

Responses from Issue 22

Consultation Issued 7 July 2006

Representations were received from the following parties

No	Company	File number	No BSC Parties Represented	No Non-Parties Represented
1.	E.ON UK Energy Services Limited	Issue22_01	0	1
2.	Good Energy Ltd	Issue22_02	1	0
3.	IMServ Europe	Issue22_03	0	5
4.	BizzEnergy	Issue22_04	1	0
5.	RWE npower	Issue22_05	11	0
6.	Scottish and Southern Energy plc.	Issue22_06	6	1
7.	SmartestEnergy	Issue22_07	1	0
8.	SAIC Ltd. (for and on behalf of ScottishPower)	Issue22_08	7	0
9.	Centrica	Issue22_09	9	0

ISSUE 22 CONSULTATION QUESTIONS

BSC Parties (“Parties”) and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within the consultation document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	<i>Alastair Barnsley</i>
Company Name:	<i>E.ON UK Energy Services Limited</i>
No. of BSC Parties Represented	<i>0</i>
Parties Represented	
No. of Non BSC Parties Represented (e.g. Agents)	<i>1</i>
Non Parties represented	<i>E.ON UK Energy Services Limited</i>
Role of Respondent	<i>Party Agent</i>

Q	Question	Response	Rationale
1.	Do you believe that any of the potential solutions developed by the group would better facilitate the achievement of the BSC Objectives? Do you agree with the group's conclusions in respect of these solutions? Please give rationale.	Neutral	Whilst any of the proposed solutions that propose a change to the methodology for producing the settlement runs will impose a cost on party agents this is not perceived to be significant. As such we would not object to any of the suggested solutions. However as there is no perceived benefit to ourselves from this proposal we would not actively seek to promote any of the proposed solutions.
2.	Which solution (or combination of solutions) do you favour? If you wish, you may also provide a preference ranking instead of a list. Please give rationale.	Neutral	Please see response to question 1
3.	Would you like to make any other comments on Issue 22? Please give rationale.	No	

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Respondent:	<i>Chris Welby</i>
Company Name:	<i>Good Energy Ltd</i>
No. of BSC Parties Represented	<i>1</i>
Parties Represented	<i>Good Energy Ltd.</i>
No. of Non BSC Parties Represented (e.g. Agents)	
Non Parties represented	
Role of Respondent	<i>Supplier</i>

Q	Question	Response	Rationale
1.	Do you believe that any of the potential solutions developed by the group would better facilitate the achievement of the BSC Objectives? Do you agree with the group's conclusions in respect of these solutions? Please give rationale.	Yes	Good Energy believes that the use of Credit rating to determine a credit allowance would be a reasonable solution. While Credit arrangements are there to protect parties in the event of default by another party. They should be done in a way that imposes the minimum resource from parties whom are not a credit risk.
2.	Which solution (or combination of solutions) do you favour? If you wish, you may also provide a preference ranking instead of a list. Please give rationale.		Good Energy favour credit rating similar to that used by distribution businesses as it imposes the least resources to those parties that are credit worthy, especially smaller parties who do not have the benefit of a bank credit rating. It is also simple to maintain.

Q	Question	Response	Rationale
3.	Would you like to make any other comments on Issue 22? Please give rationale.	Yes	Maintaining credit by cash or LoC locks up valuable resources the cost of which are ultimately borne by the customer. Any system that allows parties to avoid credit cover by virtue of a good payment record should be supported. It should also be cost efficient to implement and maintain.

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Respondent:	<i>Clare Hannah</i>
Company Name:	<i>IMServ Europe</i>
No. of BSC Parties Represented	
Parties Represented	
No. of Non BSC Parties Represented (e.g. Agents)	<i>5</i>
Non Parties represented	
Role of Respondent	<i>Party Agent: HHDC, HHDA, NHHDC, NHHDA and MOP</i>

Q	Question	Response	Rationale
1.	Do you believe that any of the potential solutions developed by the group would better facilitate the achievement of the BSC Objectives? Do you agree with the group's conclusions in respect of these solutions? Please give rationale.	Yes / No	
2.	Which solution (or combination of solutions) do you favour? If you wish, you may also provide a preference ranking instead of a list. Please give rationale.	Yes / No	
3.	Would you like to make any other comments on Issue 22? Please give rationale.	Yes	As Agents we are not affected by the issue under discussion and therefore do not believe that it is relevant for us to respond to the above questions. However, as one of the “recommended” options (i.e. Changing the SVA

Q	Question	Response	Rationale
			<p>Timetable) is totally dependant on a process performed by Agents, we do have some comments relating to this particular option.</p> <p>This is the third consultation which the Group has initiated with regard to Issue 22: each of the previous two has resulted in many Agents highlighting their concerns regarding the proposed option at various Industry meetings. IMServ has responded to each of these consultations noting the technical problems which could both affect the accuracy of the proposed approach and also result in further Market issues.</p> <p>The SVA Agent has echoed some of these same concerns in their initial response which has been included in this third consultation document. Responses to the second consultation could potentially support the view that this recommended option is of questionable accuracy/ prone to non-completion.</p> <p>It could therefore be misleading to further consult on a “preferred” option which may not be viable: this also appears inefficient in terms of gathering Market opinion.</p> <p>In conclusion, we are disappointed that this third consultation has been issued by the Group prior to their review of the responses to the second consultation (as per last sentence of section 3.2.5). We understand that there are no timescales attached to the completion of the work being performed by the Group which would indicate that it would have been possible to postpone this third consultation and progress the issue in a more considered manner.</p> <p>In addition we would recommend that in issuing any consultation that all responses received from any previous consultation are made available as reference information in order that this might stimulate further opinion on the issue in question.</p>

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Respondent:	<i>Steve Fearn</i>
Company Name:	<i>BizzEnergy</i>
No. of BSC Parties Represented	<i>One</i>
Parties Represented	<i>BizzEnergy</i>
No. of Non BSC Parties Represented (e.g. Agents)	
Non Parties represented	
Role of Respondent	<i>Supplier</i>

Q	Question	Response	Rationale
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Q	Question	Response	Rationale
1.	Do you believe that any of the potential solutions developed by the group would better facilitate the achievement of the BSC Objectives? Do you agree with the group's conclusions in respect of these solutions? Please give rationale.	Yes	<p>Solutions 3.2.2 and 3.2.5 would both contribute to improving the accuracy of data used in the credit cover calculations which can only support BSC Objective (c) by ensuring a party is only required to provide credit to match their actual position.</p> <p>Solution 3.2.1 would also support Objective (d) by allowing many participants not to have to manage their credit position as actively under normal conditions where they are attempting to balance their positions and minimise trading charges.</p> <p>Solution 3.2.4 could potentially support Objective (d) as the risk of a party defaulting would be borne by a third party rather than managed within the BSC. This solution requires further development however before a final conclusion could be drawn on its merits.</p> <p>We believe that solution 3.2.3 would actually hinder Objective (c) by requiring additional working capital to be tied up in deposits. This could be considered to cause greater impact on smaller parties and provide a barrier to entry. A more efficient solution to the problem of parties defaulting might be to create a modification reducing the 20 day wait before action can be taken against non-paying parties.</p>

Q	Question	Response	Rationale
2.	Which solution (or combination of solutions) do you favour? If you wish, you may also provide a preference ranking instead of a list. Please give rationale.		<p>Our favoured combination of solutions would be the extended II settlement run laid out in solution 3.2.5 but with the manner of calculation of the CEI portion performed as suggested in solution 3.2.2 as opposed to the latter half of 3.2.5. The credit ratings described in 3.2.1 could be overlaid as an additional layer if also popular. We feel that the method of calculating CEI described in 3.2.2 would have better scope to accurately approximate public holidays and other unusual day types than the average described in the latter half of 3.2.5.</p> <p>Indeed regardless of the solution (if any) decided upon to improve the current credit cover arrangements we would favour implementing the improved II settlement run described in 3.2.5 as well. Allowing actual metered volumes in to settlement earlier can only improve accuracy and has benefits to many other areas outside the credit arrangements.</p> <p>The basic principle behind solution 3.2.4 is also appealing to ourselves although until further details can be provided by the insurance broker it is difficult to judge whether this option would be more favoured than the combined suggestion above.</p> <p>We would be against the implementation of solution 3.2.3.</p>
3.	Would you like to make any other comments on Issue 22? Please give rationale.	Yes	<p>While several of the identified solutions would be an improvement to the credit cover arrangements none of them would be perfect and so we would like to see the existing material doubts provisions continue to allow parties to challenge requirements for additional credit where they believe there is convincing evidence that the data these calculations are based on is not representative in some manner.</p>

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Respondent:	<i>Carl Wilkes</i>
Company Name:	<i>RWE npower</i>
No. of BSC Parties Represented	<i>11</i>
Parties Represented	<i>Please list all BSC Party names of Parties responding on behalf of (including the respondent company if relevant) RWE Trading GmbH, RWE Npower plc, Great Yarmouth Power Ltd, Npower Cogen Trading Ltd, Npower Commercial Gas Ltd, Npower Direct Ltd, Npower Ltd, Npower Northern Ltd, Npower Northern Supply Ltd, Npower Yorkshire Ltd, Npower Yorkshire Supply Ltd</i>
No. of Non BSC Parties Represented (e.g. Agents)	<i>None</i>
Non Parties represented	<i>Please list all non Parties responding on behalf of (including the respondent company if relevant).</i>
Role of Respondent	<i>(Supplier/Generator/ Trader / Consolidator / Exemptable Generator / Party Agent</i>

Q	Question	Response	Rationale
1.	Do you believe that any of the potential solutions developed by the group would better facilitate the achievement of the BSC Objectives? Do you agree with the group’s conclusions in respect of these solutions? Please give rationale.	Yes	Recent experience has shown that the current arrangements are not sufficient. We are particularly in favour of one of the group’s suggestions (see answer to question 2).
2.	Which solution (or combination of solutions) do you favour? If you wish, you may also provide a preference ranking instead of a list. Please give rationale.		Our favoured solution would be to use Credit Ratings to determine a Credit Allowance threshold.

Q	Question	Response	Rationale
3.	Would you like to make any other comments on Issue 22? Please give rationale.	No	

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Respondent:	<i>Andrew Colley</i>
Company Name:	<i>Scottish and Southern Energy plc.</i>
No. of BSC Parties Represented	<i>6</i>
Parties Represented	<i>SSE Energy Supply Ltd., SSE Generation Ltd., Keadby Generation Ltd., Medway Power Ltd., Southern Electric Power Distribution plc., Scottish Hydro-Electric Power Distribution Ltd.</i>
No. of Non BSC Parties Represented (e.g. Agents)	<i>1</i>
Non Parties represented	<i>SSE Services Ltd.</i>
Role of Respondent	<i>Supplier/Generator/Trader/Party Agent/Distributors</i>

Q	Question	Response	Rationale
1.	Do you believe that any of the potential solutions developed by the group would better facilitate the achievement of the BSC Objectives? Do you agree with the group's conclusions in respect of these solutions? Please give rationale.	Yes	The current process has failed to fully securitise the industry over the Winter of 2005/6 and needs reform. Greater time or flexibility needs to be introduced within the process to allow for debt to be called in through the courts if required. As such we believe that either a process based on market capitalisation/credit rating or independent assessment of financial strength, or an improved approximation of metered energy coupled with an elongated period of credit cover will provide better security for BSC Parties.

Q	Question	Response	Rationale
2.	Which solution (or combination of solutions) do you favour? If you wish, you may also provide a preference ranking instead of a list. Please give rationale.		<p>SSE favour the adoption of credit scoring methodologies in the first instance, as described within option 3.2.1. This would facilitate a more targeted approach to managing the risk of bad debt, i.e. companies with greater financial strength can rely on their financial assets to underpin their BSC business, companies with lesser financial strength would need to provide additional security. The methodology described (based on Basel II principles) seems an appropriate starting point and is consistent with other areas of the industry. Whilst this would require increased effort to manage the fluctuations in credit scores, such effort would be more effectively utilised than the current effort and cost associated with maintaining or changing constituent parts of the credit calculation. Operational efficiencies would accrue and such a change would have the benefit of reducing the cost of securitisation to the industry as a whole.</p> <p>Whilst this is SSE's preferred approach, SSE are mindful that there may be little appetite for such a change in arrangements, particularly given Ofgem's previous reluctance to change the current mechanisms within their previous review of industry credit arrangements.</p> <p>As such, SSE's second preference is a combination of options 3.2.3 and 3.2.5. We believe that an increase in the period requiring securitisation, as described in 3.2.3, is necessary given experience of the events of Winter 05/06. This demonstrated that the effectiveness of the current arrangements are significantly diluted by the fact that any Party/licensee needs to have entered into liquidation/administration before its licence is revoked and the assets are subjected to Panel ruling or de-energisation or compulsory transfer (i.e. SoLR). The practical impact being that where Elxon is the principle creditor impacted and needs to pursue the debt through the courts, then a lead time of 3 weeks is required by which time the defaulting party is able to substantially increase its indebtedness to the detriment of the market.</p>

Q	Question	Response	Rationale
2.			We also believe that 3.2.5 will provide a better approximation of the energy consumption/production than the current methodology, and in particular facilitate the removal of the significantly inaccurate approximations realised through capacity * load factor calculations. This will provide the additional benefit of removing the need to calculate, submit, approve and monitor such values on a seasonal basis. Whilst we are concerned that the ongoing DTN costs are significant, we still believe that the net ongoing cost, once discounted for the oncosted efficiency savings realised through Elexon operations, is acceptable given the improved approach to managing the risk of bad debt that we believe will ensue.
3.	Would you like to make any other comments on Issue 22? Please give rationale.	No	

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Respondent:	<i>Colin Prestwich</i>
Company Name:	<i>SmartestEnergy</i>
No. of BSC Parties Represented	<i>1</i>
Parties Represented	<i>SmartestEnergy</i>
No. of Non BSC Parties Represented (e.g. Agents)	
Non Parties represented	
Role of Respondent	<i>(Supplier/ Trader / Consolidator /</i>

Q	Question	Response	Rationale
1.	Do you believe that any of the potential solutions developed by the group would better facilitate the achievement of the BSC Objectives? Do you agree with the group's conclusions in respect of these solutions? Please give rationale.	Yes	Improved indebtedness calculations would better facilitate efficiency within the code and encourage competition

Q	Question	Response	Rationale
2.	Which solution (or combination of solutions) do you favour? If you wish, you may also provide a preference ranking instead of a list. Please give rationale.		<p>We favour developing a combination of 3.2.2 (meter counts for NHH for the whole period and HH for the CEI period) and 3.2.5 (getting HH data in the II run). This gives the most accurate assessment of actual physical positions of all the options.</p> <p>Ranking of the remaining ideas in descending order of preference:</p> <p>3.2.3 – simple but blunt 3.2.1 -- Using credit ratings is not going to do anything for the smaller player 3.2.4 -- Using commercial insurance is a non-starter</p>
3.	Would you like to make any other comments on Issue 22? Please give rationale.	No	

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Respondent:	Gary Henderson
Company Name:	SAIC Ltd. (for and on behalf of ScottishPower)
No. of BSC Parties Represented	7
Parties Represented	Scottish Power UK plc, ScottishPower Energy Management Ltd, ScottishPower Generation Ltd, ScottishPower Energy Retail Ltd, SP Transmission Ltd, SP Manweb plc, SP Distribution Ltd
No. of Non BSC Parties Represented (e.g. Agents)	0
Non Parties represented	N/A
Role of Respondent	Supplier / Generator / Trader / Consolidator / Exemptable Generator / Distributor

Q	Question	Response	Rationale
1.	Do you believe that any of the potential solutions developed by the group would better facilitate the achievement of the BSC Objectives? Do you agree with the group’s conclusions in respect of these solutions? Please give rationale.	Yes	See answer to Question 2
2.	Which solution (or combination of solutions) do you favour? If you wish, you may also provide a preference ranking instead of a list. Please give rationale.	Yes	<p>ScottishPower would support implementation of the following options:</p> <p>Using Credit Ratings to determine a Credit Allowance threshold</p> <p>ScottishPower believe that the current credit cover requirements do not adequately reflect the true financial stability of Parties. Parties such as ScottishPower are forced to post credit far in excess of their day to day</p>

Q	Question	Response	Rationale
			<p>operational trading charges (sometimes up to ten times the required amount). As well as being costly to arrange, this ties up funds unnecessarily. As has been seen by the failure of some smaller Parties, the current arrangements do not ensure that Parties have cover appropriate for their own needs. Linking the credit level to both the Parties credit rating and market capitalisation would ensure those Parties who pose a risk to the market would be required to post adequate cover. Financially stable Parties would not be required to post excessive cover. Keeping track of current market capitalisation need not be overly expensive if it were only revised on a periodic basis (e.g. monthly or quarterly), or event based (e.g. in line with a change in a credit rating or a percentage change in the Parties share price)</p> <p><u>Change the SVA Timetable</u> An improved II run would improve the credit arrangements by ensuring most of the HH SVA data was included in the AEI calculation. NHH data is likely to be mostly estimated at this point, but would give an indication of volumes. We also see other benefits in this data being available to Parties this early in the process, e.g. enabling them to validate against their demand forecast process.</p> <p>Our only concern is that this seems to be an overly expensive change for an, as yet undefined level of benefit. Central system change costs seem high for what appears to be a streamlining and standardisation of the current process for dealing with II data. Changes to Parties systems (notably HHDA and Sonet) could be disproportionately expensive for the level of benefit realised. Some sort of cost benefit analysis would be required by ELEXON on central costs.</p>
3.	Would you like to make any other comments on Issue 22? Please give rationale.	Yes	<p>ScottishPower are surprised that the group have decided not recommend the use of FPNs to estimate metered volumes. Although the ELEXON analysis states the inaccuracy of FPNs against historical volumes, the graph seems to show a relatively accurate spread of values. FPNs are considered</p>

Q	Question	Response	Rationale
			perfectly valid for use with interconnector operators. In our experience, Parties tend to trade to their FPN position. A mechanism to encourage the submission of accurate PNs is already contained within the Code

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Respondent:	<i>Dave Wilkerson</i>
Company Name:	<i>Centrica</i>
No. of BSC Parties Represented	<i>9</i>
Parties Represented	<i>Accord Energy Ltd; British Gas Trading Ltd; Centrica Barry Ltd; Centrica Brigg Ltd; Centrica KL Ltd; Centrica KPS Ltd; Centrica PB Ltd; Centrica RPS Ltd; Centrica SHB Ltd</i>
No. of Non BSC Parties Represented (e.g. Agents)	<i>–</i>
Non Parties represented	<i>–</i>
Role of Respondent	<i>(Supplier/Generator/Trader)</i>

Q1: Do you believe that any of the potential solutions developed by the group would better facilitate the achievement of the BSC Objectives? Do you agree with the group’s conclusions in respect of these solutions? Please give rationale.

Yes

Centrica believes that the solution(s) identified in Section 3.2.5 of the consultation document *would* better facilitate the achievement of the BSC Objectives. It has been shown that both the improvement of SVA data in the II run and the revised CEI calculation would be an improvement to the accuracy of the credit calculations, for the reasons outlined in our response to Q2, and therefore we believe both options would better facilitate BSC Objectives (c) and (d). We do not believe, however, that the two options need to be pursued as a single solution. The improvement of the CEI data should be the first priority, and we would indicate a preference for the second CEI improvement option – taking average metered volumes from the most recent number of days necessary. Further detail on this preference is shown in the response to Q2.

We do not believe that any of the other suggested options would better facilitate the achievement of the BSC Objectives, for the reasons outlined below in Q2 and Q3.

Q2: Which solution (or combination of solutions) do you favour? If you wish, you may also provide a preference ranking instead of a list. Please give rationale.

Centrica agrees with the conclusions of the Issue 22 Group in respect of the options that were **not** supported and we do not believe that they merit further investigation.

In respect of the options that **were** generally supported by the Group, we welcome the opportunity to comment on them individually. In summary, we would not support options 3.2.1, 3.2.2, 3.2.3 or 3.2.4, but we would express some support for the options within 3.2.5.

3.2.1 – Using credit ratings to determine a credit allowance threshold.

Arrangements similar to this suggestion exist in the CUSC and are being proposed for the DCUSA. Centrica also notes the Best Practice Guidelines written by Ofgem and noted in this consultation document. However, we believe that it is not appropriate to use credit scoring in the BSC. There are issues around barriers to entry for smaller players; there would be an administrative burden in maintaining the calculations which may well be greater than at present; and the use of market capitalisation as a base is inappropriate, as share price movements can be based on non-BSC-related changes and issues. Centrica would not support this option.

3.2.2 – Using the number of Non-Half-Hourly meters to estimate NHH consumption

It's difficult to come to a firm conclusion on this proposal given the lack of robust and reliable analysis. However, if the aim of this process is to improve the accuracy of the credit calculations, then a solution reliant on a large amount of estimated data is not ideal.

There are also issues around version control and development of NHHDA software, which would need robust solutions to be developed. Centrica would not support this option.

3.2.3 – Extending the Credit Cover Period to 49 days

This option does not address the central concerns of the group, which can be summarised as: a) the perception that there is an over-collateralisation of credit in the market; b) the perception that there is an onerous burden of credit requirements on smaller players; and c) a need for increased accuracy and therefore protection for the market in the event of a Party default. It could be added to one of the other options, as noted in the consultation document, but would have a negative effect on a) and b) above, and a neutral impact on c). Centrica therefore does not believe that there is a positive case for this proposal and would not support it.

3.2.4 – Using commercial insurance

Again, it is difficult to come to a firm conclusion on this proposal due to the lack of any robust cost estimate. However, we would have genuine concerns around the processes for making claims under such a scheme, the length of time it may take to go through a claims procedure, and legal costs arising from

any dispute about claims raised. The market would also be at relatively unmanageable risk from increased premiums. Centrica would therefore not support this proposal.

3.2.5 – Changing the Supplier Volume Allocation Timetable

As noted in the response to Q1 above, Centrica believes that this option is in fact two standalone solutions that should be examined on their own merits. It is not clear from the attached BSC Agent impact assessment what the costs would be of pursuing each of these two options separately – this would be useful information to have.

Undertaking an 'improved' version of the II run

This may give benefits in terms of the general accuracy of the overall credit calculation. It is difficult to quantify this improvement due to lack of information presented in the consultation document, and a comparison of the accuracy of data based on EACs compared to data based on historic share of GSP Group take would help any future deliberations. However, if it could be shown that the improvement was significant, Centrica may support such a proposal.

Changing the calculation of the CEI component of the credit calculation

Centrica believes that this is the most viable of all the options presented, as it directly addresses some of the defects of the current methodology. The issues surrounding the lack of accuracy and the administrative burden of GC/DC and CALF processes have been noted on many occasions. We would also express a preference for the second variant of this solution, where the average metered volume is taken from a smaller number of days than the first variant. This would improve the accuracy of the calculation still further, and would help when needing to take into account any portfolio changes of Suppliers.

We would raise one concern with this method, however. If, for example, the CEI window consists of five weekdays, the days used to derive average metered volume would then consist of two weekend days and three weekdays. It might be better to use for the CEI days the nearest equivalent available day, so a Wednesday in the CEI window would be populated with data from the nearest available Wednesday. There would be issues around public holidays that would need to be managed, but this could be a more accurate option.

We agree with the conclusions of the Group with regard to this solution's use of contract data and lack of actual price data.

If this option were to be raised as a Modification Proposal Centrica would generally be in support, provided that further analysis supported the initial conclusions presented here.

Q3 - Would you like to make any other comments on Issue 22? Please give rationale.

We believe that any Modification originating from this consultation process should also examine the CAP calculation methodology. Each time it has been reviewed, the CAP has been set on an average of SBP, but there is no defined methodology and no comfort that it always will be tied to SBP. Parties are therefore exposed to an increased level of risk compared to a situation where they could perform their own calculations or forecast what CAP will be. A robust and fixed methodology would also relieve the administrative burden for BSCCo.

Please send your responses by **5pm** on **Friday 07 July 2006** to modification.consultations@elexon.co.uk and please entitle your email '**Issue 22 Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Group.

Any queries on the content of the consultation pro-forma should be addressed to Emrah Cevik on 020 7380 4375, email address emrah.cevik@elexon.co.uk