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Dear Lesley,

RE: The Exit Capacity Substitution and Revision Methodology Statement - Effective from 1 April 2011

As set out in our previous comments on entry capacity substitution, in principle substitution seems a logical idea (to the extent that it is a method of making better use of existing assets), but that it must be implemented in a way which delivers genuine, long-lasting benefits for the whole market and ultimately customers – not just cost-savings for National Grid NTS. In addition, we are conscious of the potential for unintended consequences that implementation of this methodology may have, due to significant additional complexity in the exit capacity regime for all Shippers, and particularly for new entrants. However, we recognise that these are issues for Ofgem's Impact Assessment rather than the methodology itself.

In respect of some of the points raised in the covering letter:

Timescales

We support the application of substitution only in Y+4 timescales, which is consistent with the starting principle of substitution; to avoid unnecessary network investment. Substituting capacity in shorter timescales presents unacceptable risks to Users, as it provides virtually no notice in order to manage the risk of scale backs. This could have serious consequences for directly connected customers, including CCGTs and gas storage.

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We disagree that substitution should not occur nor capacity be released at all if a revenue driver has not been agreed in advance and included in the licence. This is a problem for NG NTS to resolve with Ofgem. Failure to do so will continue to have an adverse impact on Users of the network.

Exchange Rates

We agree that substitutions should be permitted where the exchange rate is less than 1:1. This is something we argued for strongly during the entry capacity substitution development process but was opposed by NG NTS. Inclusion of this principle makes it inconsistent with entry substitution methodology and therefore, we believe entry substitution requires review in light of this change in policy by NG NTS.

In addition, we offer the following comments on the detail of the proposed methodology:

Para. 40

"The objective shall be to avoid incremental increase in risk". This issue was raised repeatedly throughout the development of entry capacity substitution. It is not clear (as is also the case for entry) whether, if one substitution increases risk and one substitution reduces it, would both be made? As the methodology is drafted, it would seem that only one (de-risking) substitution would be made even if the net result is no change to NG's risk profile overall.

I hope that the above comments prove useful. Should you wish to discuss our response in any further detail, please do not hesitate to contact me on T: 02476 181421.

Yours sincerely,

Richard Fairholme (by email)

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