

Responses from P158 Assessment Report

Consultation Issued 26 April 2004

Representations were received from the following parties

No	Company	File number	No BSC Parties Represented	No Non-Parties Represented
1.	Central Networks	P158_AR_001	1	0
2.	British Gas Trading	P158_AR_002	1	0
3.	EDF Trading Ltd	P158_AR_003	2	0
4.	EDF Energy	P158_AR_004	9	0
5.	British Energy	P158_AR_005	3	0
6.	Npower/Innogy	P158_AR_006	10	0
7.	Powergen	P158_AR_007	14	0

P158 _AR_001.txt

From: Deregulation Control Group [dcg@central-networks.co.uk]
Sent: 26 April 2004 09:43
To: Modification Consultations
Subject: Central Networks Response to P158 - P158 Assessment Consultations .

Good Morning,

Central Networks would like to return a response of 'No Comment' to P158 - P158 Assessment Consultations.

Regards,

Deborah Hayward
Distribution Support Office &
Deregulation Control Group
Central Networks West PLC

P158 ASSESSMENT CONSULTATION QUESTIONS

At its meeting on 9 April 2004 the Panel considered the P158 Assessment report and the Settlement Standing Modification Group's recommendation that P158 should not be made.

The Panel decided to submit P158 to the Assessment Procedure for a further month so that a second industry consultation could be undertaken. For details on the Panel's P158 discussions reference should be made to Annex 7 of the Assessment report.

The Panel requested that industry participants have sight of additional information, which only became available after the first consultation period had ended. Therefore, during the second consultation, the SSMG request that participants review the following information before completing the consultation questions:

- Historical evidence of a consolidated Letter of Credit (LoC) being utilised in the past (Section 1.3.8 of the Assessment Report);
- Banking source view provided by the FAA not in support of a consolidated LoC (Annex 7 of Assessment Report); and
- Banking source view provided by the Proposer in support of a consolidated LoC (Annex 7 of Assessment Report).

The SSMG have discussed the above information (Section 1.3.8) and the initial consultation responses (Section 6) which can be found within the Assessment report.

The Panel therefore, have requested that industry participants consider the additional information when assessing whether P158 better facilitates the achievement of the Applicable BSC Objectives.

The Panel have also considered that further assessment of the two main issues associated with P158 was required as follows:

- The perceived level of risk should be quantified. In particular further rationale for and qualification of the perceived risk associated with a consolidated LoC is required; and
- Potential cost savings for Parties needs to be explored further. In particular the savings to Parties potentially utilising P158 must be quantified.

The issues above reflect two arguments for (potential cost savings) and against (risk) the consolidated LoC. Therefore, in order for the SSMG to assess the two arguments against each other, the SSMG requests that industry participants:

- Review the additional information provided;
- Provide comments on the perceived level of risk associated with a consolidated Letter of Credit;
- Quantify responses associated with the potential costs savings P158 offers companies.

The SSMG acknowledge that industry participants have already provided comments on the perceived level of risk during the first consultation, but would like to obtain further comments once the industry has had the opportunity to review the additional information.

BSC 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 this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	Mark Manley
No. of BSC Parties Represented	
BSC Parties Represented	British Gas Trading (BGT)
No. of Non BSC Parties Represented	
Non BSC Parties represented	
Role of Respondent	

Q	Question	Response Error! Bookmark not defined.	Rationale
1.	Do you believe Proposed Modification P158 better facilitates the achievement of the Applicable BSC Objectives (c) in promoting competition and (d) in promoting efficiency? Please give rationale and state objective(s)	Yes	BGT continue to believe that allowing Parties the ability to lodge a consolidated Letter of Credit (LoC) provides a more efficient process for lodging credit. We currently lodge fourteen LoC each year and this not only costs more than it needs to it imposes onerous administrative obligations. This is clearly not the most efficient process that could be utilised to lodge credit. The process imposes inefficiencies on Parties who are required to lodge multiple LoC, removing these onerous obligations would improve efficiency and therefore improve the process. BGT therefore believe that P158 better facilitates Applicable BSC Objective (d). Furthermore during the Assessment phase the FAA has indicated that this change to their current working practices could be incorporated at zero cost. On the basis that the modification proposal introduces efficiencies and therefore cost savings and is costing nothing to implement BGT believes the modification better facilitates Objective (d).

Q	Question	Response Error! Bookmark not defined.	Rationale
			BGT also believe that to a lesser extent the modification proposal better facilitates Objective (c) as it streamlines the process and removes some unnecessary costs from the current process.
2.	Would your company utilise a consolidated Letter of Credit? Please give rationale	Yes	<p>BGT would take advantage of this proposed additional functionality and would lodge a consolidated LoC for the BSC Parties it owns. This would be an improvement on the existing process of lodging credit, which is inefficient and resource intensive. Utilising a consolidated LoC would be a much more efficient process.</p> <p>Furthermore BGT have had discussions with a financial institution which has confirmed they would provide credit cover under a consolidated LoC.</p>
3.	What is the cost benefit of P158 for your company? Please quantify the potential cost savings a consolidated Letter of Credit would provide for your company.	Yes	<p>BGT believe there would be a cost saving in terms of lodging credit cover. BGT would benefit from a saving of approximately £3,500 as there would be only 1 'refresher' charge per year as opposed to the 14 BGT currently pay.</p> <p>BGT would also see a cost benefit in the reduction in man-hours that is currently spent in sourcing and lodging credit cover. A number of people are involved in the process of acquiring and providing the cover. This specifically includes members of the Risk and Treasury functions and an approval process involving senior management. BGT estimate that there is a cost saving of approximately £7,500.</p> <p>BGT also believe the likelihood of problems occurring when lodging credit cover would be diminished by the ability to lodge a consolidated LoC. If there are problems in lodging credit cover then it has been necessary to</p>

Q	Question	Response Error! Bookmark not defined.	Rationale
			provide cash as a short-term fix to the problem. The reduced number of renewals should lessen the chances of this occurring and thereby reduce the costs of lodging credit cover. BGT is unable to quantify those benefits.
4.	<p>i) Do you believe a consolidated Letter of Credit would provide Parties with a suitable level of assurance (taking into account the views which have been expressed as to whether or not a consolidated Letter of Credit would provided a level of assurance equivalent to the existing single Letter of Credit)? Please give rationale.</p>	Yes	<p>BGT in raising this modification proposal had no intention of increasing the risk that BSC Parties may face in the event of a Party going into default. BGT as such do not believe that the proposal increases the risks for BSC Parties and therefore the consolidated LoC provides a suitable level of assurance. To support this conclusion BGT notes the views of ELEXON's internal and external legal advice plus the views of an external credit expert.</p> <p>BGT's internal legal advice also supports the view that providing a consolidated LoC does not increase the risk of non-payment. BGT note the claim by one of the financial institutions that using a consolidated LoC may lead to an application to freeze the funds. BGT believes that if an injunction were to be sought the same risks exist under the current baseline. Furthermore BGT have provided internal legal advice and suggested an amendment to the proposed drafting of the consolidated LoC in an attempt to address these concerns. If this eases the concerns of respondents BGT would be happy to support this change, as it would lessen the likelihood of an application to freeze the credit cover lodged by a party who may be deemed to benefit from the freezing of funds.</p> <p>BGT note the views of one of the financial institutions that suggested it would prefer not to enter into such an agreement. BGT respect that view however we have spoken to a financial institute that has given its agreement in principle to entering into such an agreement. BGT therefore believe it would be possible to lodge a consolidated LoC.</p>
4.	<p>ii) If you believe a consolidated Letter of Credit would not provide Parties with a suitable level of</p>	N/A	

Q	Question	Response	Rationale
	assurance as compared to the current baseline of a single Letter of Credit, please specify the increase in risk you believe to be associated with a consolidated Letter of Credit?	Error! Bookmark not defined.	

Parties are encouraged to provide financial information with regards to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on Monday 26 April 2004** to modifications.consultations@elexon.co.uk and please entitle your email '**P158 Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Michelle Spurdent (Lead Analyst) on 020 7380 4374, email address michelle.spurdent@elexon.co.uk or Thomas Bowcutt (P158 Chairman) on 020 7380 4309, email address Thomas.bowcutt@elexon.co.uk.

P158 ASSESSMENT CONSULTATION QUESTIONS

At its meeting on 9 April 2004 the Panel considered the P158 Assessment report and the Settlement Standing Modification Group's recommendation that P158 should not be made.

The Panel decided to submit P158 to the Assessment Procedure for a further month so that a second industry consultation could be undertaken. For details on the Panel's P158 discussions reference should be made to Annex 7 of the Assessment report.

The Panel requested that industry participants have sight of additional information, which only became available after the first consultation period had ended. Therefore, during the second consultation, the SSMG request that participants review the following information before completing the consultation questions:

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The Panel have also considered that further assessment of the two main issues associated with P158 was required as follows:

- The perceived level of risk should be quantified. In particular further rationale for and qualification of the perceived risk associated with a consolidated LoC is required; and
- Potential cost savings for Parties needs to be explored further. In particular the savings to Parties potentially utilising P158 must be quantified.

The issues above reflect two arguments for (potential cost savings) and against (risk) the consolidated LoC. Therefore, in order for the SSMG to assess the two arguments against each other, the SSMG requests that industry participants:

- Review the additional information provided;
- Provide comments on the perceived level of risk associated with a consolidated Letter of Credit;
- Quantify responses associated with the potential costs savings P158 offers companies.

The SSMG acknowledge that industry participants have already provided comments on the perceived level of risk during the first consultation, but would like to obtain further comments once the industry has had the opportunity to review the additional information.

BSC 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 this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	<i>Steve Drummond for EDF Trading Ltd</i>
No. of BSC Parties Represented	<i>2</i>
BSC Parties Represented	<i>EDF Trading Ltd and EDF (Generation)</i>
No. of Non BSC Parties Represented	<i>None</i>
Non BSC Parties represented	<i>N/A</i>
Role of Respondent	<i>Trader / Generator</i>

Q	Question	Response Error! Bookmark not defined.	Rationale
1.	Do you believe Proposed Modification P158 better facilitates the achievement of the Applicable BSC Objectives (c) in promoting competition and (d) in promoting efficiency? Please give rationale and state objective(s)	Yes	EDFT and EDF(Gen) believe that this modification would primarily promote greater efficiency through the reduction of administration arrangements for all the parties concerned and, therefore, it would in a small way help to promote greater competition.
2.	Would your company utilise a consolidated Letter of Credit? Please give rationale	Yes / No	Possibly, although unlikely at the moment due to the small number required.
3.	What is the cost benefit of P158 for your company? Please quantify the potential cost savings a consolidated Letter of Credit would provide for your company.	None	Because we are unlikely to use it then there is unlikely to be any cost savings. Should we choose to in the future then the savings would be small, no more than £5k per annum.

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4. i)	Do you believe a consolidated Letter of Credit would provide Parties with a suitable level of assurance (taking into account the views which have been expressed as to whether or not a consolidated Letter of Credit would provided a level of assurance equivalent to the existing single Letter of Credit)? Please give rationale.	Yes	Despite reviewing the conflicting opinions from the Financial Institutions given in the report, EDFT and EDF (generation) still cannot understand why a consolidated LoC would provide any less assurance than separate individual LoCs. Elexon would still have recourse to the monies against each relevant account. We acknowledge that this is untried and so may be perceived as being risky, but if this was always an acceptable reason for not doing something there is the danger that nothing would change.
4. ii)	If you believe a consolidated Letter of Credit would not provide Parties with a suitable level of assurance as compared to the current baseline of a single Letter of Credit, please specify the increase in risk you believe to be associated with a consolidated Letter of Credit?		

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Respondent:	Tony Diccico – EDF Energy
No. of BSC Parties Represented	9
BSC Parties Represented	EDF Energy Networks (EPN) plc; EDF Energy Networks (LPN) plc EDF Energy Networks (SPN) plc; EDF Energy (Sutton Bridge Power) EDF Energy (Cottam Power) Ltd; EDF Energy (West Burton Power) Ltd; EDF Energy plc; London Energy plc; Seeboard Energy Limited
No. of Non BSC Parties Represented	0
Non BSC Parties represented	N/A
Role of Respondent	Supplier/Generator/ Trader / Party Agent

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P158 better facilitates the achievement of the Applicable BSC Objectives (c) in promoting competition and (d) in promoting efficiency? Please give rationale and state objective(s)	Yes and No	EDF Energy believes this P158 could better facilitate applicable BSC Objective (d) by potentially reducing administration costs. This could also have a knock-on effect to help competition if Parties are able to operate under more efficient processes.
2.	Would your company utilise a consolidated Letter of Credit? Please give rationale	Possibly	EDF Energy is indifferent to this modification and are not sure at this point if we would use a consolidated LoC.
3.	What is the cost benefit of P158 for your company? Please quantify the potential cost savings a consolidated Letter of Credit would provide for your company.	N/A	

Q	Question	Response	Rationale
4. i)	Do you believe a consolidated Letter of Credit would provide Parties with a suitable level of assurance (taking into account the views which have been expressed as to whether or not a consolidated Letter of Credit would provided a level of assurance equivalent to the existing single Letter of Credit)? Please give rationale.	Yes	EDF Energy is of the opinion that a consolidated LoC would be sufficiently robust and as workable as the current single LoC. External legal advice in the Assessment Report is consistent with this view.
4. ii)	If you believe a consolidated Letter of Credit would not provide Parties with a suitable level of assurance as compared to the current baseline of a single Letter of Credit, please specify the increase in risk you believe to be associated with a consolidated Letter of Credit?	N/A	

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P158 ASSESSMENT CONSULTATION QUESTIONS

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Respondent:	<i>Martin Mate</i>
No. of BSC Parties Represented	<i>3</i>
BSC Parties Represented	<i>British Energy Power & Energy Trading Ltd, British Energy Generation Ltd, Eggborough Power Ltd</i>
No. of Non BSC Parties Represented	<i>-</i>
Non BSC Parties represented	<i>-</i>
Role of Respondent	<i>Supplier/Generator/Trader/Consolidator/Exemptable Generator/Party Agent</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P158 better facilitates the achievement of the Applicable BSC Objectives (c) in promoting competition and (d) in promoting efficiency? Please give rationale and state objective(s)	No	<p>Although some parties may obtain efficiency gains from the proposal, these benefits have still not been quantified in any detail. On balance we are unconvinced that the efficiency gains for the industry as a whole merit the costs under the BSC and to individual parties (BSC Objective (d) not met), and have some concerns that competition may be diminished by allowing efficiencies to parties which are part of larger groups (BSC Objective (c) not met).</p> <p>Companies weigh up the advantages and disadvantages of operating as a larger consolidated company or smaller affiliations of individual companies. The BSC credit requirements are only one of the factors a company must take into consideration in choosing its corporate structure and trading methods. The BSC currently treats parties as individual entities for financial and legal purposes (with the exception of voting), and this avoids any charge that the BSC favours larger groups of companies or discriminates against smaller or single company parties.</p>

Q	Question	Response	Rationale
2.	<p>Would your company utilise a consolidated Letter of Credit? Please give rationale</p>	Unlikely	<p>Unlikely. The benefits of the proposal indicated in the consultation document appear to be limited. BE currently provides most of its credit through one party, the party undertaking group external trading and to which most physical energy is credited. In any case, all the normal processes for increasing or reducing levels of credit for individual parties would apply. The main saving in internal effort would be the ability to undertake changes for more than one party at the same time, but these savings are probably not large. There may be some benefits where credit can be swapped from one party to another without changing the overall level, but in practice these would still require similar effort at a party level as at present. Negotiation for provision of consolidated credit from a provider would probably incur up-front costs, and provision for the service may incur an explicit or implicit operating cost.</p>
3.	<p>What is the cost benefit of P158 for your company? Please quantify the potential cost savings a consolidated Letter of Credit would provide for your company.</p>		<p>No clear benefit identified. Potential small internal operational savings would need to be weighed against definite set-up and management of the consolidated credit arrangement.</p>
4.	<p>i) Do you believe a consolidated Letter of Credit would provide Parties with a suitable level of assurance (taking into account the views which have been expressed as to whether or not a consolidated Letter of Credit would provided a level of assurance equivalent to the existing single Letter of Credit)?</p>	No	<p>Advice received by Elexon indicates a possible risk that calling on credit for one party covered by a consolidated Letter of Credit could affect, delay, or even block, its use in relation to other parties. If this risk is proven to exist and is not removed, it would represent a reduction in assurance to other parties compared with current arrangements. Otherwise, the proposal as currently constituted appears to provide a level of protection equivalent to the current requirement.</p>
4.	<p>ii) If you believe a consolidated Letter of Credit would not provide Parties with a suitable level of assurance as compared to the current baseline of a single Letter of Credit, please specify the increase in risk you believe to be associated with a consolidated Letter of Credit?</p>		<p>See response to question 4(i).</p>

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P158 ASSESSMENT CONSULTATION QUESTIONS

Respondent:	<i>Carl Wilkes</i>
No. of BSC Parties Represented	<i>Ten</i>
BSC Parties Represented	RWE Trading Gmbh, RWE Innogy plc, Innogy Co-gen Ltd, Innogy Co-gen Trading Ltd, Npower Direct Ltd, Npower Ltd, Npower Northern Ltd, Npower Northern Supply Ltd, Npower Yorkshire Ltd, Npower Yorkshire Supply Ltd
No. of Non BSC Parties Represented	
Non BSC Parties represented	<i>Please list all non BSC 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 Error! Bookmark not defined.	Rationale
1.	Do you believe Proposed Modification P158 better facilitates the achievement of the Applicable BSC Objectives (c) in promoting competition and (d) in promoting efficiency? Please give rationale and state objective(s)	No	Please see answer to 4 (i).
2.	Would your company utilise a consolidated Letter of Credit? Please give rationale	No	There are no plans to use these type of letters at present.
3.	What is the cost benefit of P158 for your company? Please quantify the potential cost savings a consolidated Letter of Credit would provide for your company.		Potential savings are small e.g. £500 - £1000 p.a.

Q	Question	Response Error! Bookmark not defined.	Rationale
4. i)	Do you believe a consolidated Letter of Credit would provide Parties with a suitable level of assurance (taking into account the views which have been expressed as to whether or not a consolidated Letter of Credit would provided a level of assurance equivalent to the existing single Letter of Credit)? Please give rationale.	No	We are concerned that the terminology now being used is 'suitable level of assurance'. The advice received so far suggests that the use of Consolidated Letters of Credit would increase risk to the market. No relevant party has given a categorical assurance that they would not increase risk.
4. ii)	If you believe a consolidated Letter of Credit would not provide Parties with a suitable level of assurance as compared to the current baseline of a single Letter of Credit, please specify the increase in risk you believe to be associated with a consolidated Letter of Credit?		This is difficult to quantify because the market has no direct experience of this type of change. However, we believe the increase would far outweigh the small level of benefits on offer.

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Respondent:	<i>Powergen</i>
No. of BSC Parties Represented	<i>14</i>
BSC Parties Represented	Powergen UK plc, Powergen Retail Limited, Cottam Development Centre Limited, TXU Europe Drakelow Limited, TXU Europe Ironbridge Limited, TXU Europe High Marnham Limited, Midlands Gas Limited, Western Gas Limited, TXU Europe (AHG) Limited, TXU Europe (AH Online) Limited, Citigen (London) Limited, Severn Trent Energy Limited (known as TXU Europe (AHST) Limited), TXU Europe (AHGD) Limited and Ownlabel Energy
No. of Non BSC Parties Represented	N/A
Non BSC Parties represented	N/A
Role of Respondent	<i>Supplier/ Generator/ Trader / Exemptable Generator</i>

Q	Question	Respos e Error! Bookmark not defined.	Rationale
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Q	Question	Response <small>e Error! Bookmark not defined.</small>	Rationale
1.	Do you believe Proposed Modification P158 better facilitates the achievement of the Applicable BSC Objectives (c) in promoting competition and (d) in promoting efficiency? Please give rationale and state objective(s)	No	<p>We believe that the negligible benefits to be gained from efficient sourcing/administration to be outweighed by the potential risk of a party going in to default because of a flawed LoC. We therefore consider this modification to have a potentially negative impact on applicable BSC objective 'C'. Please refer to (4) for clarification of the perceived risk.</p> <p>We also note that a financial institution has even questioned whether P158 would facilitate efficient administration.... <i>'Whilst it would be possible to issue a standby on behalf of multiple applicants it could potentially cause problems from an operational point of view in that the lender could only record a liability against one name. To record against multiple names, covered by a consolidated LoC, the lender would need to open a separate instrument for each applicant to record their portion of the overall liability. The lender would also need to have a 'base' file which would be the actual instrument that the lender would issue and all of these files would need to be cross referenced. Due to the extra work involved and greater potential for errors the source suggested that it would prefer to steer clear of this type of document.'</i> (74/007 – ELEXON Assessment Report for P158).</p>
2.	Would your company utilise a consolidated Letter of Credit? Please give rationale	No	At present we would not wish to utilise a consolidated letter of credit.
3.	What is the cost benefit of P158 for your company? Please quantify the potential cost savings a consolidated Letter of Credit would provide for your company.	No benefit	We do not perceive there to be any tangible benefit for our company from this modification. We are however concerned that in the event that a group of companies enter credit default, the potential cost to our company (as to the industry) could be significant should the LoC not prove to be robust as a result of P158.

Q	Question	Response <small>e Error! Bookmark not defined.</small>	Rationale
4.	i) Do you believe a consolidated Letter of Credit would provide Parties with a suitable level of assurance (taking into account the views which have been expressed as to whether or not a consolidated Letter of Credit would provide a level of assurance equivalent to the existing single Letter of Credit)? Please give rationale.	No	We do not believe that the consolidated letter of credit provides an equivalent level of assurance when compared against the single LoC.

Q	Question	Response <small>e Error! Bookmark not defined.</small>	Rationale
4.	ii) If you believe a consolidated Letter of Credit would not provide Parties with a suitable level of assurance as compared to the current baseline of a single Letter of Credit, please specify the increase in risk you believe to be associated with a consolidated Letter of Credit?		<p>We believe that the increase in risk is inherent in the preference of a new, relatively untested and unproven format over a historically proven and robust single letter of credit.</p> <p>We note with great concern the advice of one financial institution which foresees a circumstance where... <i>'In the event of a claim against one of the applicants, it would be possible for another applicant to obtain a court injunction to prevent the bank from paying.....any lender would be obliged to act in accordance with the terms of any Court Order, even if it were to 'freeze' the entire standby.'</i> (74/007 – ELEXON Assessment Report for P158)</p> <p>Estimating the potential materiality is relatively straight forward. If P158 does introduce a flawed letter of credit (as indicated by the financial institution above) it may ultimately result in a situation where it is impossible to draw upon the entire consolidated LoC. Arguably it is the combined value of all consolidated LoC which is the potential materiality of this risk.</p> <p>With reference to the Panel minutes we note that one member mentioned the importance of the cost of credit to smaller players. We concur with this point, but agree with the subsequent Panel comment that this modification is aimed purely at the 'large players' and that the issue of security to the industry is of greater import. Furthermore, we believe that smaller players would not be able to take advantage of a consolidated LoC and yet would necessarily be exposed any potential increase in risk.</p>

Parties are encouraged to provide financial information with regards to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on Monday 26 April 2004** to modifications.consultations@elexon.co.uk and please entitle your email '**P158 Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Michelle Spurden (Lead Analyst) on 020 7380 4374, email address michelle.spurdent@elexon.co.uk or Thomas Bowcutt (P158 Chairman) on 020 7380 4309, email address Thomas.bowcutt@elexon.co.uk.