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Direct Dial: 020-7901-7491

18 August 2005

The National Grid Company, CUSC Signatories and
Other Interested Parties

Our Ref: IND/COD/CUSC/CAP086

Dear Colleague,

Amendment to the Connection and Use of System Code (“CUSC”) - Decision and Notice in relation to Proposed Amendment CAP086: “Proposal for Earlier Consideration of Implementation Dates”.

The Gas and Electricity Markets Authority (the “Authority”¹) has considered the issues raised in the Amendment Report² in respect of Proposed Amendment CAP086: “Proposal for Earlier Consideration of Implementation Dates”.

The National Grid Company plc (“NGC”) recommended to the Authority that the Consultation Alternative Amendment proposed by E.ON should be approved and that the Implementation Date should be 10 Business days following the Authority’s decision.

Having considered the Amendment Report and NGC’s recommendation, and having regard to the Applicable CUSC Objectives³ and Ofgem’s wider statutory duties,⁴ the Authority has

¹ Ofgem is the office of the Authority. The terms “Ofgem” and “the Authority” are used interchangeably in this letter.

² CAP086 Amendment Report dated 30 June 2005.

³ The Applicable CUSC Objectives are contained in Standard Condition C10 of the licence to transmit electricity treated as granted to NGC under Section 6 of the Electricity Act 1989 (the “Transmission Licence”) and are:

- (a) the efficient discharge by the licensee of the obligations imposed upon it under the Act and by this licence; and
- (b) facilitating effective competition in the generation and supply of electricity, and (so far as consistent therewith) facilitating such competition in the sale, distribution and purchase of electricity.

⁴ Ofgem’s statutory duties are wider than the matters that the Panel must take into consideration and include amongst other things a duty to have regard to social and environmental guidance provided to Ofgem by the government.

decided to direct a modification to the CUSC in line with the Consultation Alternative Amendment for CAP086 proposed by British Gas Trading.

A separate letter contains the direction to NGC to modify the CUSC in accordance with the Consultation Alternative Amendment proposed by British Gas Trading as set out in the Amendment Report.

This letter explains the background to CAP086, and sets out the Authority's reasons for its decision. This letter constitutes notice by the Authority under section 49A of the Electricity Act 1989 in relation to the direction.

Background

Appropriate consultation relating to CUSC changes helps to promote the transparency and inclusivity of the Amendments process by ensuring that all parties affected by a particular change are as fully apprised of it as possible and have the opportunity to put forward their view of a particular Amendment Proposal. Section 8.19 of the CUSC contains provisions dealing with when, how, and for how long consultation should take place. Section 8.20 addresses, amongst other things, what matters should be included in an Amendment Report, and to this end specifies that details of implementation timescales should be included.

NGC must consult with Parties regarding potential solutions to the issues raised in CUSC Amendment Proposals at the consultation stage, but no similar obligation exists for NGC to consult on the Implementation Date. The consultation stage typically takes place at one of two points in the development of an Amendment. The first of these is shortly after an Amendment is raised in the case that the Panel decides to progress the matter directly to industry consultation. The second is after the Working Group has delivered its report in the event that the Panel determines the Amendment Proposal should first be assessed by a Working Group. Amendment reports, which must include a proposed Implementation Date, must be circulated in draft for no less than five business days before being sent to the Authority for decision. These provisions mean that although other aspects of an Amendment Proposal are consulted on over a longer period, the proposed Implementation Date is formally consulted upon for five days during the last stage of the change process.

The proposer of CAP086 was concerned that although these provisions may allow sufficient opportunity for CUSC Parties to comment upon the proposed Implementation Date, they do not allow NGC sufficient time to take account of concerns regarding that date. It was also suggested that the current period of consultation on the Implementation Date may not allow sufficient time for users to identify potential problems with the date, provide a rationale for their concerns, and present information which may enable the Authority to make a fully informed decision.

As a result, CAP086 was raised by E.ON UK and submitted to the CUSC Amendments Panel for their consideration on 22 April 2005. At that meeting the Panel determined that Amendment Proposal CAP086 should proceed to wider consultation by NGC. A consultation paper was issued on 27 April 2005 with responses invited by 27 May 2005. Two Consultation Alternative

Amendments were raised, one by E.ON UK (hereafter referred to as Consultation Alternative Amendment A) and one by British Gas Trading (hereafter referred to as Consultation Alternative Amendment B). On 9 June 2005 a further consultation was issued inviting views on the Consultation Alternative Amendments raised in relation to CAP086. Responses were invited by 21 June 2005. The final Amendment Report was submitted to the Authority on 30 June 2005.

The Proposed Amendment

CAP086 suggests amending section 8 of the CUSC to include an obligation on NGC to consult CUSC Users on Implementation Dates and provides that this would form part of the Amendment Consultation. The effect of CAP086 would be that consultation on a proposed Implementation Date would occur substantially earlier in the amendment process than is currently the case.

Implementation of the Amendment Proposal would also ensure that where the Amendments Panel directs that a Working Group may consider a potential Implementation Date, but that date differs from that recommended by NGC, the consultation document consults on both options.

It was the view of the proposer that implementation of CAP086 would better facilitate the achievement of Applicable CUSC Objective (a) by enabling NGC to better assess the complexity, importance and urgency associated with an Implementation Date, by enabling NGC to be more certain that it had not unduly delayed an amendment, and by ensuring that the licence obligations placed on NGC by the Electricity Act and the Transmission Licence were interpreted consistently across the regulated codes which NGC is required to maintain. The proposer also suggested that the Amendment Proposal would give industry comfort that Implementation Dates had been derived by means of an equitable process, and as a result this would enhance confidence in the arrangements and thereby promote competition and better facilitate the achievement of Applicable CUSC Objective (b).

Although NGC saw some merit in the Amendment Proposal it was concerned that the original amendment may not better facilitate the achievement of the Applicable CUSC Objectives because of its potential to create regulatory uncertainty as a result of CUSC parties putting forward a variety of Implementation Dates during the consultation.

Respondents' views and Consultation Alternative Amendments

NGC issued a consultation paper on 27 April 2005 inviting responses from CUSC Parties and interested parties by 27 May 2005 on the original Amendment Proposal for CAP086.

NGC received 4 responses to the consultation, of all of which expressed support for the Proposed Amendment. There was general consensus amongst the respondents that Implementation Dates were an important element of an Amendment Proposal and earlier consideration of them would better facilitate achievement of the Applicable CUSC Objectives. One party noted that although in some cases such earlier consultation did occur, this was not the default arrangement, and as a consequence believed there was a defect to be addressed. Another recognised that although it was unaware of instances where industry had disagreed with NGC over a proposed Implementation Date, this did not mean that the situation could not arise

in the future. The respondent also considered that requiring consultation regarding prospective Implementation Dates at the consultation stage would not represent a particularly onerous burden on NGC, and as such considered the changes proposed by CAP086 to be appropriate.

Two respondents put forward a Consultation Alternative Amendment designed to remove the risk of parties putting forward a variety of Implementation Dates forward during the consultation period. Consultation Alternative Amendment A was essentially the same as the original Amendment Proposal, but also provided that when a consultation on an Amendment Proposal and a proposed Implementation Date had closed it would be for NGC to consider the deliberations of the Working Group and CUSC Party responses and put forward a single Implementation Date. Consultation Alternative Amendment B also shared many features of the original Amendment Proposal, but provided that if a number of different Implementation Dates were proposed by Users and NGC, that the CUSC Panel should assume responsibility for proposing the Implementation Date.

The respondents' views are summarised and contained in the Amendment Report in respect of Proposed Amendment CAP086.

Respondents' views on the Consultation Alternative Amendments

NGC issued a consultation paper on 9 June 2005 inviting responses from CUSC Parties and interested parties by 21 June 2005 on the Consultation Alternative Amendments raised in relation to CAP086.

NGC received 3 responses to the consultation, one of which expressed support for both A and B, one which expressed support for Alternative A but did not mention Alternative B, and one which supported Alternative B, but which did not support Alternative A.

The respondents' views are summarised and contained in the Amendment Report in respect of Proposed Amendment CAP086.

Amendments Panel Members' views

Some Panel Members felt that a specific requirement on NGC to consult CUSC Users earlier regarding the Implementation date for a CUSC Amendment Proposal could be beneficial as visibility on the views of CUSC Users would be gained at an earlier stage, be more transparent and could therefore be more accurately reflected in the Amendment Report to the Authority. Some Panel Members felt such a requirement would also make the circumstances surrounding the choice of Implementation Date clearer for the Authority, should the industry favour a different Implementation Date to NGC. It was noted that since the CUSC Panel had been established, the Amendments Panel was not aware of any instances where the industry had disagreed with National Grid on a proposed Implementation Date for a CUSC Amendment Proposal, and that National Grid had taken all reasonable steps to secure and implement all CUSC Amendment Proposals to date consistent with its licence requirements, and taken into account, as far as possible, the views of the industry.

NGC's recommendation

The National Grid Company plc ("NGC") recommended to the Authority that Consultation Alternative Amendment A should be approved and that the Implementation Date should be 10 Business days following the Authority's decision.

Ofgem's view

Having considered the Amendment Report, Ofgem considers, having regard to the Applicable CUSC Objectives and its statutory duties, that Consultation Alternative B would better facilitate the achievement of the Applicable CUSC Objectives.

Implementation Dates are a fundamental element of an Amendment Report and the Amendment Proposal(s) detailed in those reports. As such, it is Ofgem's view that the introduction of provisions to the CUSC ensuring that consultation on this issue takes place at an appropriate time, and that the conduct of these consultations strike a suitable balance between providing appropriate information and easing the regulatory burden on parties involved in the consultation process, will better facilitate achievement of Applicable CUSC Objectives (a) and (b). Earlier formal consultation on a proposed Implementation Date will enable industry parties to make their views on that date known as early as possible in the Amendments process, giving both the body recommending the Implementation Date to the Authority, and the Authority itself, maximum visibility of the issues involved in the development and discharge of the implementation timetable. The promotion of greater transparency and inclusivity in the development of Implementation Dates, and by inference their subsequent approval or variance by the Authority, will help to provide greater market certainty and thereby facilitate effective competition in the generation and supply of electricity.

It is Ofgem's view that although the implementation of the original Amendment Proposal for CAP086 would, overall, better facilitate the Applicable CUSC Objectives than the current baseline, its potential to result in the proliferation of a number of alternative amendments differing only in respect of the Implementation Date, would act to the detriment of Applicable CUSC Objectives (a) and (b). As such, Ofgem considers that an alternative solution which mitigates this risk without creating additional other, more substantive problems, would be likely to better facilitate the achievement of the Applicable CUSC Objectives than both the current baseline and the original Amendment Proposal.

Ofgem considers that both Consultation Alternative Amendment A and Consultation Alternative Amendment B better facilitate the achievement of the Applicable CUSC Objectives as regards both the current baseline of the CUSC and the original Amendment Proposal by providing a proportionate solution to the perceived defect. In Ofgem's view, Consultation Alternative Amendment B is better able to deal with this risk than Consultation Alternative Amendment A as it ensures that any Implementation Date recommended in relation to a Proposed Amendment is endorsed by the representatives of a cross section of the industry (the Amendments Panel). Accordingly, it is Ofgem's view that Consultation Alternative Amendment B marginally better facilitates the Applicable CUSC Objectives than Consultation Alternative Amendment A by

promoting greater transparency in the decision making process, which will increase confidence in the operation of the market and Applicable CUSC Objective (b).

Ofgem notes that NGC is not entirely clear how comfortably Alternative Amendment (B) sits with its existing obligations to make recommendations on CUSC Implementation Dates. Ofgem considers there are two areas in which such obligations would arise; these are the Transmission Licence and the CUSC itself.

Ofgem does not consider that the provisions in the Transmission Licence obligate NGC to make a recommendation on Implementation Dates. Rather, they create an obligation on NGC to accurately record the implementation timetable recommended by the body specified under the CUSC, and for NGC to put in place and operate procedures for the modification of the CUSC which better facilitate the Applicable CUSC Objectives by, amongst other things, enabling the timetable for implementation to be assessed in a manner best able to take into account of all the relevant issues and thereby produce a timetable which will enable the modification to take effect as soon as practicable after the Authority directs the modification to be made.

A number of provisions in section 8 of the CUSC deal with Implementation Dates and ensuring that the best implementation timetable is developed. Specifically, section 8.20.2 (g) requires NGC to prepare and submit to the Authority a report detailing, amongst other things, the proposed date for the implementation of the Proposed Amendment or any Alternative Amendment. Ofgem considers that neither 8.20.2 (g), nor the wider provisions of section 8 preclude NGC from including within the report an Implementation Date it does not agree with, if other provisions of section 8 place the obligation for determining that date on another body.

NGC has also noted that the company is not entirely clear about how the Amendments Panel would be able to come to a recommendation as to a suitable Implementation Date. Ofgem considers that it would be appropriate for the Amendments Panel to consider Implementation Dates suggested to it by NGC and other industry members, and for it to evaluate the rationales for those suggested dates when coming to its decision. Ofgem anticipates that NGC would work closely with the Panel regarding the selection of an appropriate date, and would bring forward information that would best serve the Amendments Panel when coming to that decision.

Ofgem notes that section 8.2.3.2 of the CUSC requires the CUSC Panel to endeavour to operate in an efficient, economical manner, taking into account the complexity, importance and urgency of particular Amendment Proposals. Ofgem considers that, when recommending an Implementation Date, it would aid the Panel's discharge of this obligation to bear in mind the potential impacts of its decision on NGC, and for it to recommend an Implementation Date which takes appropriate account of the work needed to implement an Amendment Proposal.

It is Ofgem's view that it is possible for Consultation Alternative Amendment B to be implemented into the CUSC without requiring additional amendments to either the CUSC itself or the Transmission Licence.

The Authority's Decision

The Authority has therefore decided to direct that Consultation Alternative Amendment B, as set out in the Amendment Report, should be made and implemented. An attached letter contains this direction.

If you have any queries in relation to the issues raised in this letter, please feel free to contact me on the above number.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'N. Simpson', written over a horizontal line.

Nick Simpson
Director, Modifications

Signed on behalf of the Authority and authorised for that purpose by the Authority