E.ON UK plc
Westwood Way
Westwood Business Park
Coventry
CV4 8LG
peter.bolitho@eon-uk.com
Tel: 02476 183384

Mark Cox
Associate Partner, Industry Codes and Licensing
The Office of Gas and Electricity Markets
9 Millbank
London
SW1P 3GE

8 December 2009

Dear Mark

Code Governance Review Initial Proposals: illustrative licence modification drafting

We have now had the opportunity to review the illustrative drafting for the three work strands of the Governance review. Broadly speaking the drafting appears to accurately reflect the intent of the Initial Proposal documents published in August and September.

That said we continue to have fundamental concerns about how Ofgem plans to implement its Major Policy Review Proposal and the exact form of user rights to propose changes to charging arrangements. The apparent focus of the Code administrator reforms particularly the emphasis on providing support for small participants rather than all classes of user is at best unhelpful and at worst is unduly discriminatory.

Our views are set out in detail in our responses to the Initial Proposals on Major Policy Review and Self Governance, Code administrators and small participant/consumer initiatives and Charging Methodologies and these can be found at the links below:
http://www.ofgem.gov.uk/Licensing/IndCodes/CGR/Documents1/E.ON%20response%20-%2084-09.pdf
http://www.ofgem.gov.uk/Licensing/IndCodes/CGR/Documents1/E.ON%20Response%2085-09.pdf
http://www.ofgem.gov.uk/Licensing/IndCodes/CGR/Documents1/E.ON%20response%20108-09.pdf

Rather than revisit every detailed point, I would like to stress where E.ON UK believes further work on the drafting is required. In terms of the MPR proposals the drafting fails to provide the essential procedural checks and balances to minimise the chance of inappropriate regulatory intervention or the necessary safeguards to protect the rights of affected parties, e.g.

their ability to appeal decisions under the statutory Industry Code Modification Appeals process Appendix A of our 18 September 2009 response provides a summary of the suggested checks and balances that could be incorporated into licence conditions

The lack of a clear statutory mandate for this MPR process is problematic and the drafting (e.g. Clause 4B relevant to the BSC) would permit Ofgem to direct particular (as yet unspecified) proposals that must be brought forward, is highly irregular. Such a 'constitutional' licence change surely undermines the right of the licensee to object to future specific proposals under the existing statutory objection process and possible referral to the Competition Commission. Ofgem may argue that the licensee would have to agree to this by agreeing to the 'constititution' licence change in the first place. It must be remembered however, that those that are typically most affected by code modifications are the users (generators, shippers and supplies) have no formal right to object to this 'constitutional' licence change (at least with respect to the BSC, UNC and CUSC). In our view it would be inappropriate for National Grid to 'waive' rights to object to as yet unspecified proposals in this way.

It may be marginally more acceptable for Ofgem to propose a specific licence change every time they wish the licensee to bring forward a proposal to implement the conclusions of a MPR. This at least preserves the existing objection rights of the relevant licensee.

Changes to the constitution of the Panel including having an Ofgem approved 'independent' Panel chair with a casting vote will inevitably affect potential rights of appeal of Modification decisions to the Competition Commission. If Ofgem wish to pursue this route then we do not believe that it is appropriate for the chair to have a casting vote. Overall we think the rights of affected parties would be best preserved (and accountability and transparency of process best achieved) if there was an automatic right of appeal of all modification decisions arising from MPRs.

The whole MPR process could be brought into question if an affected party that is aggrieved with an eventual modification decision were to test the legitimacy of the process at a Judicial Review. A successful challenge might even question the validity of of other modification decsions arising from earlier MPRs.

We are supportive of many of the proposals suggested in relation to the Code administrators and small participant/consumer initiatives. Certain clauses however are very unhelpful including the attempt to define small participants and the "critical friend" support that should be offered to them by the code administrators. We believe such support should be offered to all users, but that different users will naturally avail themselves of these services as they see fit. This may therefore be of more benefit to small participants but other classes of users who may be unfamiliar with a particular aspect of code procedures may benefit as well. In our view, a much better approach would be to place an obligation on code administrators to *"reflect the views of all classes of users and customers that are likely to be affected by a proposal"*. This would avoid the need to define small participants especially given large well resourced organisations such as Gazprom, BP and Fred Olsen would be included in the current definition of "small participant".

On the Charging Methodology proposals we would again urge Ofgem to think carefully about opening up the process without consideration of the safeguards necessary to protect against

disproportionate influence of special interest and vocal lobby groups e.g. from particular regions of GB.

In our response to the Ofgem's Initial Proposals on Charging Methodologies we had assumed that Option 2, 3 and 4 all included Ofgem positively approving or rejecting each proposal as all competing proposals would be submitted to Ofgem. Thus our analysis concluded that Options 2, 3 and 4 all scored badly in terms of regulatory certainty given that this 'open-ended' 'code decision making process compares badly with the time bound veto/not veto process.

We are therefore confused to see that the legal drafting seems to envisage the veto/not veto process persisting even under Option 2. Our confusion arises because the practice is for the network operator to only put forward the proposal he wishes to implement and then it is for Ofgem to choose to veto or not veto that proposal. There is no positive approval process although Ofgem invariably chooses to say why they have chosen to not veto a proposal. If a veto decision were not to be received in time it gets implemented anyway. Overall we think such a decision making process is efficient.

However, we cannot see how a number of competing proposals including those of users can each be submitted under such a process. What if Ofgem did not veto in time - this would mean all alternatives would have to be implemented and that is clearly nonsense?

Hence we think that E.ON's variant of Option 2 which would allow users to bring forward proposer and have these considered and consulted on but the relevant network operator(s) would decide which user proposal would go forward to Ofgem for a decision remains the best way forward.

We hope you find these observations helpful. If you wish to discuss this further please feel free to give me a call on the number shown at the top of this letter.

Yours sincerely

Peter Bolitho
Trading Arrangements Manager