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Dear Stuart,

Project Transmit: next steps on connection issues

Thank you for the opportunity to respond to the open letter issued on 22 March on the above issue. In your letter you request views on a number of issues relating to obtaining new connections to the transmission system. Our response on each of the points follows.

Electricity User Commitment

Although we have previously been concerned about the user commitment arrangements in electricity and the effects they can have on new projects, we believe that currently they are largely fit for purpose. The two main concerns that we held were subsequently addressed in the following ways:

- In 2006, we raised the issue of the significant levels of Final Sums Liabilities (FSLs) that were being incurred by some developers before consents had been obtained on their projects and the unpredictable and uncontrollable nature of those FSLs going forward. This issue was largely addressed by the introduction of the optional Interim Generic User Commitment Methodology (IGUCM) by National Grid.
- Subsequently, a number of developers expressed concerns about the levels of FSLs that were required from certain projects, particularly in Scotland where a number of relatively small projects were each required to underwrite the entire costs of reinforcements such as the proposed offshore "bootstraps", when in reality they were only individually triggering a proportion of that build. We believe that this issue was addressed by National Grid with the introduction of its revised FSLs arrangements in 2010.

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Whilst we are now largely content with the current status quo, both as a developer of new technology and an existing player who would be exposed to a significant proportion of the costs of any stranded assets, we accept others may still not be happy with the current user commitment arrangements. Therefore, it seems proper that they are reviewed as part of Project Transmit. However, what is most important is that any arrangements that are put in place are done so on an enduring basis without the expectation that they will be reviewed and revised again in the near future. Uncertainty around future liabilities is a significant concern for developers.

In terms of the high level principles outlined for the user commitment arrangements in the open letter, these would largely appear to be appropriate. In particular we agree on the importance of protecting customers, avoiding barriers to entry to all generation types, whilst ensuring that security of supply is not adversely affected. On the issue of discrimination, we believe that the focus should be on the avoidance of undue discrimination. Discrimination in itself should not be an issue as long as any difference in approach is justified. Similarly, unjustified similar treatment of two groups would constitute undue discrimination.

In the open letter, reference is made to ensuring that the arrangements deliver the correct level of stranding risk between new and existing network users, the network companies and consumers. However, it should be noted that consumers are not directly exposed to any stranding risk. Instead, under present arrangements other users of the network, both generators and suppliers, are exposed to the risk through the potential for higher transmission charges. Of course, ultimately it would be assumed that these costs would feed through to customers in some form or another, through higher wholesale and/or retail prices, and consequently the effects of any proposals on customers must be assessed and taken into account. However, it should be recognised that the arrangements in the first instance pose a risk to retail businesses as well as generation businesses and therefore the incentives should be set accordingly.

We are not certain that the arrangements would allocate stranding risk to the network companies, except to the extent that any investment might be disallowed under the relevant transmission price control. Although the transmission companies should be expected to invest in an efficient and prudent manner, directly incentivising transmission companies in this respect tends to result in more risk for market participants as the transmission companies tend to seek to offset their risk, often onto network users. We would be concerned if transmission companies were exposed to more risk and associated reward, but were then simply allowed to back off the risk element in this way.

The letter asks for our views on the current modification proposal CMP192. At the moment the proposal is still in the process of being fully defined and so we are not in a position to give a definitive view. However, we are concerned about the general principle of the modification that, in seeking to reduce the burden on pre commissioning generators, it aims to increase the burden on post commissioning generators through the introduction of increased user commitment.

We understand National Grid's position that it would be helpful to understand when existing plant will close or reduce TEC so that it can better plant investment on the network. However, we also believe that as during discussions under the transmission access review, and through consideration of CUSC amendment CAP165 in particular, it became clear that generators were not in a position to give more than one or two years'

notice of their intention to close a station or reduce its TEC. Any increase in user commitment is therefore unlikely to result in better information provision in reality. Nevertheless, the transmission companies would tend to rely on the increased user commitment as a signal and justification for the investment they make in their networks. If generators are unable to give that signal that far ahead this would seem to simply act as a vehicle to transfer transmission investment risk from the transmission companies to generators.

Significant Code Review

The open letter asks for views on which issues may appropriately trigger the Significant Code Review (SCR) process in relation to user commitment in electricity transmission. We believe that there is no specific list of trigger events. However, if Ofgem does embark on an SCR in this area, it must believe that in doing so it will deliver a better and/or timelier solution than continuing with the CMP192 amendment process.

Timely Connections

In our response to the December consultation on timely connections we expressed our views on a number of issues relating to obtaining a new connection, including whether or not it would be desirable for transmission companies to provide compensation to generators for late connections. We continue to believe that it would be unlikely that any arrangements would provide sufficient payments to generators to act as compensation for a delayed connection, such as to cover consequential loss for instance. However, it might be possible to financially incentivise desirable behaviour from the transmission companies, although we would continue to be concerned about how this may impact on other users. For instance, if the payments made by the transmission companies were simply spread over other users or were potentially of such a magnitude so as to impact on the rate of return required by the companies, then we believe that this would be of significant concern to all network users. On balance, we continue to believe that timely connections are an existing licence requirement and that further financial incentives are probably not appropriate at present.

We do however support the introduction of a reporting requirement on TOs to gather information on the issues that prevent timely connections to the transmission network. This would help the assessment of how well TOs are performing and inform any work to provide improvements to the arrangements.

I hope that the above comments prove helpful. Should you wish to discuss this further please contact me on the above number in the first instance.

Yours sincerely,

Paul Jones
Trading Arrangements