

Your Ref: 176/05

Our Ref: NS/JH/IDNODec

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Dear Mark

Regulation of Independent Electricity Distribution Network Operators - Decision Document

CE Electric UK Funding Company (CE) is the UK parent company of Northern Electric Distribution Limited (NEDL) and Yorkshire Electricity Distribution plc (YEDL). This letter represents the views of CE, NEDL and YEDL on the regulation of independent electricity distribution network operators (IDNOs) decision document.

We have structured this response in line with the decision document, namely:

- Price control arrangements;
- Financial ring-fencing; and
- Commercial arrangements.

Our main outstanding areas of concern exist with the lack of clarity over the application of credit cover arrangements for IDNOs.

Price control arrangements

We are pleased that Ofgem have chosen Option 1 for the approach to the price control of IDNOs, with a start date of April 2006. We would also like to state that we support Ofgem's intention to keep the protection for non-domestic customers under review.

Financial ring-fencing

We believe that the proposals for financial ring-fencing are appropriate and that the alignment of these proposals with those implemented for ex-PES DNOs in DPCR4 is sensible.

Commercial arrangements

Boundary metering

We are generally supportive of your views on boundary equipment and metering. We also recognise our obligations to provide connections based on the minimum-cost, technically-acceptable solutions. However, we have seen very few applications to date for connections to IDNO sites. This lack of experience leaves some uncertainty over the precise nature of the arrangements that will develop to address the necessary operational, technical and

safety requirements in addition to minimising costs where possible. We are committed to working closely with IDNOs to ensure appropriate solutions are developed.

Credit cover requirements

We would endorse the approach to seek congruence with the existing best practice credit cover guidelines issued in February 2005. The eventual solution should ensure that:

- the processes are straightforward and avoid unnecessary complexity;
- the system is efficient from a GB plc perspective; and
- the mechanism appropriately reflects the risk of default on each counterparty relationship.

There is a trade-off to be achieved in successfully delivering the first point above relating to simplicity and efficiency. By introducing an over-complex process it would be possible to ensure that the cover provided was truly efficient at a GB level. However, the complexity could itself introduce further inefficiency due to the costs of operation. Also, declaring a GB system as inefficient could be misrepresenting the actual costs, since much of the cover is provided by parent company guarantees to leverage investment grade credit ratings. Therefore, there is no additional cost, as there would be if all cover were provided as physical security.

Our view would therefore be that simple, efficient systems for controlling credit cover should take precedence over arguments relating to GB plc inefficiencies that prove to be theoretical rather than practical.

As per the supplier/DNO relationship we are assuming, and require confirmation, that 100% pass-through arrangements will exist in the instance of downstream IDNO failure where the upstream DNO was following the best practice guidelines. This reflects the nature of the relationship where the DNO has a licence obligation rather than a commercial choice to enter into contractual agreements with the IDNO. There is also a general point where we would support the appropriate drivers existing to reflect the risk of default appropriately on each counterparty relationship. Therefore, where possible, the cover mechanisms seek to redress any default in the first instance prior to the introduction of pass-through arrangements.

I hope that you find these comments helpful. If you would like to discuss any of them further, then please do not hesitate to contact me.

Yours sincerely



Joseph Hart
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