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Ofgem's Forward Work Programme FY2013-14

Dear Philip,

We welcome the opportunity to respond to Ofgem's proposed Forward Work Programme for 2013-14, and to comment on the key projects planned for this period. Our response is provided on behalf of the RWE group of companies that includes: RWE Npower plc, RWE Innogy GmbH and RWE Generation SE.

We present our comments to the projects listed under the four themes in the following pages, but we provide a high level summary below of some of our main points.

- **Retail Market Review** – we support the work towards more simple and transparent measures to enable customers to navigate through the market, but are surprised that Ofgem has opted to restrict choice so much. We do not agree that there is insufficient competition in the energy retail market. With regards to the non-domestic market, we believe Ofgem must allow sufficient time for new measures to be developed by suppliers before new licence conditions can take effect.
- **Conclude Enforcement Review** – we consider that Ofgem's enforcement arrangements for its investigations are not fit for purpose, and believe it is difficult to challenge Ofgem. We feel the best approach would be both the overseeing of the conduct of the investigation and the decision in relation to any investigation, were not made by Ofgem. Our view would be that Ofgem would benefit from appointing an expert adviser to provide necessary expertise. We would strongly support greater dialogue between all parties, increased quality of updates from Ofgem, and greater clarity over the principal issues of concern.
- **Gas Security of Supply and Significant Code Review** - we believe that the GB market is already widely regarded as the benchmark for a competitive, liquid and efficient wholesale gas market. Further intervention will be detrimental to the market and will increase customer costs. Ofgem has identified a gap in security of supply from capping VoLL. We do not agree that there will be a gap. In our view, sharpening price signals from the current cash-out arrangements will be sufficient to deliver further investment in both the demand and supply side which will enhance security of supply.

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- **Smart meters, smart grids and LCNF** - we support the Smarter Markets Strategy and believe that it must take the long term in mind (to 2050), with clear sight of what smarter markets may look like at intermediate dates. We believe the LCNF and Smart Grid Forum have been successful in bringing together suppliers, generators and networks that enables solving short term industry issues.
- **Finalise Consumer Vulnerability Strategy proposals** – we have reservations about Ofgem’s proposal for suppliers to adopt the standard which is at the core of its proposed vulnerability strategy. We believe this will add significant costs to suppliers without equal benefits, whilst possibly alienating some customers.
- **Manage transition from CERT and CESP to ECO** - we believe that there still remains uncertainty about the extent of the ECO and its impact, and this will therefore affect the transition from CERT and CESP. The interaction with Green Deal adds another degree of complexity. Therefore, as administrators for ECO, CERT and CESP, we would hope Ofgem will apply discretion of how this role is discharged.

Yours sincerely,

Jill Brown

Economic Regulation

Theme 1 – Promoting value for money

Key Ofgem projects planned for 2013-14:

- Follow through the **Retail Market Review (RMR)** and implement proposals

Domestic

We support the desire to work towards a more simple and transparent market for customers, recognizing the need for choice in a competitive market. We therefore agree that some simplification would help customers to navigate the market. However, given the importance of customer choice in the market and the benefits of innovation (both of which have been championed by Ofgem), we are surprised that Ofgem has opted to restrict choice so much, by setting a limit of only four tariffs and is proposing rules which will stymie the innovative proportions offered, for example, by Telecom Plus. In weighing the merits of simplicity against choice and innovation, we strongly believe that Ofgem is creating a system which will prove detrimental to customers.

We do not agree with Ofgem's assertion that there is insufficient competition in the energy retail market as we believe this is not supported by the evidence. A key concern of RMR is that it reinforces the impact of the competitive distortions arising from exemptions for small suppliers, and which undermines the scope for their larger rivals to compete with them.

We foresee two serious potential consequences of RMR and the small supplier exemption policies:

- a) It encourages inefficient new-entry based on short term cost advantage and risky business models which is ultimately to customer detriment if they exit the market due to rising costs.
- b) Ofgem's consultation documents admit a degree of uncertainty as to whether the proposals will have the desired effect of engaging the least active customers. One credible outcome is a migration of the more active customers towards low cost offerings by small suppliers, leaving the least active and potentially more vulnerable customers to fund a disproportionate share of the cost of social and environmental programmes and obligations.

Non-domestic

We have been involved in the RMR discussion groups and have fed our views into the consultations. We support many of the proposals and consider that they will improve the customer experience. However, Ofgem must allow sufficient time for the new measures to be developed by all suppliers before any new licence conditions take effect.

We are particularly concerned with the enforcement proposals for standards of conduct, which we consider will be inevitably subjective. The enforcement framework should ensure consistency of decision making, which these proposals do not; and this is especially important in view of the proposals for consumer redress.

- A review of regulatory framework for **Third Party Intermediaries (TPI)**

We welcome Ofgem's stated intention to review the regulatory framework as it might apply to TPIs. In doing so we would hope Ofgem draws the appropriate distinction between addressing specific issues in the non-domestic sector with respect to TPIs, and the separate strand of encompassing into its remit the responsibility for overseeing the role in the market of domestic online comparison services, including their expansion into other sales channels. The latter involves Ofgem picking up responsibility for the voluntary mechanism that is the Confidence Code from Consumer Focus, and addressing through its

consultation ensuring that domestic brokers move into other channels in an appropriate manner, particularly if they are, or are claiming they are, replicating their online model.

Within the non-domestic market we support the general proposition that TPIs should be regulated in an effort to increase quality and consumer confidence in that area. Our preference is that they should be directly regulated by Ofgem perhaps under the Business Protection from Misleading Marketing Regulations. However, we would also support the development of a single code of practice for all TPIs enforced by Ofgem, with accredited TPIs only being able to operate within the market. Suppliers, through a condition in their licences, could be prevented from using all but accredited TPIs.

We look forward to contributing to Ofgem's further review and the development of its proposals.

- *Implement **wholesale energy market integrity (REMIT)***

RWE will continue to work closely with DECC and Ofgem in GB on the development of REMIT as well as communicating with ACER and the European Commission along with ENTSO-E on the Electricity Transparency Regulation. Given the new nature of REMIT's regulatory requirements and enforcement powers, we will look to Ofgem to provide full support and guidance in these areas. In addition, we would welcome education for large customers caught by REMIT, as they will have to register (or arrange to be registered) with Ofgem as market participants.

- *Pursue **price control review for electricity distribution (RIIO – ED1)***

In our response to 52/12 *Mitigating Network Charging Volatility arising from the Price Control Settlement* (April 2012), we highlighted our concerns that RIIO-ED1 has the potential to create significant volatility in network charges. RIIO-ED1 will be different from previous price controls in terms of the levels of investment that need to be made by DNOs to meet the new requirements of Smart Grid, low carbon technologies, etc. This, when combined with a regulatory framework based around baseline allowances with additional revenue triggered from incentive or uncertainty mechanisms, will increase the uncertainty around price control revenue. We welcome Ofgem's proposals to improve the predictability of allowed revenues and therefore network charges, but we still believe that a focus on these issues should be retained.

A positive aspect of the RIIO-T1 process was the level of stakeholder engagement. We expect that this will continue to be a key element of RIIO-ED1, although given the number of DNOs, coordination needs to be carefully considered to allow efficient utilisation of industry resources.

- *Engage with regulatory design for **smart meter rollout***

We support Ofgem's work in this area and view it as being closely related to the smarter markets development work. The key is to solve quickly any regulatory hurdles that may impede rollout, and encourage small or large suppliers to install SMETS compliant (smart metering equipment technical specifications) smart meters in a manner that minimises risk to customer experience. We believe that agent and DCC charging methodologies form an important component of this, and in ensuring commercial interoperability and a level playing field for all.

- *Conclude **Enforcement Review***

In general, we consider that Ofgem's enforcement arrangements for its investigations are not fit for purpose. In effect, Ofgem brings the action and makes the decision, albeit within different areas of Ofgem. We believe it is difficult to challenge Ofgem when it has not followed the correct process, because, unlike court proceedings there is no judicial presence holding for example pre-trial reviews, to ensure that Ofgem is compliant with its obligations in the Enforcement Guidelines. We feel the best approach would be both the overseeing of the conduct of the investigation and the decision in relation to any investigation, were not made by Ofgem.

However, if the current arrangements continue where Ofgem's enforcement section brings and progresses the action and then the Authority decides on an outcome, then at the very least we believe there must be:

- a) a third party who can intervene on the conduct of the investigation, and
- b) a clear right of appeal to the decision on the merits of the case.

Whilst we support the standards of conduct, given the potential impact of regulatory breaches triggering customer redress claims, it is increasingly important that Ofgem decisions are appealable on the merits (to an independent body). In addition, our view would be that Ofgem would benefit from appointing an expert adviser, such as a judge or QC, to the Enforcement Committee to provide expertise particularly on the reasonable person test.

- *Conclude a number of **mis-selling investigations***

Given the time that has elapsed, we look forward to some or all of the investigations concluding in the near future, and to the appropriate lessons-learned as part of Ofgem's wider, general review of its enforcement process. This will help ensure that such exercises are proportionate, targeted and consistent in their application to licensees.

- *Publish final proposals to address electricity **theft***

We have supported the industry's work on theft issues for a number of years not least because we recognise the significant safety risks involved in meter interference and the additional costs to honest customers.

We have been closely involved with Ofgem and industry work streams to deliver the new gas theft processes and licence conditions. We've also worked closely with industry colleagues to agree a new code of practice for dealing with electricity theft and look forward to helping deliver further improvements to the electricity processes this year to align them with gas.

Theme 2 – Promoting security of supply

Key Ofgem projects planned for 2013-14:

- *Take forward work following the **Gas Security of Supply Report**, including gas storage*

It is unclear to us which elements of its report Ofgem intends to take forward. The report concluded that supplies to domestic consumers were secure in all but the most extreme combination of circumstances.

Our understanding is that DECC will consider the case for any storage intervention. Under its Proposed Final Decision¹ Ofgem identifies a gap in security of supply from capping VoLL. We do not agree that there will be a gap. In our view, sharpening price signals from the current cash-out arrangements will be sufficient to deliver further investment in both the demand and supply side that will enhance security of supply. The GB market already comfortably exceeds the infrastructure and supply standard laid out in the Security of Supply Regulation 994/2010. If Ofgem is concerned, we believe it should set out what security standard it requires to be delivered and the costs and benefits of meeting it.

- *Complete the **Significant Code Review (SCR)** in relation to a **Gas Deficit Emergency***

We welcome Ofgem's initiative to respond to industry concerns by setting up policy discussion workgroups to explore key policy design questions, and believe that this should facilitate completion of the SCR. Any solution should:

- Improve the signals that come from the present cash-out arrangements with a minimum level of further market intervention. The demand-side is important, but it should be a matter for customers and shippers to determine the value of providing the services, possibly alongside a last resort mechanism;
- Exclude automatic compensation at VoLL for involuntary demand side response (DSR). The fundamental assumption that it will create incentives for customers to sign commercial interruption contracts with shippers is incorrect, and will only create additional financial risk;
- Be implemented through standard UNC governance, which will allow alternative solutions to be considered; allow development of workable business rules, and permit full consideration of wider industry policy initiatives including Electricity Market Reform and gas security of supply further interventions; and
- Include a lead time of at least two years so that Shippers and Suppliers can reflect any new arrangements in their forward contracting strategies.

- *Develop proposals under a **Electricity Balancing SCR** to improve charging arrangements*

We welcome that Ofgem has taken on board consultation responses that suggested industry should be involved in developing proposals. We look forward to participating in the expert group.

- *Work with **ACER and European Regulators** on development of network codes to implement **European Target Model***

We support Ofgem's approach on EU issues and active approach in ACER in particular on the development of the Network Codes including its participation domestically in the Joint European Standing Group. We look for this to continue and once the Codes have passed through the legislative process, for Ofgem to consult fully on their implementation in GB. In the case of the Network Code on connection requirements for generators (NC RfG), we would expect this to be through the Grid Code. On NC RfG we also would stress the importance of the cost benefit analysis to determine whether the

¹ 11/12 Gas Security of Supply Significant Code Review - Proposed Final Decision

NC RfG applies to existing plant, being carried out by a party independent of the TSO (i.e. National Grid).

- *Take forward plans to consult on **Integrated Transmission Planning Regulation (ITPR)** across the planning and delivery of onshore, offshore and cross-border transmission.*

We welcome the joined up approach to regulation set out in the ITPR project. However, we believe that Ofgem's work in this area should be careful not to introduce any additional cost or risks for renewable generation projects already in development or operation.

Theme 3 – Promoting sustainability

Key Ofgem projects planned for 2013-14:

- *Run the annual competition for innovative electricity distribution projects funded through the **Low Carbon Networks Fund (LCNF)***

We believe that the Low Carbon Network Fund and the Smart Grid Forum have been very successful in bringing together suppliers, generators and networks in a manner that enables the solving of short term industry issues relating to responsibilities around meters, data and network efficiency, and the longer term evolution of an industry design that can keep both the customer at the centre of the design, whilst facilitating the network innovation required to manage the highly challenging electrical flows of the future. We support the work of the SGF and in particular to progress of the specific workstreams.

Whilst recognising the high cost of the LCNF, we do believe that it has delivered value for money, as each project has brought together networks, generators and consumers in novel ways, which now provides a rich source both for the possibilities of network management, consumer engagement, and network innovation, but also for the potential evolution of the retail market design.

We recognise that networks play a vital role in delivering low carbon generation projects. We are concerned by the threat of potential increases to transmission use of systems charges in England and Wales under Project TransmiT and by the overall number of changes being proposed in relation to network charging over the next few years. Ongoing regulatory stability is very important in order to facilitate the delivery of renewable projects.

- *Progress the **Smarter Markets Strategy***

We support the Smarter Markets Strategy and the structure of the four key areas. We believe it essential that the strategy has the long term (2050) in mind, with as clear as possible sight of what smarter markets may look like at intermediate dates (for example, 2020, 2030). Each activity has a different mix of importance, urgency and range of possible outcomes. For example, we believe that unified registration in the DCC; unification of gas and power processes, and high resolution settlements and supplier volume allocation, are all essential longer term goals. In the shorter term, it is essential that Change of Supplier works as well as it possibly can for now and at each stage of industry evolution.

- *Finalise the **Consumer Vulnerability Strategy** proposals*

While clearly it is important for suppliers to keep, and be kept, up to date regarding their customers' circumstances, Ofgem will have seen from our response to the consultation at the end of last year that we have significant reservations about the proposal for suppliers to adopt the standard BS18477, which seems to be at the core of Ofgem's proposed vulnerability strategy. Without repeating the points made in our response, if applied across-the-board, the Standard will, in all likelihood, add significantly to suppliers' costs with questionable benefits, and with the possibility of alienating some customers, as it will require a degree of intrusion that they will find unacceptable.

We would, therefore, strongly urge Ofgem to discuss and consult fully with suppliers before finalising its proposals in this area.

- *Maintain monitoring and reporting of suppliers' obligations towards customers at risk of **debt or disconnection***

In our domestic systems we have implemented the required changes to reporting this information based on Ofgem's new requirements. It has been far from easy; and while we welcome Ofgem's cooperation and assistance during the period while the revised reporting was being implemented, we would urge strongly that no new requirements are introduced in the medium term.

Following receipt of Ofgem's non-domestic "spring package" letter towards the end of 2011, we began to voluntarily report the number of disconnections for micro business customers and have reviewed our debt and disconnections processes. We have also attended joint meetings with Ofgem and Consumer Focus to examine those processes and are pleased to say that feedback has been positive. We will continue to review in the light of the December 2012 open letter from Ofgem, which outlines good practice expectations. By doing so we will continue to fulfil our aim of treating customers fairly and helping those in debt wherever possible.

- *Publish revised guidance on **approach to impact assessments***

Any impact assessment (IA) framework must ensure a transparent and consistent approach, whilst providing for a process that allows a case-by-case basis to be addressed in a proportional and realistic manner as distinct from long-run, more complex issues. Any IA process must also be able to be reviewed and challenged, particularly where more qualitative rather than quantitative considerations are being presented.

Industry must also be able to contribute to discussions regarding any key tests that Ofgem will be proposing, and how they are to be applied. Furthermore, any IA framework that Ofgem devises, especially where it encompasses environmental and strategic sustainability considerations, must be mindful of overlap with other government departments and other regulatory authorities, to ensure minimal 'double-accounting' occurs.

Theme 4 – Ensuring efficient delivery of Government’s consumer and environmental programmes

Key Ofgem projects planned for 2013-14:

- *Regulate **offshore transmission***

We continue to support the Offshore Transmission Owner (OFTO) regime and support continued operation of the generator build model. We also support incremental improvements to the existing OFTO regime including proposals to improve the availability incentive.

- *Manage the transition from the **Carbon Emissions Reduction Target** and the **Community Energy Saving Programmes** to the **Energy Company Obligation***

There is still a considerable amount of uncertainty about the extent of the ECO and its impact (both in terms how it will be delivered and the associated cost). This is still being discussed with Government. Clearly, therefore, this will affect the transition from CERT and CESP.

There are some significant lessons to be learned from how the policy intent for domestic efficiency was to be driven by legislation, and how the Order was implemented and to be enforced in practice. Whilst we recognise that ECO extends beyond Ofgem’s remit, we do believe that the design of the ECO Orders, and of the transition from one regime to the next (in this case ECO1 to ECO2) must be informed by the insights and experiences gained by Ofgem. There have in addition, been real challenges in setting the ECO obligations in a short period after laying of the Order. Early consultation on the details of obligation setting would be helpful for obligations in the future.

Related to this, will be the interaction with Green Deal, which again adds a degree of complexity that suppliers will be required to grapple with. As administrators of ECO, CERT and CESP, we would hope and expect Ofgem to apply its discretion in terms of how this role is discharged.

- *Administer the **Warm Home Discount**, **Renewables Obligation** and **Feed-In Tariff** schemes*

The Warm Homes Discount and the Feed in Tariff had implementation effects that were not envisaged in the legislation. We recognise that Ofgem must at all times be consistent with the legislation, but at the same time, believe that it is also essential that Ofgem bear in mind the policy intent. Where these conflict, then we believe that Ofgem should use what discretion is available to it and be mindful of the best outcomes for consumers.

We welcome Ofgem’s recent consultations on the administration of the Renewables Obligation (RO): ‘Fuel Measurement and Sampling Guidance’ and ‘Guidance for Generators’, and welcome the opportunity to feed back our experience to enable the administration of the process to be efficient and effective. We would urge Ofgem to be pragmatic in its approach and to take account of the operational activities of stations when administering the requirements of the RO.