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Dear Andy

Ofgem's Five Year Strategy 2011-2016

I refer to the open letter of 30 July and am pleased to respond with views on the development of Ofgem's next five year strategy.

As Lord Mogg notes in the open letter, we recognise that this is a period of significant uncertainty for Ofgem, against a background of the change of government, the publication of the first government Annual Statement of energy policy and the continuing economic situation, affecting all companies in the sector as well as public spending priorities.

We believe that one of the main themes for Ofgem's work remains that of ensuring security of energy supply, as we have mentioned in successive inputs to Ofgem's corporate planning process. There is also, in our view, a need for Ofgem to radically cut back on its day-to-day level of intervention in the competitive markets, where continuing initiatives, in the wake of an intensive period of re-regulation of the supply market, is threatening to undermine the stability of these markets. Finally, we are acutely aware that ongoing developments at European level have a great influence over the markets in the UK and we value Ofgem's continuing role in seeking to ensure that European harmonisation preserves the benefits of the pro-competitive markets in the UK. These topics are discussed in more detail below.

Security of Supply

SSE has engaged over the last year or so with Ofgem's "Project Discovery" which covers the outlook for security of supply in the light of potential challenges facing the sector as a whole over the next decade. In particular, we responded in April this year to the second consultation on the results of Ofgem's work, where specific issues were highlighted. We think it would be very pertinent for Ofgem's corporate strategy document to set out what Ofgem itself is now going to do in the light of the issues raised. As the main outcome of Ofgem's Discovery work confirms that there are continuing risks to security of supply, it is appropriate that all bodies that can



influence the development of the market are clear about the actions that they can each take to minimise risks to security of supply.

In this context, it is extremely welcome that Ofgem have announced a review of transmission charges. It is vital that the review considers the impact of those charges on carbon targets and wider system security. Going forward, we would urge Ofgem to ensure that security of supply is front and centre of all decision making and policy development going forward such that the necessary appetite for investment is maintained in the markets.

Overall, we believe that Ofgem should work with Government and with the grain of the existing market structure to propose modest targeted interventions that would stabilise and confirm its overall policy framework around security of supply. It should also amend the economic policies within its own control to ensure that they align with the best possible outcome for security of supply.

Reduction in Regulation

In keeping with the well-publicised Government targets for reduction in public sector spending, we are aware that Ofgem is considering its own budget and scope of activity going forward, in parallel with the Government's recently announced review. In this context, we believe it would be very helpful for Ofgem to plan to radically reduce the amount and scope of regulatory interventions across the "business as usual" activities in the energy markets.

Perhaps the area where Ofgem's level of intervention is causing most concern is that of the energy supply markets in the wake of the intense period of re-regulation of this competitive market following the energy supply Probe, the outcome of which was finally implemented in July this year. The increased level of detailed regulation in this area is in real danger of undermining the competitive market – reducing the ability of companies to differentiate their services and encumbering normal competitive processes with detailed prescriptive requirements. Regulation should always be proportionate to the issues identified and we would like to see no additional regulatory burdens or initiatives proposed in this area going forward. A period of regulatory stability is required.

For energy suppliers, as well as for Government and Ofgem, the smart metering project is also a significant challenge that will demand material resources and effort for the companies to bring forward successfully. It is, as Ofgem is aware, a project that will fundamentally change the way that supply companies, their agents and customers will interact and the whole timescale for delivery is under pressure. A wide range of benefits have been identified with this project for customers, for innovation and for the security of supply and sustainability agenda. It would be helpful therefore if Ofgem could support the companies by focussing resource on the achievement of this project rather than continuing to review detailed issues associated with the current supply market arrangements, which naturally diverts resource within the supply companies when they need to address and respond on these topics.

European Engagement

In the European theme of work, the implementation of the new package of energy legislation is currently underway and clearly of great importance to the development of energy markets in the UK. We continue to believe that Ofgem has a key role to



play in the European institutions in ensuring that the harmonisation of measures in Europe does not undermine the competitive market structure which has evolved in the UK. In particular, in the medium term, we are aware of the project to harmonise industry network codes across Europe. We look to Ofgem to be in the vanguard of preserving the benefits of the UK's code content and governance structures as this project unfolds.

I hope these comments are helpful. These are challenging times for companies, customers, regulators and Government. We have set out above what we believe to be the three most important considerations for Ofgem when finalising its strategy for the next few years. Naturally, I would be very happy to contribute further to the debate, if that would be helpful.

Yours sincerely

Rob McDonald
Director of Regulation