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## **Ofgem Five Year Strategy 2009-2014**

**- Initial comment by E.ON:**

E.ON welcomes the continuing consultation process for Ofgem's rolling 5 year strategy, and this opportunity to provide a response to the 2009-14 strategy. The commitment to full consultation is an important contribution to understanding how the Authority intends to interpret its statutory duties.

### **The Key Industry Challenges**

#### **The energy market**

We note Ofgem's response to growing consumer anxiety that rising energy prices are partially a symptom of a market which is not functioning properly, and await with interest the results of its probe into the energy supply market. We recognise the importance of providing consumers as well as politicians and interest groups with objective information about the functioning of the energy market and that consumers need to be assured that competition is functioning effectively. It is also important that consumers and broader stakeholders understand the longer-term implications for energy prices of rising fuel and raw material costs, substantial investment requirements for new capacity and the delivery of EU targets for renewable energy supply and we would like to see Ofgem also taking a more prominent public role in communicating this. More objective information will help consumers make better choices about their energy consumption and encourage investment in energy efficiency measures.

Ofgem also has an important role in ensuring that we maintain a stable regulatory and fiscal framework to reduce the risks, and thus the cost to the consumer, associated with the very large

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volumes of capital investment the industry has to undertake. We do not see Ofgem's implicit advocacy of taxes on the market value of emission credits allocated to the power sector as consistent with that role, particularly at this late stage in Phase II of the EU ETS.

In the wholesale market, there may be opportunities through the current code modification procedures to introduce arrangements which could improve the transparency of market data. By better facilitating an objective analysis of the market (through highlighting liquidity, for example), wholesale energy markets can demonstrate their efficiency and competitiveness.

#### **Distribution Price Control Review:**

The next Distribution Price Control (DPCR5) will be a key priority for, the network companies, the energy industry and consumers, given the central role of distribution networks in enabling delivery of the UK's energy policy goals.

Network companies have historically succeeded in reducing costs and driving prices down for consumers by some 50% in real terms since privatisation. However, DPCR4 signalled a need to change from a focus on driving efficiencies towards a focus on the need for new investment to replace an ageing asset base which was predominantly installed in the 1950s and 1960s.

The future requirements for our networks are also looking far less certain as new energy policy and new technological innovations across the industry lead to a new and different requirements for our networks.

This paradigm shift in energy policy has the potential to require networks to adopt a more proactive role than presently in facilitating their connections and building new assets, but contains significant uncertainties around the timescales and nature of this change and ultimately the impact such a change will have on distribution networks and their efficiency.

It is important that this changing role and inherent uncertainties are captured by the regulatory framework for DPCR5 such that networks, and indeed Ofgem in this regard, are seen as part of the solution for the country's energy needs, and in particular, are not seen as a barrier to the UK meeting its energy policy goals and commitments, such as the EU 2020 targets for renewable energy use.

#### **Renewable Electricity and Strategic Network Investment:**

The Renewable Energy Directive and the subsequent work which is currently being undertaken on the UK's Renewable Energy Strategy, suggest that a significant proportion of renewable energy is expected to come from the electricity sector, with some estimates suggesting around 35% by 2020.

Accommodating this level of renewable capacity on the electricity network will require significant investment in transmission assets. Ofgem needs to focus on how timely, efficient and strategic investments can be made to networks ahead of user commitments, as this may be required to meet the UK's mandatory renewable target. It would be helpful if Ofgem could clarify how it intends to approach this issue.

A major challenge will be enabling the market to reach the stretching renewables targets whilst balancing the cost to consumers resulting from transmission upgrades and those resulting from constraining generation.

**Policy Review:**

E.ON believes that the industry code modification processes generally serve to enhance the wholesale market arrangements. However, there have been some instances where anticipated implementation costs have been higher and anticipated benefits lower than expected.

If the industry is to gain the maximum benefit from a robust modification process it must have regard to the lessons from the past. In this respect, we believe that there is a strong case for a post project/policy review process.

**Code Modification Processes:**

Within the existing code modification processes we would also like to propose two areas for improvement:

Firstly, given that the ultimate decision-making power on industry amendments resides with the Authority, we would like to see a greater level of engagement by senior Ofgem staff during the modification deliberations.

Secondly, the industry is facing tough decisions as we strive to deliver clean, affordable and secure energy supplies. To assist with the challenges which continue to face we would like to see Ofgem focus on pragmatic solutions to issues such as grid access, rather than immediately turn to overly complex market mechanisms.

If you would like to discuss any of the matters raised within our response please do not hesitate to contact me.

Yours sincerely

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