

1 INTRODUCTION

energywatch was set up under the Utilities Act 2000 and came into being in November 2000. It represents all gas and electricity consumers but has particular regard for the needs of low income, elderly, disabled, chronically sick and rural consumers.

Our mission is to be an independent consumer champion, dynamic in developing safe, confident and assertive consumers. We are committed to improving the services provided to all gas and electricity consumers.

energywatch has produced a composite response in response to key issues from the various scoping papers provided by the Performance and Innovation Unit as part of its review of Energy Policy.

We believe that there are several high level points that are applicable across all of the issues. Firstly, nothing can be off the agenda because it is too difficult or unpopular to think about. Second, we can no longer hide behind the view that markets provide the right investment signals and we need to accept that risks and costs need to be shared. We need clear impact assessments based on the key deliverables set out in the paragraph below so that

we can clearly explain decisions to consumers. Finally we need effective tools for assessing risk and developing contingency plans.

2 THE ENERGY POLICY REVIEW AND ITS IMPACT ON CONSUMERS

energywatch believes that there are 3 fundamental deliverables for consumers from the review of energy policy that is being undertaken by the Performance and Innovation Unit, namely the delivery of secure, safe and affordable energy.

A secure supply of energy is one that is secure both in terms of internal systems (i.e. that there is appropriate investment in pipes and wires for example) and in terms of the external geo-political environment. A safe supply is one that gives consumers confidence and meets the principle that people will not be put at risk by the provision of energy. Finally, affordable energy enables the UK to compete effectively both within Europe and globally.

The Energy Policy Review will inevitably develop a series of options as a consequence of its work. *energywatch* believes that it is essential that each option be tested against the above and that the criteria for each of these tests need to be clear and transparent. It would also need to be explicit in

addressing the likely impact of proposals on fuel poor consumers. The intention would not be to change proposals but so that mitigating action might be taken to ensure that Government remains on target to deliver the eradication of fuel poverty.

3 COAL

The abundant supply of coal, and its potential as stored energy, means that it must be taken seriously as a means of generating electricity. There may be a continuing role for coal, particularly as new technologies (to increase efficiency and reduce emissions) are developed, and in any event as a contingency to offset the risks associated with other fuels.

4 GAS

4.1 Investment in infrastructure

The energy policy debate needs to analyse whether there is likely to be an infrastructure in place to access and deliver remaining reserves. It is already evident that strains are beginning to show in the gas supply network. It is vital we address this as we become increasingly dependent on gas for generation.

The question is in part being discussed as part of the debate into planning future investment into Transco's price control.

Transco must balance investment into extending existing capacity of North Sea production and cope with increased importation of gas from Europe and elsewhere (increased use of LNG may change the economics of locating terminals) It may very well require looking again at the mechanisms and conventions of price controls.

Whilst it is likely that both types of investment will be needed, it highlights the problems of maintaining capacity in the network that avoids constraints. This is particularly important as perceived lack of capacity in the network can have an important, and detrimental, impact on wholesale gas prices.

4.2 Storage and LNG

It is clear that the increasing dependence upon gas for electricity generation means that we must review the function of storage (for example both France and Italy have sufficient storage capacity for 6 months) and whether the investment drivers in place are sufficient to meet any revised role. There is also likely to be a greater role for LNG (Liquid Natural Gas) storage.

LNG is an easy way to store gas and is not confined to the geology of a particular area as is salt cavity storage. It can be placed on the periphery of the

gas network to manage both supply and system constraints. It is also clearly a very mobile source of a commodity that is conventionally viewed as needing a fixed “gas chain” from production to burner tip.

Since energy prices are only likely to increase, given the predicted shortfall in production, it is likely that LNG will become more economic. *energywatch* expects the review to consider ways in which energy security can be managed at a truly global level. This would inevitably include the development of greater international trade in LNG.

4.3 Auctions

Auctions are an effective short-term mechanism for transmitting price signals to market participants or establishing “price discovery” of the value of a service or commodity that was previously unknown. However applied to energy, there are some significant drawbacks.

Unlike an auction for a painting, all participants in the gas market are forced to bid for the service from a monopoly service provider. If they do not get the service, such as network capacity, gas shippers face expensive financial penalties for going out of balance.

Auctions can also create volatility in related markets. Uncertainty over Transco’s maintenance programme and doubts about offshore reliability have caused significant price spikes sending out peculiar investment signals. In fact, one of the reasons why the largest players are vertically integrated is to mitigate risk in these open markets and make some money along the way from their smaller competitors. Companies that are not integrated nor have long term contracts have been exposed to the recent price rises. In this way uncertainty caused by auctions has a negative impact on long term investment strategies and impacts on a secure, safe and affordable energy supply.

Market-based mechanisms such as auctions are not the right instruments for something as vital as ensuring that there is sufficient investment in networks. We have relied too much on the notion of the market and need to accept that sharing risk is part and parcel of a secure, safe and affordable energy regime.

4.4 Safety

Safety in energy networks is of prime concern to *energywatch*. Traditionally safety has been linked to investment and safety standards. However the competitive market has created new types of issues that need to be addressed by the review. For

example, we have concerns that there is a shortage of gas service engineers that will affect any major work on the gas supply network. *energywatch* believes that investment in people should be recognised alongside other forms of investment.

5 ENERGY EFFICIENCY

It is difficult to underestimate the importance of increasing the take up of energy efficiency measures in the context of the Energy Policy Review.

It is a sure fire win-win for companies, consumers and the environment. Its major difficulty, however, has been the ability get consumers interested in its take-up at a time of low energy prices. It is also well identified as a key tool for increasing the affordable warmth for fuel poor consumers.

Consumers' interest in energy efficiency may change, given a sufficiently high profile campaign, when presented with the alternative options for sources of energy presented in the findings of the review.

6 NUCLEAR POWER

If we are serious about CO₂ reduction and supply security, nuclear power must be on the agenda along with all other options. We recognise the concern people have regarding

the safe disposal of nuclear waste and it is vital that efforts continue to be made to resolve this issue. We also need to accept that this is an issue that needs to be dealt with whatever the outcome of this review.

In particular clear and unequivocal attention must be given to developing a public relations strategy to ensure that people are aware of the options that are available to them and their consequences.

We also need to be able to convince consumers of the need for real diversity in energy so that we can prevent having energy that is the most expensive in Europe and with its inevitable consequences for jobs.

It will be important to present these issue starkly so that consumers are in no doubt regarding their importance; for example new nuclear power stations or dependence upon Russian gas or a comprehensive programme of renewable energy are just some of the choices of which consumers need to be aware.

7 SECURITY

There will inevitably be difficult decisions that will need to be taken as a consequence of the review. Having a clear set of tests based on key deliverables

as mentioned above provides a clear and consistent means of assessing their impact.

energywatch believes that it is neither practical nor desirable to have different security standards for domestic consumers and others who do not have the means available to them to source alternative supplies.

Given that it would be physically impractical to implement such a proposal it would only be possible through tariff structures. This would inevitably lead to first and second class consumers, with those on lowest incomes (and possibly with the greatest need for constant supply) suffering the most. Energy is an essential service key to UK competitiveness and such a proposal would jeopardise this.

It is inevitable that there will be an increased dependence on imports of energy. Against this we need to develop clear risk assessment strategies along with appropriate contingency plans.

8 ELECTRICITY AND GAS NETWORKS

We do not believe that network users should pay different prices for the provision of network services and there needs to be a fundamental review before any further cost-reflectivity is imposed. Such an approach has implications for programmes

to extend the gas supply network that have clear social and environmental benefits and we believe that there is a case for increased cost smearing to provide equal access to networks.

We discuss above our concern at any suggestion of different security standards for energy and our belief that this is not appropriate. We are strongly supportive of Ofgem's Information and Incentive Project as a start and believe that it is correctly focussed. However we believe that it needs to be developed further, over time, to cover system security and availability.

9 A NEW REGIME FOR REGULATORY CONTROL

energywatch feels that the market cannot be relied upon to provide supply security in the future. Markets can only take us so far in the provision of secure energy and that we need to reconsider their role.

The Energy Policy Review has also highlighted the real difficulties in trying to reconcile social, environmental and economic objectives. We believe one body needs to take ownership of these competing issues and make certain that the proposals from PIU can be coherently implemented. Such an arrangement would tend

towards the development of a strategic energy authority.

safe and affordable energy supply.

10 CONCLUSION

Nothing can be off the agenda because it is too difficult or unpopular to think about.

We can no longer hide behind the view that markets provide the right investment signals and we need to accept that risks and costs need to be shared.

There are 3 key deliverables from the review of energy policy, namely the provision of secure, safe and affordable energy.

We need clear impact assessments based on the key deliverables we have set out so that we can clearly explain decisions to consumers.

It also needs to be explicit in addressing the likely impact of proposals on fuel poor consumers so that mitigating action might be taken to ensure that Government remains on target to deliver the eradication of fuel poverty.

We need effective tools for assessing risk and developing contingency plans.

Government must play a leading role in developing both the investment drivers and regulatory framework to guarantee delivery of a secure,