



Ofgem  
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### **Update on the Electricity Balancing Significant Code Review (EBSCR) and request for comments on proposed new process to review future trading arrangements**

EDF Energy is one of the UK's largest energy companies with activities throughout the energy chain. Our interests include nuclear, coal and gas-fired electricity generation, renewables, and energy supply to end users. We have over five million electricity and gas customer accounts in the UK, including residential and business users.

We welcome Ofgem's decision to reduce the scope of the EBSCR. Focussing on longstanding and reasonably well understood issues could lead to potential "quick wins" for implementation in 2014 or 2015, providing a more certain framework for investment resulting from the proposed Electricity Market Reform (EMR) arrangements.

We also support the proposal to launch a new project on the design of future electricity trading arrangements. There are several parallel initiatives being developed both in the EU and GB and a holistic approach is required to consider the strong interactions between the multiple drivers of change in the electricity market. However, it must be made clear, not only from the outset but on an ongoing basis, that the objective of the project is to make EMR, the EU Target Model and the other initiatives work as intended and not to redesign them. The temptation to tinker with pre-defined components of future arrangements or solve potential problems immediately must be resisted. This is particularly important to mitigate investor uncertainty.

Ensuring an appropriate scope for the project will be critical. There is a need to establish clearly what the issues are that this project is trying to address. This may be more complex than initially assumed. The first phase of the project should focus on clearly defining its scope, and securing stakeholder agreement to that scope, including with Government.

Our detailed responses are set out in the attachment to this letter. Should you wish to discuss any of the issues raised in our response or have any queries, please contact Mark Cox on 01452 658415, or myself.

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I confirm that this letter and its attachment may be published on Ofgem's website.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Angela Pearce".

**Angela Pearce**  
Corporate Policy and Regulation Director

## Attachment

### Update on the Electricity Balancing Significant Code Review (EBSCR) and request for comments on proposed new process to review future trading arrangements

#### EDF Energy's response to your questions

#### **Q1. Do you agree Ofgem should launch a project to create a high level design for the future electricity trading arrangements?**

Yes. We welcome the proposal to set up a new project to create a high level design for the future electricity trading arrangements. There are several parallel initiatives being developed both within GB and in Europe and a holistic approach is required to consider the strong interactions between the multiple drivers of change in the electricity market. We agree that without a clear and common understanding of the future trading arrangements, we could end up with an incoherent set of mechanisms borne from a piecemeal approach to market reform, and/or a series of overlapping reforms which may involve undoing previous decisions within a short space of time. Clearly, we should make every attempt to avoid this situation.

Since Ofgem's proposed approach is to build on the successful characteristics of NETA and consider potential changes to align with the 'pre-defined' components of the future arrangements such as the EMR CfD instrument design and the EU Target Model Network Codes, the project should enhance investor certainty rather than create regulatory risk. However, Ofgem must not lose sight of the objective of the project (i.e. to make EMR and EU Target Model work as intended and not to redesign them) and resist any temptation to alter pre-defined components of future arrangements or solve potential problems immediately. This is particularly important to mitigate investor uncertainty.

#### **Q2. What key issues should be examined as part of a work stream on future GB trading arrangements?**

We agree with the seven work areas identified in Annex 2 of the open letter and add some specific points below under the relevant headings. Although 'SO Incentives' is not a driver of reforms, given the interactions with other initiatives and the need to develop an enduring SO incentive scheme from 2015, it could be set up as another work area.

##### Facilitating Demand Side Response (DSR)

The open letter mentions that consideration of the role of DSR in the trading arrangements will be informed by discussions in other fora such as the Smart Grids Forum and Ofgem's Smarter Markets projects. We are involved in these fora and agree with many of the issues identified by Ofgem. However, for the future trading arrangement project, answers to some fundamental questions will be

needed to flush out the issues. For example, we will need to understand how DSR would work in practice. Additionally, new participants such as non-regulated aggregators, DNOs and consumers are likely to have a role to play in the future - we will need to understand the regulatory and commercial arrangements.

New players could significantly impact balancing, especially in the longer term, and market participants will need to have visibility of their actions – both forecasted and actual. Generators and suppliers (and not network operators) are exposed to unfavourable imbalance charges, by the half-hour, for differences in energy from that contracted in advance. Parties can be held harmless to quantified balancing actions initiated by the transmission system operator (demand reduction being more difficult), but if the role of DNOs or aggregators increases, there may be new uncertainties for suppliers (and generators to the extent they may be exposed to imbalance prices for their own imbalances).

#### Effective integration with the wider European market

European legislation for the EU Target Model and the Network Codes that follow from it, may increase the challenge of realising benefits for GB consumers from greater European integration. While we appreciate that implementation of the EU Target Model will necessitate changes to GB trading, balancing and settlement arrangements, it is not currently clear what framework Ofgem would use to ensure that GB consumers will benefit from greater European integration. The provisions of the Third Package have added, to Ofgem's principal objective of protecting (GB) consumer interests, the promotion of an internal energy market and the removal of restrictions to trade between Member States. This may mean that, from time to time, Ofgem might find itself have conflicting objectives.

The delivery of cross border interconnection is a prime example of where it is not entirely clear how Ofgem would ensure GB consumers would benefit from greater European integration. Ideally, market arbitrage opportunities should provide the driver. For non-merchant interconnection, and regardless of how it is funded, the market frameworks must ensure that the costs of using the interconnector and costs of having the option of interconnection must be recovered from those benefiting from the asset or option. We will be responding to Ofgem's consultation on the 'Cap and Floor Regime for Regulated Electricity Interconnector Investment' separately.

### **Q3. What form should the process take? How can the process help increasing certainty about the impact of the EU TM and its interactions with EMR while limiting any unintended detrimental effect on investors' certainty? What structures should we use to maximise the opportunities for stakeholder involvement?**

The open letter states that if the decision is made to go ahead with the project, the project scope, timeline and engagement process will be set out at the launch. We think the actual scoping exercise, including the problem identification stage,

would take longer. Identifying the problem and understanding the problem fully may be much more complex than initially assumed.

The first phase of the project should build on the potential issues outlined in the open letter. There is a need to establish clearly what the issues are that this project is trying to address. Securing stakeholder agreement, including across government, is crucial before moving on to the next phase

It would also be helpful if within the first phase of project some clarity is provided on what Ofgem can and might expect to be able to change. For example, there may be some clearly defined constraints arising from the EU Target Model. This would help industry participants and investors understand the scale of change we are facing. It is worth reiterating throughout the project that the objective of the project is to ensure EMR, the EU Target Model and the other initiatives work as intended, and not to redesign them.

Once the problem or issues to address have been identified, options must be considered and discussed and consulted upon with industry. In developing the options, the key principle should be to develop options which require 'minimum change'. It will only be possible after this stage to develop a high level design of future trading arrangements.

There will also be a need to develop and agree a roadmap. The roadmap should illustrate the longer term timetable to implement the agreed high level future trading arrangement design.

We agree that the work stream should be structured to enable stakeholder engagement at all levels. Buy in and agreement from stakeholders is crucial to ensure a successful outcome and will probably work best if some form of Project Board and Expert Groups are appointed to engage in the project going forward.

Whether Ofgem can do this in a year will depend on the resource it is able to provide towards this project – it should not detract from other important work streams. We are interested to find out what resource Ofgem is able to commit towards the project.