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Ofgem  
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30 September 2010

Dear Rachel

### **Open letter consultation on Gas Distribution Price Control Review 2 (GDPCR2) – the way forward**

Thank you for the opportunity to comment on Ofgem's letter regarding the way forward for the Gas Distribution Price Control Review 2 (GDPCR2). I can confirm that this response is not confidential and can be published on the Ofgem website.

EDF Energy is one of the UK's largest energy companies with activities throughout the energy chain. We provide 50% of the UK's low carbon generation. Our interests include nuclear, coal and gas-fired electricity generation, renewables, combined heat and power plants, and energy supply to end users. We have over 5 million electricity and gas customer accounts in the UK, including both residential and business users.

The key points of our response are as follows:

- We agree that Ofgem has correctly identified the key issues for GDPCR2, and fully support a fundamental review of the funding and governance of xoserve.
- The approach to developing output measures described by Ofgem seems reasonable and the initial thoughts on output categories are appropriate.
- We are satisfied with the anticipated level of stakeholder engagement but request that Ofgem work closely with distribution network owners to align consultations, workshops and seminars to minimise the resource requirements of GDPCR2.
- The initial business plan guidance should provide distribution licensees with a reasonable indication of Ofgem's expectations.
- We welcome publication of the key milestones and the timetable for the review. This seems challenging and so we suggest that there should be some flexibility in the timetable.
- There should be a fundamental review of the NTS to LDZ metering standards to ensure that they are fit for purpose.

EDF Energy has taken considerable interest in the development of the RPI-X@20 framework. In our response to the recent consultation on the recommendations, we were

able to offer support to the large majority of proposals, but we were concerned about the difficulty of implementing certain aspects and the lack of detail in some areas. As a consequence we intend to take a close interest in both the Gas Distribution and Electricity Transmission price control reviews and look forward to engaging positively with both in order to realise the potential of the RIIO framework. As such, we reserve the bulk of our response to this open letter on the proposed structure, process and timetable.

## **Key Issues**

### *Environmental Issues*

We note that all of the Gas Distribution Networks (GDNs) have environmental policies and statements published on their websites outlining corporate commitments made with regard to environmental impact. When setting incentives the GDNs' corporate commitments should be taken into account to ensure that the incentives fund incremental actions. We also believe in the principle of using actual settlement data to identify shrinkage volumes. This has been the subject of significant industry debate for several years, and yet 98.5% of gas supply points are still not settled based on meter readings. We therefore question whether using actual settlement data to identify shrinkage volumes would represent a material improvement without fundamental reform of the settlement systems in gas.

### *Demand uncertainty*

We share Ofgem's concerns regarding demand forecasting and the perverse incentives that might exist. The assumptions behind the demand forecasts should be subject to scrutiny by industry and be compared with other demand forecasts that are being used as part of the GDPCR process.

### *Xoserve*

We fully support Ofgem's views regarding xoserve. As a gas shipper and electricity supplier we are aware of the very different service levels provided by xoserve and Elexon. While the services between the two are not perfectly matched we note that Elexon delivers its services for a similar budget to those provided by xoserve (even though Elexon has a higher overhead cost mainly due to its central London location). Given the developments with smart, DCC and Project nexus, we believe that this review represents a unique opportunity to review the desired services and most appropriate service provider. We believe that key to addressing this issue would be to:

- subject xoserve to a separate price control from that of the Gas Transporters,
- review the Governance of xoserve so that they are subject to wider industry control, and
- conduct an open tender to ensure that these services are provided in the most efficient manner

### *Traffic Management Act*

We consider that if an allowance is set for the Traffic Management Act, a firm allowance is preferable to the use of a re-opener. Our experience to date is that a number of permitting schemes in London and the South East are now fully in operation and hence it should be possible for GDNs impacted by live schemes to develop robust forecasts of the associated costs.

### *Metering Errors*

Ofgem should review the arrangements and standards around the NTS to LDZ metering interfaces. Currently any meter errors represent a risk to the Reconciliation by Difference community, which will ultimately be paid for by customers. In particular we note that there have been numerous meter errors reported in the last 12 months, all of which will result in a debit to Shippers in the region of £60m. We believe that this indicates that the current arrangements and standards are not fit for purpose and should be subject to a fundamental review as part of the GDP2.0.

## **Primary Outputs**

We support the shift in focus to the delivery of outputs. The six categories of output seem comprehensive and, as is stated, echo the discussions on primary outputs from DPCR5. We hope that all relevant stakeholders have had the opportunity to be involved in the development of these outputs from the outset.

## **Enhanced Engagement**

The proposals for stakeholder engagement are in line with our expectation from the RPI-X@20 recommendations and, through the use of the various mechanisms described, offer the prospect of a thorough engagement process.

We note that Ofgem is proposing to undertake Willingness to Pay (WTP) research. It was our understanding from the RPI-X@20 recommendations that the Network Companies would be expected to undertake such research. We appreciate that there may be good reasons to conduct a 'national view' to supplement the views of stakeholders in a particular region. We hope this will not create any duplication of effort in this activity, and emphasise our view that regional preferences must take precedence if company business plans are to be seen as responsive to local requirements.

## **Business Plan Guidance**

We welcome the detail provided in the letter on the anticipated content of the business case, building as it does on the RPI-X@20 recommendations.

## Key Milestones

We are supportive of many aspects of the new regulatory framework. We are therefore keen to ensure that these positive developments are not lost in attempting to stick to a strict timetable.

There are two areas of the timetable where we have particular concerns:

### *Stakeholder Engagement and production of initial business plans*

As enhanced engagement is intended to be at the heart of the R10 framework, we do not believe that the current timetable allows a full debate with stakeholders over their requirements, testing of their preferences and then subsequent validation of the proposed business plans.

We note that a number of the GDNs are currently publishing pre-consultation documents asking fundamental questions, such as who their stakeholders are, and seeking views on appropriate methods of engagement. However, companies will be expected to submit their initial business plans in around ten months. Approximately seven months has been allowed from the release of the Initial Strategy consultation document through to submission of the initial business plan, with four months allowed from publication of the business plan templates to their submission. We question whether this gives adequate time for stakeholder engagement, as it would require engagement both in respect of development of the various options stemming from the strategy document and then validation of the content of business plans to be submitted.

We note that Ofgem has allowed around six months for consideration of the business plans. We believe there may be a benefit in allowing more time to the GDNs for production of their initial business plans. This might provide more opportunity for stakeholder engagement, which combined with the greater preparation time should lead to a better quality submission. It would also have the benefit of giving Ofgem greater time to work on other issues such as financeability, tax, pensions etc., work which will need to have been completed if one or more companies are to follow the fast-track process.

### *Production of the Initial Proposals*

Experience from DPCR5 would suggest that publishing a comprehensive set of Initial Proposals in July 2012 will be challenging, if final business plans are not submitted until April 2012.

In the DPCR5 process, the July initial proposals were followed by a September update and two further updates in October. In addition, a number of significant elements of the final price control settlement, such as the Cost of Capital, were not completed until the final proposals.

We believe that Ofgem should be explicit about the contents within the initial proposal, as this will allow all parties to focus on the decisions that will need to be made. There may also be a benefit in developing a contingency plan which would allow for a September paper to deal with a more defined set of issues or decisions, rather than an update on the initial proposals. This will then give greater certainty to the companies on the likely shape of the final settlement.

Further to the points above in respect of the price control timetable, we believe that Ofgem should be conscious that this is a new process and that difficulties might arise in its operation which were not foreseen in the RPI-X@20 project. We have been concerned that there were areas of the recommendations which lacked detail, quite understandably, and it is during these price controls that these detailed issues will need to be worked through.

Ofgem also needs to be mindful of the fact that it is running two price control reviews in parallel. There is a risk of both the organisation and the industry becoming over-stretched by the demands that this will bring.

Should you wish to discuss any of the issues raised in our response or have any queries please contact my colleague Rob Rome on 01452 653170 or myself.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'D. Linford', with a long horizontal flourish extending to the right.

**Denis Linford**  
**Corporate Policy and Regulation Director**