

Andy MacFaul
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Ofgem
9 Millbank
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27 February 2009

Dear Andy

Proposed Corporate Strategy and Plan 2009-14

I am pleased to enclose EDF Energy's response to Ofgem's consultation: Proposed Corporate Strategy and Plan 2009-14.

As stated in our recent response to Ofgem's consultation addressing unfair price differentials, we welcome Ofgem's proposal to look beyond "probe-related remedies" from 2009 and to focus on the challenge of creating a more sustainable energy supply system while maintaining secure supplies. Delivery of a more sustainable market will require significant investment from energy companies. Energy companies must be allowed the flexibility to operate efficiently and profitably within the context of a strong competitive market for energy that compares favourably with any in the world.

With regard to networks, we believe that Ofgem and Industry should work together to develop an integrated approach to demand management, in the light of the considerable challenges involved in meeting the UK's statutory carbon reduction and renewable energy targets. Ofgem should carry out a detailed examination of the future role and scope of the electricity distribution business that will be required to meet these objectives. We will be pleased to play our role in such a review.


Like Ofgem, we believe that competitive markets and a stable long term regulatory and policy framework are the best way to ensure security of energy supply and to support the significant investment in infrastructure required to meet the UK's energy policy objectives. At the same time, it has to be recognised that a number of policy interventions have been and continue to be made by government to achieve particular social and environmental objectives. In this context, we believe that Ofgem has a vital role in assessing the extent to which the market will deliver a sustainable energy supply system. Where problems are identified, Ofgem has a duty to propose and implement whatever changes in market arrangements are required.

Finally, we welcome Ofgem's continued commitment to leading work to achieve a competitive and sustainable EU energy market through CEER and ERGEG. As a member of EDF Group we strongly support the development of a single, integrated energy market across the EU.

I attach our more detailed response to your consultation. We hope you will find these comments helpful and we look forward to seeing the final Corporate Strategy in March.

If you have any queries on this response, please do not hesitate to contact me.

Yours sincerely

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

Denis Linford
Director of Regulation

Attachment

Proposed Corporate Strategy and Plan 2009-14

EDF Energy's detailed response

Key points:

Competition and Fuel Poverty:

- It is essential that any “probe-related remedies” introduced by Ofgem strengthen, rather than undermine, the elements that make the market competitive.
- Companies must be able to continue to develop product and price differentiation and innovation, to drive further choice and competitiveness.
- We accept that there is a case for further improvements in the way the market works for particular customer groups and we are working with Ofgem to implement these improvements.
- Changes will not be achieved overnight. Each initiative must be subject to proper consultation and consideration.
- It is essential that any new supply licence obligation that seeks to address unfair price differentials should be proportionate to the improvements the market needs.
- The supply system needs substantial investment over the coming decade and any significant re-regulation of what is essentially a competitive supply market will simply drive up the cost of that investment to the detriment of customers
- Support for vulnerable customers is the one area where greater commonality is needed. This is a social issue not an energy issue. Those who struggle to pay energy bills will also struggle to pay for other essential services. We are doing much already, but we support properly funded mandatory social tariffs as the only sustainable solution going forward.

Wholesale Markets:

- An appropriate regulatory and competition law framework to prevent abusive behaviour is already in place and we would be strongly against any moves to introduce new or additional sector-specific market abuse powers.

Metering:

- EDF Energy supports the roll-out of domestic smart metering as long as the method of delivery is chosen with a view to it being carried out as efficiently and effectively as possible.
- With this in mind we wish to participate in discussions with Government and Ofgem as to the best market model for the roll out of smart meters.

Distributed Energy:

- We recognise that low carbon decentralised energy can play a role in achieving the UK's targets in reducing carbon emissions and increasing low carbon electricity and heat generation. However, given its relatively high costs in most circumstances, distributed generation (DG), including decentralised energy, cannot provide the whole solution and a diverse mix of both centralised and decentralised low carbon generation will be required.

Networks:

- We support the need to retain and develop an appropriate incentive framework for regulating energy networks and Ofgem's proposals for a stronger emphasis in future on quality of service and network risk.
- Ofgem should build on its important LENS work before the next price control is settled, in view of the urgency of national energy policy objectives to which DNOs must contribute, the high levels of transmission investment required, and need for effective management of distribution networks.
- Ofgem and the industry should therefore work together to prioritise the development of a more considered and integrated approach to demand-side management. This work should start before the conclusion of DPCR5,
- Ofgem's final corporate plan needs to provide detailed consideration of the future role and scope of the electricity distribution business needed to deliver the UK's objectives of reducing carbon emissions and ensuring security of supply and how any new services offered by DNOs will be funded.

Sustainable Development:

- We supported changes to Ofgem's duties which promoted sustainable development, but believe that ideally Ofgem's statutory duties should be realigned with the overriding objective of a secure and sustainable energy system of energy supply in order to strengthen regulatory support for the investment required in the UK's energy infrastructure.

Transmission Access Review (TAR):

- We support the objectives of TAR, so long as the outcome does not create undue and unmanageable costs for consumers and does not distort competition within the UK market or create undue uncertainty for companies seeking to deploy the necessary low carbon investment.

Security of Supply:

- We agree with Ofgem that competitive markets and a stable long term regulatory and policy framework to facilitate investment are the best way to ensure security of energy supplies and welcome its commitment to work with Government and other stakeholders to remove barriers to delivering secure supplies, such as planning.
- New market mechanisms should only be introduced where the benefits to customers are demonstrated or where these mechanisms support the long term investment required in the industry.
- We agree with Ofgem on the importance of the EU ETS and would welcome greater predictability of the carbon price and early clarity on the scheme beyond 2020.

European Union (EU):

- We agree with Ofgem on the need to achieve a single, integrated EU energy market that works for UK consumers and that the creation of regional markets is an important practical step in achieving this.
- Rather than of full ownership unbundling of transmission networks, the objective of enhancing competition could also be achieved through the creation of regional Independent Systems Operators.

Better Regulation:

- The RPI-3 per cent internal cost control target should not have the effect of reducing Ofgem's regulatory resources available to deliver the right DPCR5 outcome or to carry out its duties with respect to the Competition Act.

Response to issues raised in the consultation

Chapter 1 - Creating and Sustaining Competition

As we have stated in previous responses, Ofgem should aim for stability in regulating the wholesale and retail energy markets, especially in the light of the significant investment in infrastructure that will be necessary to deliver the Government's commitment to a low carbon future, with targets to reach 15% of energy from renewables by 2020 and an 80% cut in carbon emissions by 2050. Regular regulatory intervention increases investors' perception of risk, the cost of capital for the industry and will also potentially have negative consequences for consumers.

Price Probe

As stated in our recent response to Ofgem's consultation: addressing unfair price differentials, our key points are as follows:

- It is essential that any "probe-related remedies" introduced by Ofgem strengthen, rather than undermine, the elements that make the market competitive.
- Companies must be able to continue to develop product and price differentiation and innovation, to drive further choice and competitiveness.
- We accept that there is a case for further improvements in the way the market works for particular customer groups and we are working with Ofgem to implement these improvements.
- Changes will not be achieved overnight. Each initiative must be subject to proper consultation and consideration.
- It is essential that any new supply licence obligation that seeks to address unfair price differentials should be proportionate to the improvements the market needs.
- The supply system needs substantial investment over the coming decade and any significant re-regulation of what is essentially a competitive supply market will simply drive up the cost of that investment to the detriment of customers
- Support for vulnerable customers is the one area where greater commonality is needed. This is a social issue not an energy issue. Those who struggle to pay energy bills will also struggle to pay for other essential services. We are doing much already, but we support properly funded mandatory social tariffs as the only sustainable solution going forward.

Wholesale Markets

Regarding Ofgem's comments on wholesale markets, we fully recognise the need for properly functioning energy markets that operate in a transparent and orderly fashion.

Like other markets, the scope for market abuse can exist. It is therefore important that an appropriate regulatory framework is in place to prevent and protect against abusive behaviour, which could negatively affect competition and the integrity of the market generally. That framework already exists through the provisions of existing European and national competition law and specific market rules and regulations (which can be changed at short notice if required). We would therefore have very serious concerns with any moves to introduce new or additional sector-specific market abuse powers.

Metering

We support Government's expectation that all customers should have smart meters with information displays within a ten year roll out period. We believe that Smart meters can play an important role in helping to deliver the government's energy efficiency targets for 2020 and 2050 and could help to reduce the cost of achieving the renewables target.

It is important that the approach to smart metering roll-out is chosen with a view to it being carried out as efficiently and effectively as possible. With this in mind we wish to participate in discussions with Government and Ofgem as to the best market model for the roll out of smart meters.

We therefore support Ofgem's proposal to take forward work with DECC on the details of the roll out of smart meters and would welcome an early decision on this.

In addition, we would welcome further clarity on the following issues in Ofgem's Corporate Strategy:

- An assessment of options for addressing the stranded costs of legacy meters as a result of an accelerated Smart Meter roll-out;
- Mandate for smart meters for business customers, including SMEs, and any code changes required;
- 'Minimum spec' for Smart Metering for Residential or SMEs.
- Ofgem's role in delivering a central programme to support the roll out of smart meters.

Distributed Energy

We welcome Ofgem's proposals and further commitment to remove barriers to decentralised generation (DG) and recognise that this can play a role in achieving the UK's targets to reduce carbon emissions and increase low carbon electricity and heat generation. However, DG, including distributed energy, can at best only provide a partial solution and a diverse mix of both centralised and decentralised low carbon

generation will be required to deliver the UK Government's aspirations to mitigate climate change.

Chapter 2 - Regulating networks effectively

The consultation continues the emphasis of Ofgem's previous corporate plans on the need to retain and develop an appropriate incentive framework for regulating energy networks. We support this approach in principle and Ofgem's proposals to add to it with a stronger emphasis in future on explicit output measures relating to quality of service and network risk.

However, we are concerned that Ofgem does not intend to build on its important LENS work, in order to establish how the role of distributors might be developed to tackle climate change and ensure secure energy supplies, until after the next price control is settled. This timeframe does not reflect the urgency of the national energy policy objectives to which distributors are now expected to contribute.

The review of longer-term network scenarios in the final LENS report shows that a very wide range of potential outcomes is possible due to national policy objectives and other potential change agents over the longer term. However, it is already clear that the current direction of the government's renewable energy strategy will lead to a need for both high levels of transmission investment and for distribution networks to be more actively, and proactively, managed in future.

Ofgem and the industry should therefore work together to prioritise the development of a more considered and integrated approach to demand-side management. This work should start before the conclusion of DPCR5, particularly since it will need to consider the future roles of suppliers, network operators, system operators, potential new players such as aggregators and virtual power plant operators, and customers, to identify how they can all interact in an effective and co-ordinated manner.

We believe that the final plan needs to provide detailed consideration of whether the role and scope of the electricity distribution business may need to be enlarged to deliver the UK's objectives of reducing carbon emissions and ensuring security of supply. The current DPCR5 process indicates that Ofgem expects DNOs to offer a whole new range of DSM and associated services, but there needs to be recognition of how the costs of administering these will be funded and by whom.

We therefore hope that, in finalising its strategy, Ofgem will initiate a wide-ranging structural debate on the appropriate future role and scope of DNO activities in the context of the industry's ability to deliver national energy policy objectives. We will be pleased to play our role in such a debate.

Chapter 3 - Helping to achieve sustainable development

Ofgem's Statutory Duties

We welcome changes, introduced in the Energy Act 2008, which promote sustainable development in the order of Ofgem's priorities, and make it clearer that interests of both future and existing customers must be protected. These changes are likely to have a positive impact on Ofgem's activities. However, as stated in our response to the consultation on BERR's Social and Economic Guidance to Ofgem, we believe that ideally Ofgem's statutory duties should be realigned with the overriding objective of a secure and sustainable energy system of energy supply in order to strengthen regulatory support for the considerable transformation and investment required in the UK's energy infrastructure to meet the UK's carbon reduction and renewables targets.

Transmission Access Review

The current objectives of the Transmission Access Review (TAR) are to facilitate the grid connection of renewables and other low carbon generation in a timely manner. The UK Government has a target of 15% energy from renewables by 2020 and views TAR as part of the solution together with the Government's overarching energy policy goals. We believe that planning and appropriate changes to the SQSS are key to connecting more generation going forward. Notwithstanding this, we do support the objectives of TAR, so long as the outcome does not create undue and unmanageable costs for consumers and does not distort competition within the UK market or create undue uncertainty for companies seeking to deploy the necessary low carbon investment.

However, there is a danger that TAR brings changes to transmission access and charging which will:

- Undermine future investment in new transmission capacity
- Provide inappropriate signals for future generation investment and threaten security of supply (if TAR results in removing generators' firm access rights)
- Create instant windfall winners and losers within industry.

The future focus of TAR should be on delivering sufficient transmission capacity to deliver an effective electricity market consistent with the Government's energy policy objectives and should avoid unnecessary secondary changes. (e.g. MWh charging).

Chapter 4 - Helping to protect the security of Britain's energy supplies

We agree with Ofgem that competitive markets and a stable long term regulatory and policy framework to facilitate investment are the best way to ensure security of energy

supplies and welcome its commitment to work with Government and other stakeholders to remove barriers to delivering secure supplies, such as planning.

New market mechanisms should only be introduced where the benefits to customers are demonstrated or where these mechanisms support the long term investment required in the industry.

Transparency and timely availability of information are also important and in this respect we welcome Ofgem's continuing work with DECC on the Energy Markets Outlook and the medium to longer term analysis on challenges to security of supply. The 2009 report will be of particular significance, as Ofgem states, in the light of the EU Energy package, UK Renewable Energy Strategy and policy measures to achieve the first UK carbon budgets under the Climate Change Act.

We agree with Ofgem on the importance of the EU ETS and welcome recent European Commission amendments to provide greater predictability on the carbon price. In addition, we agree on the need to have early clarity on the scheme beyond 2020. In this respect, key areas of uncertainty going forward are:

- The final emissions reduction target for 2020 to be adopted by the EU and the possible revision of the linear reduction factor used to set the cap;
- Links between the EU ETS in light of the potential introduction of other international schemes;
- Use of CDM and other project credits beyond 2020;
- How the future expansion of the scheme will be managed into phase III and beyond.

With regard to using EU ETS auction receipts to tackle fuel poverty, as set out below, and in our response to Ofgem's recent consultations on the price probe, we believe that the common funding of a mandatory social tariff is the only sustainable solution going forward.

Chapter 5 - A leading voice in Europe

We agree with Ofgem on the need to achieve a single, integrated EU energy market that works for UK consumers and that the creation of regional markets is an important practical step in achieving this. We support Ofgem's continued engagement and leading role in its work with the Council of European Energy Regulator's (CEER) and European Regulator's Group for Electricity and Gas (ERGEG).

We recognise that the approach to liberalisation that we have taken in Great Britain may not be the best approach across the whole of the EU. In place of full ownership

unbundling, objectives of market integration could also be achieved through the creation of regional Independent Systems Operators.

There is still a need to carefully consider the compatibility and consistency of the UK market arrangements with those in the developing EU energy markets. In the context of a competitive single European energy market, it would be neither appropriate nor efficient for there to be significantly different, more complex or more burdensome arrangements than in the UK e.g. differing approaches to transmission charging (including transmission losses) arrangements.

Chapter 6 - Helping to tackle fuel poverty

We agree with Ofgem that fuel poverty is ultimately the responsibility of Government, as it is part of a wider problem caused by a combination of factors, including low incomes, poor housing conditions and high household costs.

EDF Energy has worked closely with Ofgem during 2008 to develop and deliver a number of new voluntary commitments, including the Fuel Poverty Action Programme and the Social Obligation agreed with Government. Such activity will continue to play an important role in supporting our most vulnerable customers, and there will be an ongoing role for Ofgem in helping to deliver supplier collaboration with Government on projects such as data sharing.

As outlined above, and in our recent response to the price probe, we believe that there should be greater commonality between energy suppliers to support vulnerable consumers and we support properly funded mandatory social tariffs as the only sustainable solution going forward.

Chapter 7 - Better Regulation

We believe that Ofgem on the whole has carried out its duties over the past five years in a way that has been consistent with the principle of better regulation, and in certain cases has increased the quality and effectiveness of its regulatory process overall. We support Ofgem's continuing commitment to better regulation principles going forward.

Whilst we support Ofgem's aims to run operations as efficiently and cost effective as possible, as we have stated in previous responses on Ofgem's corporate strategy, the RPI-3 per cent internal cost control should not have the effect of reducing Ofgem's regulatory resources available to deliver on the DPCR5.

We also note Ofgem's recent decision to close the Competition Act investigation into Scottish Power and Scottish & Southern Energy on the grounds of administrative

priority despite Ofgem having concerns with the observed behaviour. In the letter to industry dated 19 January 2009, Ofgem cited the resources required to investigate the matter further, as one of the factors that influenced its decision. Clearly these issues have significant potential to seriously distort competition within the UK market and Ofgem needs to ensure that it maintains and is seen to maintain its effectiveness by having sufficient resource to take appropriate action in these circumstances.

EDF Energy
February 2009