Joanna Campbell
The Office of Gas and Electricity Markets
9 Millbank
London
SW1P 3GE

4 November 2013

Dear Joanna

Consultation on the timing of a decision on electricity distribution networks' revenue for 2015-16

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.

EDF Energy supports Ofgem bringing forward the decision on the revenues to be used for the first year of RIIO-ED1 and supports option c), which will provide consumers with the greatest predictability of charges.

Currently the timetable for RIIO-ED1 has final proposals set for November 2014, one month prior to the publication of indicative network charges. This, clearly, does not give customers and suppliers sufficient notice of such a major change for what is a considerable portion of electricity bills (c18%). In addition, moving the notice period to earlier in the process would enable suppliers to offer products including the impact of the first year of RIIO-ED1 and therefore help to protect customers from bearing additional risk.

We note that this is a one-off proposed change and only focuses on revenues and not final charges. EDF Energy has for some time called for greater predictability and forward notification of network charges. This proposed forward notification should occur on a regular basis, throughout and between price controls, to help reducing the pricing risk inherent in what can be volatile charges. We do not agree with Ofgem's assumptions that this will result in consumers overpaying and believe that consumers will see benefits from greater predictability of charges. We regard this as a material part of making bills more affordable for our customers.

Volatility of networks charges has a significant impact on end consumers. These charges are one of the largest non-hedgeable risks for suppliers to factor into retail tariff pricing. This has become increasingly important, particularly as many domestic customers seek the security of fixed term products. With slim margins in energy retail, as illustrated by the segmental accounts, forecasting errors have considerable financial impacts.

EDF Energy therefore strongly urges Ofgem to support modifications to DCUSA (DCP 178) to bring forward notification of charges to help protect consumers from the impacts of charging volatility.

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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 Simon Vicary on 020 31262168, or myself.

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

Yours sincerely,

Paul Delamare
Head of Downstream Policy and Regulation

Attachment

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EDF Energy's response to your questions

Q1. Please provide any relevant information to improve our analysis of the benefit of each option including (if available):
(i) information on the risk premium included in contracts offered to consumers; and
(ii) the expected reduction in the risk premium an additional 4 months (option (b)) and an additional 11 months (option (c)) would provide.
Please specify if you wish any data provided to remain confidential.

EDF Energy commissioned analysis from CEPA which models the cost of suppliers, consumers and DNOs bearing the risk of charging volatility. The paper can be found at:

https://www.ofgem.gov.uk/ofgem-publications/50525/cepa-edf-volatility-reportfinal-260912.pdf

This analysis shows the premia that suppliers should have historically charged and with longer notice periods giving more certainty of costs then this could be significantly reduced or completely removed.

The difference between 4 and 11 months notice on allowed revenues would mean that there could be additional contract rounds in April and October 2014 that would have a greater degree of certainty on the direction of DUoS charges. This would enable suppliers to have more confidence in their forecast of the impact to customers. It would also mean that more products could be available earlier in the process as additional uncertainty may reduce the number of products offered to customers during this period. While this is a welcome first step, we believe that greater predictability is required by giving suppliers at least 15 months forward notification of charges, so that these can be efficiently built into retail pricing.

Q2. Do you have any views on the potential costs we have identified? Do you consider there to be other costs we have not identified?

In the consultation, Ofgem states its belief that the costs of implementing this proposal would be higher for DNOs, than the cost to suppliers or customers. However, the cost to the DNOs can be recovered through the price control and, on the basis that they will be held whole, it is therefore only an issue of cashflow. The cost to a customer or supplier who has incorrectly forecast DUoS charges due to lack of transparency will have a real impact. Even if a customer had a higher charge in the first year than eventually determined by the price control this would be rectified in the second year, assuming they were only signed to a one year fully inclusive or a pass through contract.

The work carried out by CEPA on our behalf (referred to above) found that the DNOs better placed to manage and finance the risk of deferring allowed revenues resulting in a lower overall cost to customers.

There appears to be a common assumption that customers will over-pay in the year 2015/16 if this proposal was introduced, but in some recent price controls we have seen revenues increase from initial to final proposal, so this assumption may well be incorrect.

Q3. What is your preferred treatment of deferred revenue? Please explain your reasoning.

Option 2 and 3, both seem reasonable. In some ways, both reduce the impact of the deferred revenue by spreading the collection over a number of years, but this could also lead to additional costs as the deferred revenue is financed by the DNOs. Deferred revenues would be known in November 2014 and therefore could be factored into revenues for 2016/17. Option 3 allows the revenue to be factored into 2016/17 unless the deferred revenue breaches a certain limit so this would safeguard against the impact to customers being too high.

Q4. If you prefer option 3 for deferring revenue, what do you consider an appropriate threshold? Please explain your reasoning.

An appropriate threshold for option 3 would be different for each DNO and would equate to a percentage change on charges. The appropriate percentage threshold could be determined by a expert industry group which could provide recommendations to Ofgem.

Q5. Do you have any views on our initial assessment of each option?

As above, and on the basis of the analysis provided by CEPA, we do not believe that Ofgem's assumptions that consumers will overpay is correct, provided that DNOs have sufficient flexibility to finance their activities.

Q6. Which option do you consider will drive the greatest benefit to consumers? Please support this view with analysis of the costs and benefits.

The greatest predictability for consumers would be with option (c), as this encourages suppliers to offer contracts beyond the start of RIIO-ED1.

Q7. Do you have any views on the relative complexity of option (b) and (c)?

We do not think that options (b) and (c) need to be complex. EDF Energy is ready to work with Ofgem and DNOs on workable solutions.

EDF Energy
November 2013