cable began to leak, then it may have to be de-energised.
- Replacement of fluid filled cables in large cities will cause major disruption and cannot be completed quickly. A long term plan covering many price control periods is needed to replace these assets, in order to minimise environmental damage and protect security of supply.

In general, we suggest that Ofgem conducts research into the costing (internalisation) of social and environmental impacts to better inform the cost-benefit assessment of various infrastructure investments, of which cable replacement is just one example. EDF Energy would be pleased to participate in any discussions in this area.

We support Ofgem's work with Defra to regulate the emissions of pollutants affecting air quality and acidification. Ofgem should ensure that the electricity generation industry is involved in discussions at the earliest possible stage.

Ofgem notes that there is scope for the report to incorporate additional indicators covering a wider range of environmental impacts (water usage and fly ash being the examples suggested). We suggest that Ofgem engage with industry and other stakeholders, in a process that confirms the priority environmental impacts that should be reported by Ofgem and the reasons for their selection.

We hope that this response to your report will be helpful. Please do not hesitate to contact me if there are any queries arising from our comments or if you think that further discussion would be useful.

I can confirm that this response may be placed on Ofgem's website.

Yours sincerely

A handwritten signature in black ink, appearing to read "D. Linford".

Denis Linford
Director of Regulation

EDF Energy
01.02.2007