

Consultation for Modification Proposal P157: Replacement of current Supplier Charges rules

A consultation document developed on behalf of the Volume Allocation Standing Modification Group.

For Attention of: BSC Parties and all other interested parties.

Date of Issue: 3 February 2004

Responses Due: 10:00 on 16 February 2004 (To: Modifications@elexon.co.uk)

1. INTRODUCTION

Modification Proposal P157 'Replacement of current Supplier Charges rules', (P157), was raised on 5 January 2004 by EDF Energy. P157 proposes to replace the current Supplier Charges rules in Annex S-1 of the Code with a robust set of rules that adhere to the proposed criteria for a corrective technique suggested by the Volume Allocation Standing Modification Group (VASMGM or the Group) on its work on Issue 6 (Supplier Charges – see Appendix 1).

The Proposer believes that a firm set of transparent rules will improve the quality of data entering Settlement. The latest BSC Audit has been qualified and it is the Proposer's view that a major contributory factor to this was the level of poor data quality in Supplier Volume Allocation especially within the Non Half Hourly sector. Supplier Charges are intended to be a corrective technique but the recent work of the VASMGM on Issue 6 has raised serious concerns over the appropriateness of the current rules and their effectiveness as a corrective technique.

P157 also suggests the effort required to process the existing Supplier Charges rules, calculated using pre-P99 Serials should be minimised, by ensuring that there is no need for the old set of rules to be "run off" over a period of 14 months.

The criteria proposed by the VASMGM under Issue 6 are as follows:

- **Simplicity:** Simplicity should ensure that the technique is understood by all participants and all participants would be aware of the circumstance in which the technique would apply to them. However, the VASMGM suggested that simplicity should not equate to rudimentary.
- **Transparency and Clarity:** Most VASMGM members considered it important that participants are able to see how the Performance Assurance Framework (PAF) techniques were to be applied to them. All elements of the technique should be visible and it should be clear what is expected of participants and what the effects of the technique are.
- **Significant in Magnitude:** The VASMGM agreed that there was little point in having incentives if they only had a negligible financial impact.
- **Progressive and Reflective of Performance:** The VASMGM agreed that incentives should be explicitly linked to a clearly desired outcome. The further participants deviate from their obligations, the bigger the incentive should be to comply.
- **Reflective of Impact:** The VASMGM noted that a failing participant with a significant market share would have a bigger impact on Settlement than a smaller participant. The VASMGM agreed that the ability to scale the technique was desirable, provided that it does not add too much complexity.

- **Immediacy:** The group agreed that incentives work best when the non-compliance is addressed quickly. Delayed processing may have the effect of lessening the impact

2. MODIFICATION GROUP DISCUSSION

The VASMG met on 21 January 2004 to discuss P157. One member of the Group wanted to highlight the importance of P157 in that addressing data quality issues significantly reduces the risk of future qualified audits and as such there ought to be clear incentives for Parties to comply.

2.1 Current Supplier Charges Rules

The Group considered the current Supplier Charges rules. The Group noted that it was difficult to judge whether the current rules provided an adequate incentive on Parties since the billing is currently behind schedule and hence there is currently a lack of *immediacy*. This timing issue compounds the problems of lack of *transparency and clarity* since Suppliers cannot calculate their potential charges using historical data. One member of the Group suggested that the current Supplier Charges framework is utilised & brought up to date before the framework is removed completely. This would allow an informed decision to be made as to whether the current framework does incentivise performance or not, following the application of actual charges. The Group was reminded of their discussions under Issue 6, in which there was agreement regarding the unsuitability of the current rules and which led to the raising of P157. The Group was asked to consider the current Supplier Charges rules in their entirety and whether they felt that they were appropriate or not. A majority of the Group concluded that whilst there were some aspects of the current rules that might be fitting (a definite opinion may only be formed when the rules are running to schedule), there are several aspects that the Group were not happy with and would require change. ELEXON confirmed that they would produce a simplified model of Supplier Charges and the Group and consultation respondents would be able to see what Supplier Charges were, and what they would resemble after certain manipulations e.g. with caps removed.

A majority of the Group thus confirmed the conclusion reached during discussion of Issue 6 – the current Supplier Charges rules in their existing form do not fulfil the criteria developed by the VASMG under Issue 6 and are thus ineffective and inappropriate.

2.2 New Supplier Charge Rules

The Group considered the problems that it had with the current Supplier Charges rules and how to solve them. The Group aimed to highlight the issues such that targeted consultation questions could be asked in the Definition Consultation.

- Use Of Funds

The Group considered how the funds collected from Supplier Charges should be used. Several members of the Group were unhappy with the current procedure in which the funds get redistributed¹, a majority to the Non Half Hourly (NHH) Suppliers in that GSP Group regardless of their performance. This so-called 'money-go-round' means that NHH Suppliers find it difficult to calculate the net amount of money they will have to pay (*Simplicity, Transparency and Clarity*) and that the net amount paid out by a large badly performing Supplier in the GSP Group may be small (*Significant in Magnitude and Reflective of Performance*). One member of the Group commented that whatever mechanism replaces the existing one, the charges should reflect the level of impact on the other Suppliers' businesses and not be set at a penal level that gives them a windfall gain.

¹ 10% to all BSC Trading Parties based on Funding share and 90% to all NHH Suppliers operating in the relevant GSP Group (based on share of total NHH energy in that GSP Group for that month).

The Group considered other uses of the funds collected and decided to consult industry on their respective values. The options considered were

- a) Amended redistribution. This would be a reallocation of the funds such that the NHH Suppliers whose performance was better than average, would receive a higher proportion of the funds to be redistributed. The Group preferred this option
- b) Cover cost of Performance Assurance Framework (PAF). Funds would be used partly for operating the PAF i.e a different type of redistribution. The Group considered that this was a less attractive option as it was benefiting the whole industry including the imperfect Suppliers. In addition this might result in a cap if the PAF costs were over compensated for by the Supplier Charge funds
- c) Keep the funds in a central account and the relevant Party will receive it back when its performance improves. This option has several issues associated with it such as, what to do with the funds if a Party wants to withdraw from the Code and what if a Party's performance never improves.

The Group wondered whether there were any legal issues regarding the use that the funds would be put to and whether any of the options might be deemed to be penalties and hence invalid for consideration. Legal opinion is that the options suggested do not breach the rule against penalties. The rule relates to the reasonableness of funds paid out by a Party as 'recompense' for breach of a contract. These funds must represent a genuine pre-estimate of the losses likely to be suffered by its counterparty(ies) as a result of the breach. The rule is not concerned with the use to which those funds are put once recovered - as long as that use is not itself in further breach of the contract or otherwise illegal.

The Group considered the issue of the use of funds to be an important one and wanted to consult industry on the different options available and see if any additional uses could be suggested.

- Capping

The Group considered whether the current capping rules were appropriate or not. The capping charges were thought to be opaque (*Simplicity, Transparency and Clarity*). The Group considered that the Supplier Charges would be more transparent and easily predictable were no cap applied. The Group determined to consult with industry on this matter. To assist respondents there is some analysis included as Attachment 1 with this consultation document it demonstrates a sample of the current Supplier Charges, using live PARMS Data, to provide a greater understanding of the effects of Supplier Charges costs and reallocations.

- Application of Charges

The Group wanted to consider the different charges that are applied² and which of these would be considered suitable for inclusion in a new set of Supplier Charges and consult the industry on this.

The Serials to which Supplier Charges will apply post P99 Implementation are as follows:

P99 Serials associated with Supplier Charges:

² This refers to post-P99 Supplier Charges, the current legal baseline.

Serial	Name	Description	Old Serial reference
SP01	Delivery of Routine Performance Reports	Monitors timeliness of delivery of PARMS reports. Charges applied per Working Day reports remain incomplete.	Supplier Serial 10
SP02	Delivery of Routine Performance Logs	Monitors timeliness of delivery of drill down data relating to PARMS reports. Charges applied per Working Day reports remain incomplete.	Supplier Serial 11
SP04	Installation of HH Metering in 100kW premises	Monitors when a 100kW premise has not had HH Metering Installed when it should have been. Charge applied per 100kW site, per calendar day Meter not installed.	Supplier Serial 9
SP08(a)	NHH Energy and MSIDs on AAs	Monitors energy settled on AAs. Charges applied for failure to meet the standards at R3 (80% energy on AAs) and RF (97% of energy on AAs).	Supplier Serial 1
SP08(b)	100kW HH Energy and MSIDs on Actuals	Monitors energy settled on Actuals. Charges applied for failure to meet the standards at SF (99% energy on Actuals) and R1 (99% of energy on Actuals).	Supplier Serials 3 & 5
SP08(c)	Non-100kW HH Energy and MSIDs on Actuals	Monitors energy settled on Actuals. Charges applied for failure to meet the standards at RF (99% energy on Actuals)	Supplier Serials 6 & 7

- Force majeure

The Group considered that in a new form of Supplier Charges, a force majeure provision could be included. The following was discussed as part of the hybrid SC proposal during Issue 6.

“A Supplier may claim force majeure against their Supplier Charges. A Supplier should notify the Performance Assurance Administrator (PAA), in writing, at the earliest opportunity, of the start of the force majeure event and again once the force majeure has ended, specifying the last day of the force majeure event. The notification should give details of what the Supplier believes the force majeure event to be and why it will impact their ability to perform to the agreed standards. The Supplier should further detail what actions they took to mitigate the force majeure. All force majeure claims will be considered by the PAB at the time that the performance data becomes available for the RF runs for those Settlement Days that force majeure was claimed. Suppliers may send representation to the PAB to support their claim. The PAB will decide if performance has been impacted as a result of force majeure based on any shift in the performance data. If a force majeure claim is upheld then SCs would be disappplied for those Settlement Days that the force majeure was claimed.”

The Group wished to consult industry on whether to include such a provision.

2.3 Grid Supply Point Group Correction Factor (GSPGCF)

The VASMG under Issue 6 considered the idea of amending the current rules surrounding the application of GSP Group Correction energy. Two possible scenarios were considered. First, to apply a greater proportion of the group correction energy to Estimated Annual Consumptions (EACs), than to Annualised Advances (AAs). The second scenario would see additional volumes being applied directly to EACs (as opposed to applying a Group Correction Factor).

The Group considered the positive and negative aspects, specifically with reference to the criteria, of both scenarios considered under the GSPGCF heading. The Group's discussion is summarised in the table below.

	Applying greater proportion to EAC vs. AA	Adding volume directly to EACs
+	The technique sits within Settlement hence once the parameters are decided it would be simple to implement and would not appear as a penalty	The technique sits within Settlement hence once the parameters are decided it would be simple to implement and would not appear as a penalty
[immediacy]	Non-compliance would be addressed without delay	Non-compliance would be addressed without delay
-	It is complex	It would make Settlement less accurate
[simplicity]	It is difficult to calculate the outcome as it may have unforeseen impacts on energy Imbalance charges and RCRC ³	It is complex
[transparency, clarity, significant in magnitude]	The offence is non half hourly – it may not be appropriate to have a half hourly impact ⁴	It is difficult to calculate the outcome as it may have unforeseen impacts on energy Imbalance charges and RCRC
[reflective of impact, significant in magnitude]	A negative GCF would produce perverse incentives	The offence is non half hourly – it may not be appropriate to have a half hourly impact
		A GCF that is less than unity would produce perverse incentives

The Group considered that the negative aspects of these options far outweighed the positive aspects and a majority of the Group said that it would recommend that these options not be progressed. The Group nevertheless wished to consult industry on them.

Note: the Group after further consideration of this option after the Issue 6 meetings considered that this was not its preferred approach.

2.4 Naming

The VASMG considered two proposals relating to the use of Naming as a corrective technique. The first was to use simple peer comparison reported on a regular basis. This would consist of a league

³ Residual Cashflow Reallocation Cashflow

⁴ This model has a different value every half hour to apply a charge to a Party's under-performance. This value is the imbalance price which can vary widely for reasons not relating to the data a Party enters into Settlement. This is in contrast to Supplier Charges which uses a set value to apply a charge to a Party's under-performance

table ranking Supplier Ids by some agreed performance data. The second idea was to use naming by exception. This would consist of naming Supplier Ids that had breached a certain standard of performance.

The Group considered the principle of naming as a corrective technique and acknowledged that it did not contain a financial element. Bearing this in mind the Group decided that a naming technique could be used as a supplement to another corrective technique that did have financial implications for Parties.

The Group then considered the two naming techniques and the positive and negative aspects of each, specifically with reference to the criteria. The Group's discussion is summarised in the table below

	Peer Group Comparison	Naming by Exception
+ [simplicity] [transparency, clarity] [immediacy] [reflective of performance]	Simple Transparent Reflective of Performance Attention Grabber Better understanding of issues	Less simple Less transparent Reflective of Performance Attention Grabber
? [significant in magnitude]	The Group were unsure whether this could be considered significant in magnitude	The Group were unsure whether this could be considered significant in magnitude
- [reflective of impact]		This is not reflective of impact Smaller Suppliers will vary more and thus may oscillate widely between being named and not There is no indication how those not being named are performing Setting the level at which Parties are named would be difficult and may become a goal in itself It does not incentivise continuous improvement

The Group considered that the peer group comparison naming option was preferred. The Group considered that this would take the form of a league table, produced monthly.

The Group considered what information the league table would show. Several options were suggested, these are;

- a) Settlement Data - related to the data the coupled technique⁵ was drawing on
- b) Settlement Data - *un*related to the data the coupled technique was drawing on
- c) Financial Data – the funds a Party has paid as a result of non compliance

⁵ The coupled technique: This refers to the technique that naming will be used alongside.

The Group considered these three options and stated a preference for (a) as this provided added transparency. It did not like (b) since it considered that if the two techniques were unrelated regarding the data they considered this would be confusing and naming might also receive less attention within the respective companies. It was not keen on (c) since larger Parties are likely to have received larger invoices. The amounts could be scaled relative to Party size, however, the Group considered method (a) more suitable.

The Group decided that the league table would involve publishing performance tables on a monthly basis, split by NHH and Half Hourly (HH) Suppliers. For HH Suppliers the performance at R1 (1st Reconciliation Run) with respect to actuals rather than estimates entered into Settlement would be published whereas for NHH Suppliers the performance at RF (Final Reconciliation Run) with respect to EACs rather than AAs entered into Settlement would be published.

The Group wanted to consult industry as to whether there was support for its approach.

Note: the Group after further consideration of this option after the Issue 6 meetings considered that naming used in isolation was not its preferred approach.

2.5 Other Techniques

2.5a Considered

Another option was suggested by a member of the Group and the Group wished to consult industry on its suitability as a corrective technique.

This technique states that a Party that enters too high a proportion of EACs into Settlement would not be allowed to change the values entered in a Post Final Settlement Run and any EAC entered would have to be greater than or equal to default values applied at RF. It is thought that making Parties enter high EAC values at RF and then not allowing them to alter these would incentivise Parties to meet target AA levels.

2.5b Discarded

The Group also considered the option of not allowing a Supplier, who breached the set performance level, to register any new customers. Several members of the Group considered that this was too harsh.

2.6 Implementation Date

The Group discussed the options available to them to choose an Implementation Date and assist in the development of a legal text. The Group considered the proposed timetable for running Supplier Charges.

If the proposed rate of Supplier Charge calculation is agreed by the Performance Assurance Board (PAB) and maintained, Supplier Charges will be calculated at a rate of 3 months calculation per calendar month. The April 2004 reporting month Supplier Charges will be calculated in November 2004. Therefore November 2004 may be the first calendar month during which the P99 May 2004 Supplier Charges will be calculated.

The Group deliberated what it wanted to bring about from any Implementation Date. The Group considered two things

- To prevent the need to "run off" the pre-P99 Supplier Charges provisions within the Code
- To replace these with a new mechanism that would incentivise Suppliers to enter accurate data into Settlement

The Group's preferred approach would be to implement the new rules coincident with the Implementation of P99 enabling a seamless transition from pre P99 rules to post P157 rules without

the need to run any P99 charges for a limited period. The Group also considered the delay to billing existing for the pre P99 rules on possible Implementation Date decisions. The Group wanted to consider Implementation Dates that would achieve its desired objectives.

3. CONSULTATION

This consultation seeks respondent's views on the issues raised by P157.

For information the Applicable BSC Objectives are;

- (a) The efficient discharge by the Transmission Company of the obligations imposed under the Transmission Licence;
- (b) The efficient, economic and co-ordinated operation by the Transmission Company of the Transmission System;
- (c) Promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity;
- (d) Promoting efficiency in the implementation and administration of the balancing and Settlement arrangements.
- (e) without prejudice to the foregoing objectives and subject to paragraph 3A, the undertaking of work by BSCCo (as defined in the BSC) which is:
 - (i) necessary for the timely and effective implementation of the proposed British Electricity Trading and Transmission Arrangements (BETTA); and
 - (ii) relevant to the proposed GB wide balancing and Settlement Code;and does not prevent BSCCo performing its other functions under the BSC in accordance with its objectives.

You are invited to provide a response in respect of the questions on the attached pro forma.

Please send your responses entitled 'P157 Definition Consultation' by 10:00 on 16 February 2004 to the following email address: Modifications@elexon.co.uk

Any queries on the content of the consultation pro-forma should be addressed to Dena Harris (020 7380 4364) e-mail address Dena.Harris@elexon.co.uk

Appendix 1: Paper 69/020 – Issue 6 report from the VASMG

Meeting name	BSC Panel
Date of meeting	13 November 2003
Paper Title	ISSUE 6 - REPORT FROM THE VASMG
Purpose of Paper	For Information
Synopsis	This paper outlines the issues discussed and the ideas considered by the Volume Allocation Standing Modification Group (VASMG) in relation to Issue 6 'Appropriateness of the Current Supplier Charging Mechanism'.

INTRODUCTION

On 6 August 2003 energywatch asked that the appropriateness of the current Supplier charging mechanism, as an incentive to improve data quality, be considered by a standing Modification Group. energywatch requested that the group explore whether an alternative incentive mechanism could be proposed that would be simpler and more transparent. The issue was logged as Issue 6 and passed to the Volume Allocation Standing Modification Group (VASMG).

The VASMG met four times to consider the issue and this paper provides a summary of the conclusions of the VASMG discussions.

CURRENT SUPPLIER CHARGES MECHANISM

The VASMG discussed the effectiveness of the current Supplier Charge (SC) mechanism. A number of issues were noted by the group and it was concluded that:

- current SCs are not easily understood by industry due to their complexity;
- there is no certainty that the SCs applied for under-performance still represent a genuine pre-estimate of the current losses;
- Suppliers are unable to accurately calculate what their SC liabilities are
- funds collected from one Grid Supply Point (GSP) Group are redistributed to the other Suppliers who may be under performing in other GSP Groups (whilst it was noted that this is where the original loss may have been incurred it is clear that this dilutes the technique as an incentive);
- there is no clear mechanism for disapplication, under appeal or for claims of 'force majeure';
- there is little evidence to suggest that Suppliers' behaviour has changed as a result of the threat or application of SCs (however, one member noted that as SCs have not been applied continuously since NETA Go-Live and as such there is little evidence for the counter argument)
- there are no formal rules for separating liabilities for SCs as a result of a mid month trade sale (and that only a workaround exists).
- the SC capping process further serves to reduce the impact of SCs and reduces the effect of recovering any genuine pre-estimate of loss, by significantly reducing charges.

The VASMG discussed whether the current SC process could be improved by amending the current rules but were unable to conclude that any simple adjustments would significantly improve the process. The example set out in paragraph 3 typifies the difficulty in seeking an effective, simple amendment.

At its final meeting the VASMG concluded that the current SCs were ineffective. This, coupled with the costs of processing, testing workarounds, report checking and query processing led the group to agree that they could be removed.

The group recognised, however, that other corrective techniques should be considered to replace the current SCs. The removal of the current SCs from the Performance Assurance Framework (PAF) would potentially lead to an imbalance in what was intended to be a complementary framework of techniques (a diagram showing the list of PAF techniques, showing where SCs sit within the PAF, is included as Appendix A). Any change would need to be given effect through use of the Modification Proposal process.

EXAMPLE OF AMENDING THE CURRENT MECHANISM - THE REMOVAL OF THE CAPS.

A simple idea would be to remove the caps which reduce the impact of the SCs. In theory this would seem to increase the incentive created by the current SCs by increasing the liabilities involved. In practice the VASMG recognised a number of issues.

Removing the caps would expose Suppliers to potentially unreasonable levels of charges

Removing the caps may impact smaller Suppliers more significantly than larger Suppliers. This is because not all SCs are volume weighted.

The most significant occurrences of SCs for non compliance with Serial 10 (late submission of PARMS data) tend to occur mainly when a newly qualified small Supplier enters the BSC arrangements. This may be because they have not agreed reporting requirements with their Agents or understood the process sufficiently.

The VASMG felt that caps should not be removed without further consideration of the Serials to which the SCs applied.

Do the SCs still represent a genuine pre-estimate of loss if the caps were removed?

The total SCs collected would certainly increase, based on current performance, but it is unclear whether this represents a better genuine pre-estimate of loss than the current SC levels.

Simply removing caps would not resolve the other issues referred to in 2.1

As funds would still be redistributed to those who had created the charges initially, albeit in different GSP Groups, Suppliers would still have no idea of their liabilities (as only one of the complex processes has been removed in this example) and there still remains no clear mechanism for disapplication

PRINCIPLES OF A CORRECTIVE TECHNIQUE

The VASMG concluded that a set of principles should be agreed that could be applied as a test to determine the effectiveness of any corrective techniques. It was the VASMG view that any corrective technique should satisfy a most of these principles.

The principles agreed by the VASMG were:

- **Simplicity:** The VASMG felt that simplicity was a desirable feature of a corrective technique. Simplicity should ensure that the technique is understood by all participants and all participants would be aware of the circumstance in which the technique would apply to them. However, the VASMG suggested that simplicity should not equate to crude. A corrective technique that met all the other principles but remained complex could be preferable to a simple technique that did not meet all the other principles.
- **Transparency and Clarity:** Most VASMG members considered it important that participants are able to see how the PAF techniques were to be applied to them. All elements of the technique should be visible and it should be clear what is expected of participants and what the effects of the technique are. One member observed that, if the incentive were a financial one, then the inability to gauge the cost of failure may incentivise participants to act in accordance with their obligations.

The VASMG noted that the Authority's ability to 'financially incentivise' Parties (through the existing legislative framework) was effective because Parties do not know what the cost of their non-compliance will be. The VASMG acknowledged that the BSCCo may not be able to apply a financial incentive of the same magnitude as the Authority as the BSC is bound to comply with general rules of contract law and by application of 'liquidated damages' as a genuine pre-estimate of loss.

- **Significant in Magnitude:** The VASMG agreed that there was little point in having incentives if they only had a negligible financial impact.
- **Progressive and Reflective of Performance:** The VASMG agreed that incentives should be explicitly linked to a clearly desired outcome. The further participants deviate from their obligations, the bigger the incentive should be to comply. One member suggested that there are some difficulties with the transfer of data at Change of Supplier (CoS) and, therefore, some participants may be penalised for inherited problems. The VASMG noted that issues associated with poor data quality were being addressed elsewhere, and also agreed that the effects of CoS were a business risk and individual Parties should take this into account as part of their Risk Management Plans when taking on new customers.
- **Reflective of Impact:** The VASMG noted that a failing participant with a significant market share would have a bigger impact on Settlement than a smaller participant. The VASMG agreed that the ability to scale the technique was desirable, provided that it does not add too much complexity.
- **Immediacy:** The group agreed that incentives work best when the non-compliance is addressed quickly. Delayed processing may have the effect of lessening the impact.

The group agreed that the current Supplier Charges do not meet these principles.

CORRECTIVE TECHNIQUE IDEAS CONSIDERED BY THE VASMG

A number of ideas for alternative incentive mechanisms and corrective techniques were discussed by the VASMG. For example, one of the ideas was to make Party Agents signatories to the Balancing and Settlement Code so that obligations could be placed directly on Agents. This idea was discounted as it would require primary legislation and could not be explored further within this group.

The group agreed three main ideas for further consideration under Issue 6 which are outlined below. More detailed information on these options can be found in Attachment 2.

Idea 1 - New Supplier Charges:

The VASMG considered a new form of SCs. The components of which are:

- SCs to be based on the percentage of energy entering Settlement only, so Suppliers can easily ascertain their liabilities based on their own performance;
- that no capping should be applied;
- to use Settlement data to allow for apportionment in the event of a trade sale and disapplication in the event of appeal/ 'force majeure' claim
- to have a robust appeal mechanism and mechanism for dealing with 'force majeure' claims
- to allow validation of the data by Supplier
- to use funds collected to contribute to the cost of the PAF (via part of the costs of the BSC Co)

The group agreed that further consideration of the appropriate levels of SCs would be required for any new form of SCs.

The group was unconvinced that an alternative form of SCs had any merits. There remained concerns that the SCs should be a genuine pre-estimate of loss and this may yield SCs that are not sufficient to naturally encourage compliance. The group was also unconvinced that funds should be directed towards the cost of the PAF, especially if the costs of the PAF are reduced then the PAF cost effectively becomes a cap. Similarly the reduction of funds from the BSCCo is a form of redistribution of funds.

Idea 2 – Reallocation of Grid Supply Point (GSP) group correction energy based on estimates submitted into Settlements:

The VASMG considered the idea of amending the current rules surrounding the application of GSP Group correction energy. Two possible scenarios were considered. First, to apply a greater proportion of the group correction energy to Estimated Annual Consumptions (EACs) than to Annualised Advances (AAs). The second scenario would see additional volumes being applied directly to EACs (as opposed to applying a Group Correction Factor).

The group showed interest, particularly for the first idea and noted that it created a financial incentive as an intrinsic part of the trading arrangements. The group were keen to see more detail but also recognised that further consideration of this issue would require significant work to be undertaken, including how this activity would apply to Half Hourly data and how it would be put into practice.

The group also noted that EACs are a legitimate means of settling data and essential to the Supplier Volume Allocation processes. Therefore, any application of group correction energy should avoid creating a perverse incentive to submit inaccurate AAs or Actuals. The group made some suggestions that the incentive could be applied at latter Settlement Runs.

Idea 3 – Naming

The VASMG considered two proposals relating to the use of Naming as a corrective technique. The first was to use simple peer comparison reported on a regular basis. The second idea was to use naming by exception.

The group noted a suggestion that peer comparison could be used on a quarterly basis, posted on the ELEXON website showing performance against the percentage energy Serials. The proposal included a data validation process and appeal process.

The group also noted that a process of naming by exception could be used, akin to the one used for naming when Parties fall into Level 1 or Level 2 Credit Default. Again, the use of the percentage energy Serials was proposed and the technique could be used as a result of participants being outside a certain threshold (e.g. 90% of the standard). The process includes a data validation and query process.

Of the two ideas the VASMG felt naming by exception was the more favourable. It was noted that the rules surrounding this technique would need to be clear, such that no participant is named in error. The group acknowledged that the resistance of industry previously to any form of naming suggests that the technique could be a powerful one. One member suggested that the threat of naming was probably more potent than the naming itself.

General comments

The group briefly considered whether these ideas could be taken forward as a package. It was recognised that naming could exist as a stand alone technique. Naming may be useful in moving a participant from a position, for example, 10% below a standard to within 5% of a standard but would not incentivise an errant participant who chooses to remain non compliant. Therefore the naming would need to be used in conjunction with techniques such as escalation. It was recognised that the naming technique could be used alongside either of the two financial incentives outlined above. However, it felt that it would not be appropriate to use the two financial incentive techniques together as this is effectively a double penalty.

At its final meeting the VASMG noted that the Authority seemed to have the ability to impose more effective financial incentives outwith the Code. The group had previously noted that any financial incentive within the BSC may be constrained by general contract law.

At the extreme end of the BSC Panel powers, any serious or persistent non compliance with the Code, can lead to notices of breach and default, resulting with the ultimate sanction of expulsion from the Code. Whilst this is a useful measure for persistent non compliance it was felt that a lesser but effective corrective technique was desirable to encourage compliance without having to resort to drastic measures.

NEXT STEPS

The ideas contained within this paper and its attachments have been given due consideration by the VASMG, however for any further detailed work to be carried out it would be more appropriate to undertake this under the auspices of a Modification Proposal. The group recognised that any Modification Proposal would need to better meet the combined Applicable BSC Objectives.

The details within this paper and its attachments provide enough information for Parties to consider the effectiveness of the current Supplier Charges mechanism and the potential for alternative corrective techniques, should they wish to raise a Modification Proposal.

RECOMMENDATION

The Panel is asked to **NOTE the discussions and findings of the VASMG.**