



Direct Dial: 020-7901-7355

20 December 2002

The National Grid Company, CUSC Signatories and
Other Interested Parties

Your Ref: CAP008
Our Ref: IND/COD/CUSC/CAP008

Dear Colleague,

Amendment to the Connection and Use of System Code ("CUSC") - Decision and Notice in relation to Proposed Amendment CAP008: "Codification Errors".

The Gas and Electricity Markets Authority (the "Authority"¹) has carefully considered the issues raised in the Amendment Report² in respect of Proposed Amendment CAP008 "Codification Errors".

The National Grid Company plc ("NGC") recommended to the Authority that Proposed Amendment CAP008 be rejected.

The Authority has decided not to direct a modification to the CUSC.

This letter explains the background to Proposed Amendment CAP008, as set out in the Amendment Report, and sets out the Authority's reasons for its decision.

Proposed Amendment

"Codification errors" are defined by the Proposer as unintended changes in effect arising from the migration process from the Master Connection and Use of System Agreement (MCUSA) to the CUSC, which may only emerge in the future while the CUSC is in operation. The Proposer

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

² CAP008 Amendment Report dated 9 May 2002.

considered that Proposed Amendment CAP008 would establish the concept of “codification errors” in order to permit specific categories of amendment to be addressed and rectified.

The Proposer stated that Proposed Amendment CAP008 would better facilitate achievement of the Applicable CUSC Objectives since it would better facilitate the efficient discharge by NGC of its obligations under the Electricity Act 1989 and its Transmission Licence³. However the Proposer asserted that in the case of Proposed Amendment CAP008 the requirement to “better facilitate achievement of the Applicable CUSC Objectives” is not the correct criterion against which the Proposed Amendment should be measured. The Proposer considered that the issue is one of ensuring that there is an appropriate acknowledgement and recognition within the Transitional Issues section of the CUSC that there may have been unintended changes arising from the migration process from the MCUSA to the CUSC, which will result in a different conclusion as a consequence of the interpretation applied. In addition the Proposer stated that Proposed Amendment CAP008 would also bring the CUSC Amendment Process into line with best regulatory practice of correcting errors and would facilitate the reduction of regulatory uncertainty and increase confidence in both CUSC design and its processes.

Proposed Amendment CAP008 was raised by British Energy Generation Ltd on 31 October 2001 and was submitted for consideration at the CUSC Amendments Panel Meeting on 9 November 2001. At the meeting the Panel determined that a Working Group should be established to consider the Proposed Amendment. The Governance Amendments Working Group was established to evaluate Proposed Amendment CAP008. The Group was unable to reach a unanimous agreement as to whether the Proposed Amendment would better facilitate achievement of the Applicable CUSC Objectives, although there was support within the Group for the issue raised by the Proposed Amendment. The Working Group report was submitted for consideration at the Panel Meeting on 22 February 2002. The Panel endorsed the Working Group report and determined that the Proposed Amendment should proceed to wider consultation by NGC. A consultation paper was issued on 6 March 2002 with responses invited by 8 April 2002. On 27 March 2002 an extension to the timetable in respect of Proposed Amendment CAP008 was requested. The request was made to enable Amendments Panel Members to view the responses made during consultation before providing their views to be included in the Amendment Report. The Authority did not object to the request to extend the timetable and the final Amendment Report was submitted to the Authority on 9 May 2002.

³ The Applicable CUSC Objectives are contained in Standard Condition C7F of the licence to transmit electricity treated as granted to NGC under Section 6 of the Electricity Act 1989 as amended (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.

Respondents' views

NGC issued a consultation paper on 6 March 2002 inviting views from CUSC Parties and interested parties.

NGC received seven responses to the consultation on Proposed Amendment CAP008, of which three were in favour and four opposed to the Proposed Amendment.

Three respondents raised concerns over the removal of the link between proposed changes to the CUSC as a result of "codification errors" and proposed changes evaluated as part of the CUSC Amendment Process as assessed against the Applicable CUSC Objectives. These respondents asserted that Proposed Amendment CAP008 should not be approved as it proposes to "set aside" the Applicable CUSC Objectives and therefore would require the objectives themselves to be changed.

One respondent did not support the view that the Proposed Amendment is seeking to set aside the Applicable CUSC Objectives and stated that, in that respondent's view, the Proposed Amendment would better facilitate achievement of the Applicable CUSC Objective C7F.1(a).

One respondent that supported the Proposed Amendment considered that the CUSC was supposed to faithfully codify the MCUSA except for changes that had to be made to bring NETA into effect. It was the view of this respondent that, were errors to be found in the CUSC because of a failure to transpose the MCUSA properly, then the correction of such errors should not need to satisfy the Applicable CUSC Objectives.

Two respondents considered that it might be difficult to judge whether a change in effect arising from the migration process from the MCUSA to the CUSC was in fact a "codification error" or an intentional change required as a result of the new market arrangements. One respondent asserted that whether such changes were intentional or unintentional was a matter for the Authority to determine.

One respondent that supported the Proposed Amendment asserted that the incorporation of "codification errors" into the Transitional Issues section of the CUSC is required in order to enable NGC to be able to efficiently discharge its obligations under the Electricity Act 1989 and its Transmission Licence. This respondent considered that currently under the CUSC there is no suitable process or mechanism defined for disputes arising from "codification errors" that may have a material effect and be detrimental to Users' rights and obligations as existed under the MCUSA. This respondent stated that, late during the development of the CUSC, following representations from a number of Users, NGC recognised the potential for errors arising from codification and made available to Users 'letters of comfort' associated with the CUSC Bilateral and Construction Agreements (codified from elements of the MCUSA Supplemental

Agreements). These 'letters of comfort' provided Users with further assurance that if they identified a clause in their Bilateral Agreements that had not been codified correctly and which changed their contractual position, NGC would act to remedy the error. This respondent considered that the Proposed Amendment seeks the logical extension and recognition of "codification errors" by incorporating them into the main body of CUSC. This respondent also stated that the process and timing of translation of the MCUSA to the CUSC and its subsidiary agreements, schedules, exhibits, supporting methodologies, statements, etc, meant that there was both an "overlap" and "underlap" of sections of the CUSC. The respondent stated that a consequence of this was that it was not possible to "test" that the legal rights and obligations of the User under the MCUSA regime, subject to the intentional changes arising from the migration from the MCUSA to the CUSC, had not been compromised by the migration process.

One respondent that supported the Proposed Amendment considered that the CUSC was introduced over a very tight timescale and therefore that it was not possible to ensure that every element of the MCUSA had been correctly codified into the CUSC. It was the view of this respondent that, although no "codification errors" have yet been identified, there exists the possibility that one or more may be revealed in the future. Were such a "codification error" to be identified, this respondent considered that those CUSC Parties not in possession of a 'letter of comfort' would be in a "difficult interpretation position" relative to those CUSC Parties that are in possession. This respondent therefore considered that the Proposed Amendment would set a "level playing field" on the issue of "codification errors".

The respondents' views are summarised and contained in the Amendment Report in respect of Proposed Amendment CAP008.

Amendments Panel Members' views

It was the opinion of the majority of those Amendments Panel Members expressing a view that Proposed Amendment CAP008, as set out in the Amendment Report, should not be approved. Three Panel Members expressed the view that the Proposed Amendment should be approved.

NGC's recommendation

NGC recommended that the Authority should not approve Proposed Amendment CAP008. NGC considered that that it is not possible for the Proposed Amendment to better facilitate achievement of the Applicable CUSC Objectives since it is proposing that they be set aside for certain CUSC changes. NGC asserted that the CUSC already contains provision for amendment as set out in section 8 and therefore any differences identified between the MCUSA and the CUSC may progress using this process, where they can be properly assessed against the Applicable CUSC Objectives and can be approved or rejected on that basis.

Ofgem's view

Ofgem considers, having had regard to its statutory duties, that Proposed Amendment CAP008, as set out in the Amendment Report, does not better facilitate achievement of the Applicable CUSC Objectives.

It is Ofgem's view that the CUSC documentation, including the full draft text of the CUSC, was subject to extensive consultation by Ofgem, DTI and NGC during the period prior to designation. As part of this consultation process NGC produced an initial draft of the CUSC documentation in September 2000, which was posted on its website along with an accompanying consultation document. MCUSA signatories and other interested parties were informed and invited to participate in a number of working group sessions which took place during October and December 2000. Following this consultation NGC provided Ofgem/DTI with its revised draft of the CUSC documentation, which it also published on its web site on 19 December 2000 with responses invited.

Ofgem considers that the duration and scope of this consultation process was sufficient to enable MCUSA signatories to identify any "codification errors" (unintentional differences arising through the migration from the MCUSA to the CUSC) which they considered would materially alter their principal rights and obligations in relation to connection to and/or use of the NGC Transmission System upon implementation of the CUSC. Further, Ofgem considers that it was the responsibility of MCUSA signatories to identify "codification errors" at this time such that they could be brought to the attention of Ofgem/DTI/NGC through a formal consultation response or at a working group session and considered as part of a subsequent drafting of the CUSC text.

It is Ofgem's view that the designation of the CUSC by the Secretary of State on 25 June 2001 set in place the CUSC as the document representing the principal rights and obligations of Users in relation to connection to and/or use of the NGC Transmission System. Ofgem considers that it was on the basis of the CUSC as designated that MCUSA signatories migrated to become Original Parties to the CUSC Framework Agreement (the agreement which gives contractual effect to the CUSC). Further, Ofgem considers that MCUSA signatories were fully aware that once they became Original Parties to the CUSC Framework Agreement the only mechanism available to them for amending the CUSC would be the CUSC Amendment Procedures, as described in section 8 of the CUSC, under which all Proposed Amendments are evaluated as to whether they would better facilitate achievement of the Applicable CUSC Objectives as compared with the existing CUSC.

Ofgem does not consider it necessary to establish a new process to "facilitate a transparent review and resolution of each and any such [codification error] arising", as put forward by the Proposed Amendment, since the existing CUSC Amendment Procedures already provide for the

transparent review and resolution of Proposed Amendments, including those relating to “codification errors”, should such “errors” be found to exist. It is therefore Ofgem’s view that to establish a new process to evaluate “codification errors”, as put forward for consideration by the Proposed Amendment, would not better facilitate achievement of the Applicable CUSC Objective C7F.1(a).

It is Ofgem’s view that the existing CUSC Amendment Procedures provide transparency and clarity for existing and potential CUSC Users with regard to how their principal rights and obligations may change in the future. The existing Amendment Procedures adequately provide for all Proposed Amendments to be brought to the attention of Users and such other persons as may properly be considered to have an interest; proper consideration of any representations on a Proposed Amendment; and a proper evaluation as to whether a Proposed Amendment would better facilitate achievement of the Applicable CUSC Objectives.

Further, it is Ofgem’s view that, were Proposed Amendment CAP008 to be approved and implemented, a CUSC User would be required to consult both the MCUSA and the CUSC in order to determine its principal rights and obligations in relation to connection to and/or use of the NGC Transmission System. Ofgem considers therefore that the Proposed Amendment would not better facilitate achievement of the Applicable CUSC Objective C7F.1(a).

‘Letters of Comfort’

It is Ofgem’s view that the ‘letters of comfort’ issued by NGC to certain MCUSA signatories relate only to the rights and obligations of that Party as set out in the relevant pre-existing Bilateral Agreement. Proposed Amendment CAP008, in seeking to establish a new process to “facilitate a transparent review and resolution of each and any such [codification error] arising”, would affect the rights and obligations of all CUSC Parties, not only as set out in the Bilateral Agreements but also as set out in the main body of the CUSC. As described previously in this letter, Ofgem considers that the existing CUSC Amendment Procedures already provide for the transparent review and resolution of Proposed Amendments, including those relating to “codification errors”, should such “errors” be found to exist.

The Authority's decision

The Authority has therefore decided not to direct that Proposed Amendment CAP008, as set out in the Amendment Report, should be made and implemented.

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 'A. N. Simpson', written over a horizontal line.

Nick Simpson

Director of Industry Code Development

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