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Dear Robert,

RE: Notice under section 23 (3) of the Gas Act 1986

Thank you for the opportunity to comment on the amendment to the entry capacity baselines within the Transporter Licence, proposed under s. 23(3) of the Gas Act 1986.

E.ON UK would like to add our support to concerns raised by the industry about the surprising deviation of the Final Proposals from Ofgem's earlier Initial and Updated Proposals for new TPCR baselines. We share concerns already expressed by the industry about the levels of transparency and notification leading up to publication of the final figures, which introduced, in many instances, significant and unexpected reductions to baselines.

We have noted Ofgem's recent response to written questions from the industry arising from a recent Transmission Workstream, in which Ofgem clarified their revised approach to calculating baselines. E.ON UK considers that Ofgem's over-reliance on auction 'signals' is not the most efficient or effective approach to calculating baselines or determining system investment needs. Paragraph 5.3.9 of NGG's 10 year statement states that "*National Grid is unable to take long term auctions as the definitive signal from shippers as to their intentions to flow gas on any particular day.*"

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The exit-entry model was adopted to simplify charging for third party access and to facilitate energy trading at the National Balancing Point. It does not model physical gas flows through the system. It was not designed to facilitate investment decisions, and nor can it be used effectively for investment decisions. Investment decisions in the NTS must continue to be planned by NGG so as to meet the objectives placed on NGG, and in particular the 1-in-20 peak day obligation. NGG must continue to use all their system knowledge and expertise and all relevant information in carrying out their investment planning so as to meet their set objectives. Regulatory pressure from Ofgem on NGG NTS to support its investment decisions with 'user signals' (reinforced with the sanction of disallowing NGG investment) is likely, in our view, to have negative effects on system investment and operation. Consequently, NGG NTS will be incentivised to adopt an overly cautious, risk-averse investment strategy.

We recognise that one of Ofgem's concerns during TPCR was *"the combination of sterilised capacity and the zero reserve price essentially leading to a situation whereby shippers were able to pick up capacity in the short term without providing any signal as to the value of that capacity. This was one of the main reasons that Ofgem proposed introducing a capacity transfer mechanism"*¹. We do not consider that Ofgem's concerns over reserve prices and the link to system investment is a relevant consideration in determining baselines. If the concerns were so significant, this issue should have been explored through industry consultation, separately. Changing baselines to 'force' changes in behaviour in regard of short-term booking of capacity is simply a "back-door" approach to regulation, which does not address the fundamental perceived problems openly and transparently.

Nonetheless, recognising that the new baselines are likely to be implemented by Ofgem, we consider it imperative that Ofgem ensures National Grid NTS meets its Licence Obligation by delivering an entry capacity transfer mechanism as soon as possible; and well before National Grid's suggested earliest implementation date of November 2007 (for sold capacity). We believe it is imperative for the continued efficient and economic operation of the market that a sold, then unsold, capacity transfer mechanism (conducted in that order) is operational as soon as the 2007 AMSEC auction has concluded. If a transfer mechanism is not implemented before this date, the release of entry capacity will not be optimised, which may ultimately prevent gas supplies being delivered to the UK.

Yours sincerely

Richard Fairholme (by email)
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¹ Entry Capacity Baseline Questions - Ofgem's response (2nd March 2007).