

Date

14 May 2003

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Nicola Northway
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Dear Nicola

DISTRIBUTOR PROVISION OF MPAS SERVICES

We wrote to you on 2 May to point out that Ofgem's proposals dated 16 April 2003 to modify the standard conditions for new distribution licence holders were challengeable in law because they would fetter Ofgem's discretion and override protections given to licence applicants by section 8A of the Electricity Act.

We are sorry to write again so soon and on a similar theme, but we believe that the same kind of issues arise in relation to Ofgem's recent licence modification proposals to require all new licensed distributors, without a distribution services area, to provide MPAS and enquiry services on a regulated basis. Assuming that these proposals are technically workable (itself an arguable point), there is a case both for and against them on policy grounds, and in fact the distribution licence holders within London Electricity Group are generally supportive of the objectives set out in your consultation paper.

Our concern, however, is that the process by which Ofgem is proposing to give effect to those objectives is (i) inconsistent with the expectations created by the current boundary between licensing and exemption, and (ii) removes from new distribution entrants the safeguards that have been provided for them under standard condition 2 of the distribution licence in its current form. In view of the seriousness of this matter, we would expect Ofgem to reconsider its approach and not proceed with the proposals on their present basis.

As you will know, the Electricity (Class Exemptions from the Requirement for a Licence) Order 2001 was drawn up by the DTI on the basis that those whom it did not benefit in respect of distribution activities would, unless they were ex-public electricity suppliers, be subject to a certain limited regulatory regime under the standard distribution licence conditions determined by the Utilities Act licensing scheme. There was a clear expectation that this regime would not include the Section C licence obligations borne by the ex-PES distributors.

This principle is reflected in the structure of standard condition 2 of the distribution licence. Following a lengthy consultation process, this was specifically designed so that Ofgem could not give effect to Section C of the licence, in whole or in part, without a new licensee's consent. At the time of the creation of the new standard conditions, the requirement to obtain the licensee's consent to the switching on of the Section C obligations was considered by all parties, and in particular the DTI, to be an important protection. Yet the modifications which Ofgem now intends to make would reverse the legitimate expectation of a regime for new distribution entrants which is limited to the Section A and Section B licence obligations.

We accept that, at the time when the class exemptions order was being framed, a potential new distribution licensee would have been aware that Ofgem has power under section 11A to modify standard licence conditions pre-emptively. However, there was no expectation at that time that this power would be used mechanically to bring into Part B of the licence key elements of Section C that Ofgem could not otherwise impose on a non-consenting licensee except via a modification under section 14 following an investigation by the Competition Commission.

Ofgem's current proposals circumvent that safeguard and ensure that the burden of the regulatory regime is substantially increased for new distributors without any corresponding opportunity for them to challenge this, except via judicial review. This cannot be right since it effectively removes a protection that was entrenched in the licence for their benefit. Against that background, any potential distributor will be entitled to ask the DTI to consider whether the class exemptions order was drawn widely enough. After all, the DTI, in making that order, was subject to the same statutory duties as apply to Ofgem in its role as a licensing authority.

In view of Ofgem's policy objectives in relation to new distributors, the appropriate (and legally proper) course is for Ofgem to seek the consent of each applicant to the switching on in its licence, through a distribution services direction, of those parts of Section C that are necessary to ensure the provision by the licensee of MPAS and enquiry services for the premises connected to its network. Once such a direction has been given, the area of the network in question is the distribution services area for the purposes of the licence.

Your paper is incorrect to suggest (at paragraph 4.11) that this could only be an interim measure. On the contrary, it would be the proper and enduring measure because it preserves the condition 2 protection for the licensee, in accordance with the process envisaged when the Secretary of State determined the standard licence conditions. It also has the merit of avoiding the drafting complexity and technical weakness of Ofgem's present approach.

We have copied this letter to Edward Blades and Deborah Collins at the DTI.

Yours sincerely

Roger Barnard

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LE Group plc