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The National Grid Company, CUSC Signatories and
Other Interested Parties

Our Ref: IND/COD/CUSC/CAP068

Dear Colleague,

Amendment to the Connection and Use of System Code (CUSC) - Decision and Notice in relation to Proposed Amendment CAP068: *Competing Requests for TEC*.

The Gas and Electricity Markets Authority (the Authority¹) has carefully considered the issues raised in the Amendment Report² in respect of Proposed Amendment CAP068 *Competing Requests for TEC*.

The National Grid Company plc (NGC) recommended to the Authority that Proposed Amendment CAP068 should be approved.

Having carefully considered the Amendment Report and NGC's recommendation and having regard to the applicable CUSC Objectives and Ofgem's wider statutory duties³, the Authority has decided to direct an amendment to the CUSC consistent with the CAP068 Alternative Amendment.

A separate letter contains the direction to NGC to modify the CUSC consistent with this decision letter.

This letter explains the background to Proposed Amendment CAP068 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.

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

² CAP068 Amendment Report dated 27 May 2004.

³ 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.

Background

Proposed Amendment CAP068 was raised by NGC on 21 November 2003. The CUSC Amendments Panel determined that a Working Group should consider the Proposed Amendment and it provided a final report to the Panel on 27 February 2004. The Panel determined that the Proposed Amendment should proceed to wider consultation. A consultation paper was issued on 15 March 2004 with responses invited by 16 April 2004. The final Amendment Report was submitted to the Authority on 27 May 2004.

Transmission Entry Capacity (TEC) defines a generator's maximum allowed export capacity onto the transmission system in a financial year. Under the CUSC, parties with TEC allocations have the option of purchasing the same quantity of TEC in the following year. A generator may seek additional TEC or a new generator may seek an initial allocation of TEC. NGC has a licence obligation to offer terms to all parties seeking access to its transmission system. If NGC considers that the additional generator capacity would require network reinforcement for its system to continue to comply with its security standards then NGC would typically provide a connection offer on an invest-then-connect basis. Alternatively, if there is a willing seller of TEC parties may be able to negotiate bilaterally for the purchase of TEC (although the seller would generally need to be connected at the same grid supply point (GSP)).

The Amendment Proposal

Proposed Amendment CAP068 would facilitate the trading of TEC, including trades between GSPs, subject to NGC calculating an exchange rate. For inter GSP trades NGC would assess whether it is possible to trade TEC on a one to one basis or whether it would need to calculate an appropriate exchange rate. NGC would charge the party requesting the exchange rate for the provision of this information.

The Proposed Amendment would also provide a web based bulletin board to facilitate TEC trading within and between GSPs. Assuming NGC could not automatically accommodate a request for TEC and that the party concerned could identify another generator willing to sell an appropriate quantity of TEC, the bulletin board could be used to publish the details of the possible trade. This would assist other parties interested in selling TEC in considering whether they wished to make a better offer to the generator seeking new or additional TEC. Any counter offers would not be included on the bulletin board.

The Proposed Amendment also specifies that competing requests for TEC would be allocated by NGC on a first come first served basis by ensuring that the first generator to complete an agreement to buy TEC (where appropriate with an approved TEC exchange rate) would receive the TEC.

During Working Group discussions it was noted that the Seven Year Statements (see NGC's website⁴) contain sufficient information on generating plant and TEC allocations to allow parties interested in buying TEC to identify possible sellers of TEC. It was agreed that this website could be used to implement the CAP068 bulletin board if it were modified to include details of generating plant seeking additional TEC and the initial offer.

⁴ NGC's Seven Year Statement is available at http://www.nationalgrid.com/uk/library/documents/sys_04/default.asp?Node=SYS&action=mnch6_1.htm&sNode=6&Exp=Y

Once a party has sold TEC it would no longer have the option to purchase this TEC the following year. This option would pass to the party that had purchased the TEC.

NGC stated that it would monitor the ownership of TEC to ensure that there was no double recovery of TEC charges.

The Alternative Amendment

One of the respondents proposed an Alternative Amendment because it considered that aspects of the legal text did not reflect the Working Group discussions. The respondent proposed that:

- trades should be posted on the bulletin board after the completion of the trade, rather than at the offer stage
- NGC should have a three month limit within which to calculate an exchange rate, and
- NGC should set out its fee for calculating the exchange rate in its charging statements to ensure that the charges NGC levies for the calculation of the exchange rate are transparent and not applied on an ad hoc basis.

It was suggested that the Alternative Amendment would reduce concerns over commercial confidentiality which might arise from new entrants disclosing their TEC requirements before a trade had been agreed and that it would be helpful to competition to set a limit on the time that NGC could take to calculate an exchange rate.

Respondents' views

The respondents' views are set out in the CAP068 Final Amendment Report. This section provides a summary of those responses. Full responses are available on NGC's website.

The Amendment Proposal

NGC received four responses to the consultation on the Proposed Amendment. One respondent supported the Proposed Amendment and considered that it would allow NGC to make more informed decisions with regards to TEC applications, facilitate trading, promote the efficient use of the transmission system and facilitate effective competition.

Two respondents offered conditional support. One respondent considered that without further clarification it could not assess whether the Proposed Amendment would be beneficial or detrimental to competition. The respondent considered that the Proposal was a small step towards flexible charging regime, it was concerned that the cumulative costs associated with trading for TEC could inhibit use the service.

The respondent also had a number of concerns with the legal text. It considered that TEC trades should be published after the trade had been completed. It also thought that there should be clarification over which party should pay the exchange rate charge. Both respondents offering conditional support considered that there should be a time limit within which NGC should provide an exchange rate and that NGC's charges for the exchange rate should be published in advance.

One of the respondents thought that the bulletin board would not be used frequently. It also noted that the title of the Amendment Proposal was called *Competing Requests for TEC* but

considered that the Amendment did not address how competing requests for TEC would be treated if two applications were made at similar times and there was insufficient capacity to meet both requests. The respondent indicated that the bulletin board, which would inform participants of the first offer for TEC but not of any subsequent offers, could put subsequent applicants at an informational advantage.

One respondent did not support the Proposed Amendment. The respondent suggested that TEC trading was possible using present arrangements. The respondent took the view that any marginal improvements would be offset by additional complexity. The respondent also considered that posting confidential offer data on the bulletin board could compromise commercial confidentiality.

The Alternative Amendment

NGC received three responses to the consultation on the Alternative Amendment. One response (the Proposer) expressed support on the basis that it better facilitated the relevant objectives than the original amendment.

One respondent offered conditional support noting that some of its concerns about the Original Amendment (regarding the information problems and the lack of clarity of the application fee) were alleviated by the Alternative Amendment. The respondent indicated that the Alternative Amendment was an improvement on the Original Amendment but considered that neither of them addressed the issue of competing requests for TEC.

One respondent did not support the Alternative Amendment stating that the benefits of any marginal improvement in transparency would be offset by compromising of commercial confidentiality for new entrants. It also considered that TEC trading was possible under the existing arrangements.

Responses to Ofgem GB-wide consultation

Ofgem undertook a GB-wide consultation⁵ on the Proposals on 4 June 2004. The responses are summarised below and are available in full on the Ofgem website. There were three responses to the GB consultation.

One respondent supported the Amendment Proposal stating that it would provide a more clearly defined and flexible process for dealing with access rights. It noted that these improvements would be beneficial under BETTA in light of developments in renewable generation and the likely transmission constraint issues in Scotland.

Two respondents did not support either the Amendment Proposal or the Alternate Proposal. One of the respondents noted that the Original Amendment would enable the publication of TEC trade offers before applicants had agreed the terms. It considered that this was confidential information which should not be placed in the public domain. It preferred the Alternative Amendment on the basis that it better preserved confidentiality. However the respondent noted that the exchange rate calculation remained unclear in the Alternative Amendment. The

⁵ The GB-wide consultation was undertaken in light of the proposed introduction of the British Electricity Transmission and Trading Arrangements (BETTA) pursuant to the Energy Act 2004.

respondent also considered that the governance arrangements between CUSC amendments, charging methodologies and other processes made it impossible to assess the impact of the Proposed Amendment on industry parties. The respondent sought assurances that NGC would not be able to recover TNUoS charges from two parties for the same TEC.

The other respondent considered that the Proposal would not enable Transmission Licensees to make better informed decisions for multiple applications for TEC under BETTA, nor would it allow competing requests for TEC to be managed in a more equitable manner. The respondent also considered that by placing the requirements of new users for TEC in the public domain it could be discriminatory and would undermine competition and commercial confidentiality.

NGC's recommendation

NGC recommended to the Authority that the Original Amendment be approved with an implementation date of 1 April 2005⁶. It considered that it would better facilitate the achievement of the Applicable CUSC Objectives by enabling NGC to make better informed decisions when faced with multiple requests for TEC. NGC considered that enabling TEC trading would make more efficient use of the transmission system and would better facilitate competition in the generation and supply of electricity.

NGC did not consider that the Alternative Amendment better facilitated the achievement of the Applicable CUSC Objectives, because it was less transparent (although it acknowledged that elements of the Alternative Amendment might warrant further consideration in the future).

Ofgem's view

There is merit in encouraging the trading of TEC as it would enhance efficiency and competition in generation. Both the Amendment Proposal and the Alternative Proposal address issues relating to the trading of TEC (including between GSPs).

The Amendment Proposal would require the publication of potential TEC trades once an offer for TEC has been made but before the trade has been finalised. Such an arrangement would encourage counter offers to be made by other parties. While there are benefits in greater transparency these need to be balanced against the cost of disclosing commercially sensitive information. Disclosing information on initial offers for TEC but not counter offers appears to have the disadvantage of revealing potentially sensitive information without the advantages of a fully transparent trading mechanism.

Implementing the Alternative Amendment Proposal would ensure that the details of a TEC trade and of a generator's traded position would be published after the trade has been completed. Although this creates some limits to market transparency prior to the completion of a trade the Alternative Amendment Proposal better protects the commercial position of participants and also provides information on actual TEC trades. Therefore, the Alternative Amendment Proposal appears to better facilitate the achievement of effect competition in the generation and supply of electricity.

⁶ NGC indicated that this implementation date was contingent on receiving the Authority's decision by December 2004. Alternatively, NGC recommended an implementation date of 1 April 2006.

There are also a number of benefits in NGC setting out its charges for exchange rates in advance. This would assist participants in assessing whether it is appropriate to trade for TEC or wait for an invest then connect offer based on the costs associated with the two approaches. Furthermore, the requirement for NGC to define a timeframe within which it will have to complete the exchange rate calculation would add greater certainty to the process.

In the light of these factors the Alternative Amendment should promote the economic and efficient operation of the transmission system by facilitating the efficient allocation of TEC and better facilitate effective competition in the generation of electricity by providing generators (that are subject to invest then connect offers) with the possibility of earlier entry into the market. This could be particularly useful for new generation plant.

The legal text of the Alternative Amendment refers to exchange rate fees, as set out in the charging statement, which operates under separate governance arrangements. Nevertheless, Ofgem's view that the Alternative Amendment better facilitates the achievement of the applicable CUSC objectives is not contingent on changes to charging statements. Ofgem's decision to accept Alternative Amendment Proposal CAP068 will not fetter its discretion in the treatment of future decisions on charging, which are outside of the CUSC. In raising modifications it would be helpful if CUSC parties could seek to ensure, where practicable, that the modifications dealt with matters relating to CUSC and left matters relating to charging methodologies to the separate change processes.

While CAP068 Alternative Amendment has a number of advantages in encouraging the trading of TEC it may also be advantageous for NGC and market participants to give consideration to whether these arrangements could be further developed or enhanced in the future. For instance, it would be helpful if respondents concerns about the process for dealing with competing requests for TEC could be dealt with.

The Authority's Decision

The Authority has decided to direct that CAP068 Alternative Amendment, as set out in the Amendment Report, should be implemented on 1 April 2005. A separate letter contains this direction.

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

Yours sincerely,



Andrew Walker

Director – Transmission Networks Regulation

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