

Mark Feather
Industry Codes and Licensing
Ofgem
9 Millbank
London
SW1P 3GE



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Dear Mark

EDF Energy Response to Ofgem Consultation 132/08: “Code Governance Review: Charging Methodology Governance Options”.

EDF Energy is one of the UK’s largest energy companies with activities throughout the energy chain. Our interests include coal, gas-fired and nuclear electricity generation, electricity networks and energy supply to end users. We have around 5.5 million electricity and gas customer accounts in the UK, including both residential and business users.

EDF Energy welcomes the opportunity to respond to this consultation. We support the work that Ofgem is undertaking in this area to ensure that an appropriate Governance Regime is developed that is suitable for the industry and can accommodate all market participants.

There are a number of interactions between the outcome of this review of Charging Methodology Governance, the ongoing Structure of Charges work being carried out by DNOs and Ofgem’s proposal for a common charging methodology and the Common Licence Modification. This response is, therefore, initially framed on an ‘as is’ basis with our thoughts on interaction at the end.

We support the further development of option 2: modifying the current licence regime to enable all code parties to raise modification proposals to network charging methodologies. We believe that this should be applied to all Network Operators (NWOs), including Independent Distribution Network Operators (IDNOs) and Independent Gas Transporters (IGTs). This will open up the charging methodologies to interested parties which should help to promote competition and potentially provide Ofgem with a choice of alternative proposals when making a judgement on a charging methodology change. However, we believe that significant further work is required on these arrangements to ensure that the risks are mitigated against. In addition, we consider that the licence could be drafted to allow Ofgem itself to propose changes to the charging methodologies in particular circumstances. We believe that this reflects the current arrangements, and creates a more formal route for any change that Ofgem believed would be beneficial.

EDF Energy considers that modifying the licence would avoid the issues associated with either bringing the charging methodologies under code governance or creating a separate charging code. If the methodologies were to be brought under the code, then Ofgem would need to address the issues of different relevant objectives between the code and charging

methodologies, the different consultation periods and the different decision processes associated with a charging change. In effect this would create a sub section of the current codes, with its own unique and specific rules and requirements. It would therefore appear more effective to create a new governance regime for the charging methodologies than bringing them under code governance. However, the creation of a separate code for charging arrangements would appear to go against Ofgem's objectives of the Governance regime to create a simpler and more transparent change process making the licence modification the preferred route.

We believe that the following areas need further development were Ofgem to choose to modify the current licence arrangements:

- Drafting of licence conditions so that change proposals were limited to code parties. This should help to limit the number of charging proposals raised and so ensure that the industry is not faced with a plethora of charge proposals creating a regulatory burden. In addition this will ensure that only those parties who are directly impacted by change proposals can raise them. We would however, note that we would expect any consultation to be open to all interested parties, and not limited to just code parties.
- Definition of change proposals that Ofgem can raise. We believe that in order to maintain Ofgem's impartiality that it would be best to allow Ofgem to raise topics and issues that they believe needed further investigation. These could then pass to the industry – potentially the licence holder(s) – to investigate further and furnish a report to Ofgem either detailing a defined change proposal or setting out the reasons and explanation as to why they do not feel a change is warranted.
- Limitations on the lead time/implementation dates of any proposal. As identified within the consultation document one risk associated with opening the methodologies up to numerous change proposals would be numerous change proposals implemented throughout the year creating volatile and unstable charges. This could be mitigated by requiring changes to coincide with price changes and setting a minimum implementation period for any change.
- Development of an appeals mechanism. We believe that it would be beneficial to develop an appeals mechanism for any changes that have been directed to implement. This could mimic the current arrangements for appealing code changes, or could utilise an independent expert. The latter option would probably represent a cost saving over a full competition commission appeal but would require an undertaking from Ofgem to adhere to any decision and would require a clear set of rules to be developed as to when a change proposal can be appealed.
- Alternative proposals. We believe that there may be a benefit in allowing code participants to raise alternative charge proposals. This would provide additional options to Ofgem when reaching an implementation decision, and should also guard against charge proposals being raised for commercial advantage as it would be likely that an alternative to these would be raised.
- Due to the problems in forecasting the workload in analysis of proposals and options raised by external parties to NWOs, we propose a pass through mechanism whereby NWOs are able to recover their modification costs. This should be included within the DR5 price control and the price controls of other NWOs when they are re-set.
- Development of a co-ordinated change process across NWOs. This would ensure that the change process is administered in a co-ordinated manner and any common charging methodologies remained consistent. We would note that arrangements for a common change process have already been adopted by the Gas Distribution Networks (GDNs).

As mentioned above there are a number of interactions with other areas of work in particular:

- The DNOs (under the auspices of the Electricity Networks Association) are currently working on developing a common charging methodology in all areas with the exception

of the EHV marginal cost model in line with Appendix 2 to Ofgem's 1 October 2008 decision document "Delivering the electricity distribution structure of charges project"; and

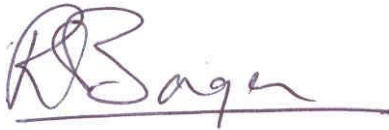
- Ofgem are currently consulting on a Competition Commission Referral following the rejection of Common Licence Modifications by Scottish & Southern and Scottish Power.

Although the timeline to which the DNOs are working to deliver commonality of methodology is very tight and given the levels of resources available to the industry we would like to see this work delivered and become the baseline from which future modifications are proposed rather than DNO's current charging methodologies.

Once a common (or mostly common) charging methodology has been achieved then it would seem appropriate that the commonality is retained where it is appropriate and that therefore there would need to be some linkage across DNOs to conduct the proposal analysis, consultation, report and decision processes. This requirement becomes even more important if there were to be a common licence condition on methodologies.

I hope you find these comments useful, however please contact me or my colleague Stefan Leedham (Stefan.leedham@edfenergy.com, 0203 126 2312) should you wish to discuss these in further detail.

Yours sincerely

A handwritten signature in purple ink that reads "R Baga".

Ravi Baga
Head of Policy, Regulation & Environment
Energy Branch

Appendix 1: Detailed Response to Questions raised in Ofgem Consultation: “Code Governance Review: Charging Methodology Governance Options”.

Chapter 2 Key Issues:

Question 1: Are there other key issues that should be considered? If so what impact would these have on NWOs and network users?

In addition to the key issues identified within our covering letter we would note that one of the key issues/risks that Ofgem does not appear to have addressed is whether opening up the charging regimes to 3rd party change would also introduce the possibility of Shippers/Suppliers proposing change for competitive advantage? Whilst this may be a risk, it is worth noting that the relevant objectives would not change and so any proposal would still have to demonstrate that it is cost reflective and non-discriminatory. In addition it is likely that other Shippers would remain interested in these changes and identify portfolio impacts. Therefore any “gaming” of the methodologies is likely to be flagged up by impacted parties. This could therefore be viewed as a minimal risk with suitable safeguards in place against this.

Question 2: Are there any aspects of the key issues that we have not addressed?

Question 3: Should Ofgem consider Governance arrangements for all charging methodologies on a common timetable, or seek to prioritise? If the latter, which methodologies do you consider should take priority and what would the benefits of this approach be?

There do not appear to be any pressing issues that would suggest a certain set of methodologies should be prioritised above another. In addition it would arguably create additional complexity and uncertainty were some methodologies to transfer to a new regime, whilst others remained unchanged. It would therefore appear beneficial to progress this issue on a common timetable, whilst recognising that the work and issues may vary for the different methodologies that may need to be considered independently. We would also note that given the current work that is taking place on the common charging methodologies for DNOs, it would appear logical for this work to be completed before implementing any new Governance arrangements.

Chapter 3: Options

Question 1: Are there alternative governance arrangements that could be considered appropriate for charging methodologies?

As previously noted, an additional option would be to keep the charging methodologies under the current Governance arrangements, whilst opening them up to allow 3rd parties to raise alternatives to any NWO proposal. This would mitigate against the majority of risks previously identified whilst opening the methodologies up to 3rd party change. In addition this would also encourage the adoption of the proposal that best met the relevant objectives. Under the current arrangements, Ofgem has to judge whether the proposal better meets the relevant objectives, which in certain circumstances can result in Ofgem accepting a proposal, whilst recognising that this may not be the best solution. An example of this could be Gas Distribution Network Charging Methodology proposal DNPC03, which introduced a 95/5 capacity commodity split. Whilst accepting the proposal as being more cost reflective than the current 50/50 split, their appeared to be the suggestion that it was not the most appropriate split. By opening the methodologies up to alternates, it is likely that Ofgem would have had a selection of proposals to chose from, which would have allowed Ofgem to implement what it believed was the most appropriate. However were this route to be employed then a mechanism would need to be introduced to ensure that dubious charging proposals were not raised to delay the implementation of a proposal. This could be resolved by allowing NWOs to seek a view from the authority on the appropriateness of any proposal, with the outcome of the authority’s view determining whether the proposal is retained or dismissed.

Question 2: Do you agree with our assessment of the options against the principles of the Review. Are there other impacts that we have not mentioned?

In general Ofgem's assessment of the options appears reasonable. However it would appear that the benefits of Option 4 in relation to a methodologies that are: "Governed by rules and processes that are Transparent and easily understood" have been over emphasised. Whilst it is recognised that the current codes are subject to different rules and procedures, EDF Energy understands that the aim of the Governance review is to address this specific issue. It could therefore be expected that these codes would develop a more common set of rules, and so the benefits of creating a new regime would appear to be over emphasised. In addition the creation of a new code under option 4 could create additional cost and complexity to all users. This would therefore potentially detract from the benefits which Ofgem has identified.

In addition we would note that due to the problems in forecasting the workload in analysis of proposals and options raised by external parties to NWOs, we propose a pass through mechanism whereby NWOs are able to recover their modification costs. This should be included within the DR5 price control and the price controls of other NWOs when they are re-set. This cost appears to have been excluded from all the Options that open up the charging methodologies.

Question 3: What are your views on the cost and risk mitigation measures set out in this chapter? Are there other mitigation measures that could be introduced?

As previously noted we believe measures should be introduced to ensure charging methodology changes can only be implemented to coincide with price changes and are accompanied by a minimum lead time. We believe that this reflects current industry requirements, either in Licence or under code, regarding price changes and notice periods and should help to ensure that market participants are not faced with unexpected price changes mid year. We therefore do not believe that exceptions to this rule are required, as we believe that this would create additional risk to market participants, and consumers who will have developed their position based on the information that is currently available to them.

We also do not believe that there should be an annual limit on the number of proposals that could be raised. Any limit would appear arbitrary and potentially prevent a proposal being implemented that would have a material benefit on the market in favour of another proposal that provides a limited benefit. For clarity we do not expect there to be a plethora of new charging proposals when these new arrangements are introduced, but would not want to artificially restrict any proposals that may be raised and developed.

We also do not believe that there should be a requirement to pass a threshold of support from network users in order to progress a charging methodology proposal. In particular we would note that this could potentially create a barrier to smaller participants raising a proposal and favour particular participants if it was based on market share, or licences. Instead we believe that the development and consultation process should provide an appropriate barrier for any proposals that do not meet the relevant objectives, and this should help to aid Ofgem's decision on whether to veto the proposal or not.