

Andy MacFaul
Head of Better Regulation
Ofgem
9 Millbank
London
SW1P 3GE

Direct line 01925 534504
Direct fax 01925 534571
paul.bircham@enwlimited.co.uk

18 September 2009

Dear Andy

OFGEM'S FIVE YEAR STRATEGY 2010-15

I write in response to Lord Mogg's letter of 28 July. As usual, we welcome the opportunity to contribute to the development of Ofgem's thinking based on a set of themes that are consistent from one year to the next and that allows for greater consistency of approach. We are pleased to provide the following comments:

1. Key challenges facing the industry in the short to medium term.

The Government's recent announcements on energy policy and the forthcoming Energy Bill will have a greater impact on DNOs than the Energy Act 2008. We perceive a gathering pace in the movement towards a low carbon economy and anticipate that our industry will need to maintain as much flexibility as possible in our arrangements and frameworks to ensure we respond promptly when required to do so.

As we have indicated previously, the gradual replacement of energy network assets needs to be planned over a substantial period and it is important that managing investment is not limited to five year price control windows. We hope the good work done on long-term future electricity scenarios can address this issue and that this initiative combined with the results of the Distribution Price Control Review will facilitate this issue.

Whilst we anticipate that the UK will recover from recession in the next year or so, the global economic crisis has resulted in a step change in investor confidence and risk/return balances. We must be conscious of the implications for investor confidence of every regulatory decision to ensure that the energy industry is able to finance the huge investments required in the next 25 years.

This response is not the vehicle for addressing concerns we have regarding progress with the Distribution price review. However, we must emphasise generally that as capital expenditure requirements continue to grow especially with the new generation requirements, it is essential that investors continue to be attracted to the energy sector and the results of DPCR5 must send

out important messages of regulatory consistency to potential investors. There must be a realistic acceptance by all parties that the cost impact of the connection of more Distributed Energy will be significant and that a failure to recognise this in the eventual DPCR5 settlement will not be beneficial to customers in the medium-long term.

2. What action is needed from Ofgem?

Ofgem's key role is to ensure that networks deliver their services efficiently and facilitate effective markets to deliver outcomes that meet both consumer requirements and broader Government policy objectives. We see a number of areas for actions during the coming years under the headings below:

2.1 Energy Bill

The new Bill will be published later this year and reflect developing Government policy on renewables and Distributed Generation. If Government targets are to be met, the need to ensure that the growth of distributed generation is effectively managed is paramount.

2.2 Distribution price control review (DPCR5)

Please refer to our earlier comments above and in the Priorities section. We would stress that the settlement will need to be flexible given the uncertainty of the economy and the extent of change for distributors given the potential rise in Distributed Energy.

2.3 Sustainable Development

The facilitation of a low carbon economy is an important driver for the Distribution review and the forthcoming legislation impacting on issues such as the revenue driver, losses, DG and smart meters. The future development of offshore wind generation and new nuclear generation will be an important element in reducing carbon emissions. It is important that Ofgem can adapt their stance on the regulatory framework to meet the renewable challenges. The increasing focus on the development Smart Grids, and particularly for example electric vehicles, as a way of reducing CO2 emissions will bring load management issues for the networks and would require significant investment and thinking. It is clear that Ofgem will have to match the political drive designed to facilitate renewable energy and try to ensure that the technical, commercial and regulatory barriers to allowing for sufficient network capacity can be overcome.

2.4 Connections

We welcome the acknowledgement in Ofgem's DPCR5 Initial proposals of the need for DNOs to earn a margin with reference to connections. This area of our business has developed more rapidly and effectively in the North West than in other parts of the UK and this should be recognised by Ofgem in developing policy in this area. Ofgem should concentrate on making the existing market for contestable services more effective across the country.

3 Priorities

Our consistent theme in response to previous consultations on strategy has been to try and focus on a smaller number of key projects. This has been put into sharper focus this year by our real concern about the quality of some of Ofgem's modelling work during the DPCR5 process. Ofgem's self imposed RPI-X cost control has shown that there is a real lack of resources to do

accurate and thorough analysis - leading to potentially damaging proposals for customers. Ofgem need to ensure that they are adequately resourced and simple cost cutting is inappropriate particularly when the results impact on customers and companies alike. Ofgem must ensure they are appropriately focussed and do not spend too much time and resource monitoring and regulating they high profile and politically sensitive energy markets and too little regulating monopolies.

Neither the industry, nor its regulator, has the resources to tackle too many projects simultaneously, doing so increases the risk of unintended interactions.

I hope you find these comments helpful. I would be pleased to join in further discussion on the issues raised.

Yours sincerely,

Paul Bircham
Regulation Director
Electricity North West Limited