

Abid Sheikh
Industry Codes and Licensing
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27 September 2010

Dear Abid,

Open Letter Consultation: Potential Significant Code Reviews (SCRs)

Thank you for the opportunity to respond to the above consultation document. I can confirm that this response is not confidential and may be placed on Ofgem's website.

EDF Energy believes that a more coordinated and transparent approach to the development and delivery of strategic change would be beneficial to both market participants and consumers. We support measures that are designed to introduce efficient governance arrangements. However, any increase in regulatory control over the code modification processes, as provided by the SCR arrangements, requires appropriate checks and balances to be built into the governance process in order to protect market confidence.

Ofgem's recently published guidance on the launch and conduct of SCRs indicates that there will be Industry consultation on the initiation and potential scope of an SCR, intensive consultation during the SCR, and an industry led implementation process via the current code processes. These measures should help ensure that key market reforms are progressed more appropriately and efficiently, and so deliver benefits for consumers.

In its open letter, Ofgem identifies a number of priority areas which could be appropriately addressed through an SCR. We offer the following views on each of these areas.

Electricity cash-out

Given the significant challenges ahead for the energy sector, including the need for substantial levels of investment, the Government is planning to publish a wide-ranging consultation on electricity market reform in the autumn, with a White Paper targeted at spring 2011. The review is expected to cover all aspects of the electricity market, including an assessment of the role that a carbon price, an emissions performance standard, a revised renewables obligation, Feed-in Tariffs, capacity mechanisms and other interventions, could play in delivering a system that supports the delivery of a secure, low carbon energy system.

Given that imbalance cash-out pricing is likely to remain a cornerstone of the wholesale electricity market arrangements, it will clearly be considered as part of the Government's review. As the conclusions of the market reform are likely to have material implications for the design of GB cash-out arrangements, we would question the appropriateness of any separate Ofgem led review.

We note that in your letter, you say that Ofgem's three priority areas (which includes electricity cash-out) are "consistent with the Government's high-level policy framework". However, Ofgem does not elaborate or justify this statement. From our perspective, the proposed SCR in this area would seem to provide a parallel, and hence unwelcome, stream of work which will sit uncomfortably alongside the Government's review.

We recognise that Ofgem made a commitment to undertake a post implementation review (after 12 months) to understand whether BSC Modification P217A has had any impact on cash-out prices, and to establish whether further change was necessary. This review was in part, intended to assess the "PAR" (depth of bid/offer averaging) parameter in the imbalance cash-out pricing formulation introduced by P217A. Given the current arrangements have now been in place for some ten months, there is a good deal of confidence that a meaningful review could now be undertaken. However, there is no need for a SCR process to achieve this – a successful outcome can be achieved under business-as-usual BSC/Elexon industry processes.

Gas Security of supply

Ofgem proposes to investigate the case for more dynamic cash-out prices at Stage 2 of a gas emergency, and also that it may more generally look at potential reforms to the cash-out arrangements applicable at other (non-emergency) times.

We recognise that the UK is moving to a world of increasing reliance on gas imports, however, any need for a review of gas cash-out arrangements needs to be fully supported by specific evidence that there is a problem that needs resolving. We do not believe that an SCR in this area will be supported by the industry until Ofgem is able to clearly and robustly demonstrate the need for it.

In any case, one of the objectives in developing changes to the industry code governance arrangements was to facilitate a holistic review of code-based issues, including issues that crossed codes and/or licences.

There can be a strong level of interaction between the gas and electricity wholesale markets in which significant change in one can have material consequences for the other. For example, a sharper price signal during a gas emergency could impact on decisions whether or not to run a CCGT plant. For this reason, in the event that a SCR on cash-out is initiated, we believe there would be clear benefits in having a single review to cover both fuels/codes at the same time.

We have said above, that we do not believe that a review of electricity cash-out arrangements is sensible in light of the Government's forthcoming review of trading arrangements. Given, the strong interaction between the electricity and gas regimes, this implies that no review of gas emergency cash-out arrangements should take place until the government's review is completed, and then only if there is a demonstrable need.

Smart metering impact on wider industry processes

We believe it is sensible for both existing industry processes, including settlements and change of supplier, to be reviewed alongside the development of the Smart Metering Implantation Programme (SMIP). A thorough review of the wider industry processes is

required to ensure that an appropriate industry governance framework for smart meters is implemented in a timely and coordinated manner. We therefore agree that an SCR should be launched at the end of the year. We note, however, that any SCR work would need to be performed in a coordinated manner so as to take account of smart metering work being undertaken by the SMIP, and in other areas outside of the SCR process, such as the development of the Smart Energy Code etc.

Transmission Charging Arrangements

Ofgem has recently launched a comprehensive review of the charging regime and associated connection arrangements for using the GB transmission network for electricity and gas ("Project TransmiT").

We note that Ofgem's thinking in this area is at a preliminary stage, and that it is not currently consulting on whether to launch an SCR in this area. Our initial view is that, given the changing governance of transmission charging, an SCR approach is likely to be appropriate so that necessary changes can be implemented in a timely and efficient way.

Conclusion

We note that Ofgem has previously indicated that it would envisage undertaking only one or two SCRs in a typical year in light of the significant level of resources likely to be required by both industry and regulator. We agree with Ofgem's view and believe that the number of SCRs active at any one time needs to be minimised. We believe that the only SCR's which should take place in 2011 are those covering smart metering and Project TransmiT. We do not support an SCR on cash-out on either electricity or gas, because of the strongly interactions between them and with the Government's review.

Should you wish to discuss any of the issues raised in our response or have any queries please contact me on 020 7752 2187.

Yours sincerely,

A handwritten signature in blue ink that reads "Paul Delamare".

Paul Delamare
Head of Regulation