

ASSESSMENT REPORT for Modification Proposal P142 Minor refinement to allow a Level 2 Default Cure period in defined circumstances

Prepared by: Settlement Standing Modification Group (SSMG)

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RECOMMENDATIONS

The SSMG invites the BSC Panel to;

- **AGREE that the Proposed Modification P142 should be made;**
- **AGREE a provisional Implementation Date of 3 November 2004, should the Authority determination be received by 23 March 2004;**
- **AGREE a provisional Implementation Date of 23 February 2005, should the Authority determination be received after 23 March 2004 but prior to 13 July 2004;**
- **AGREE that Modification Proposal P142 be submitted to the Report Phase;**
- **NOTE the development and implementation costs for Proposed Modification P142 of £487,130 and ELEXON effort of 138 man days, with an additional 30% tolerance associated with these estimates; and**
- **AGREE that the draft Modification Report be issued for consultation and submitted to the Panel Meeting of 15 January 2004.**

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SUMMARY OF IMPACTED PARTIES AND DOCUMENTS

As far as BSCCo has been able to assess the following parties/documents have been identified as being potentially impacted by Modification Proposal P142.

| Parties | Sections of the BSC | Code Subsidiary Documents |
|---|---------------------------------------|---|
| Suppliers <input checked="" type="checkbox"/> | A <input type="checkbox"/> | BSC Procedures <input type="checkbox"/> |
| Generators <input checked="" type="checkbox"/> | B <input type="checkbox"/> | Codes of Practice <input type="checkbox"/> |
| Licence Exemptable Generators <input checked="" type="checkbox"/> | C <input type="checkbox"/> | BSC Service Descriptions <input checked="" type="checkbox"/> |
| Transmission Company <input type="checkbox"/> | D <input type="checkbox"/> | Service Lines <input type="checkbox"/> |
| Interconnector <input checked="" type="checkbox"/> | E <input type="checkbox"/> | Data Catalogues <input checked="" type="checkbox"/> |
| Distribution System Operators <input type="checkbox"/> | F <input type="checkbox"/> | Communication Requirements Documents <input type="checkbox"/> |
| Party Agents | | |
| Data Aggregators <input type="checkbox"/> | G <input type="checkbox"/> | Reporting Catalogue <input type="checkbox"/> |
| Data Collectors <input type="checkbox"/> | H <input type="checkbox"/> | MIDS <input type="checkbox"/> |
| Meter Operator Agents <input type="checkbox"/> | J <input type="checkbox"/> | Core Industry Documents |
| ECVNA <input type="checkbox"/> | K <input type="checkbox"/> | Grid Code <input type="checkbox"/> |
| MVRNA <input type="checkbox"/> | L <input type="checkbox"/> | Supplemental Agreements <input type="checkbox"/> |
| BSC Agents | | |
| SAA <input type="checkbox"/> | M <input checked="" type="checkbox"/> | Ancillary Services Agreements <input type="checkbox"/> |
| FAA <input checked="" type="checkbox"/> | N <input type="checkbox"/> | Master Registration Agreement <input type="checkbox"/> |
| BMRA <input type="checkbox"/> | O <input type="checkbox"/> | Data Transfer Services Agreement <input type="checkbox"/> |
| ECVAA <input checked="" type="checkbox"/> | P <input type="checkbox"/> | British Grid Systems Agreement <input type="checkbox"/> |
| CDCA <input type="checkbox"/> | Q <input type="checkbox"/> | Use of Interconnector Agreement <input type="checkbox"/> |
| TAA <input type="checkbox"/> | R <input type="checkbox"/> | Settlement Agreement for Scotland <input type="checkbox"/> |
| CRA <input type="checkbox"/> | S <input type="checkbox"/> | Distribution Codes <input type="checkbox"/> |
| Teleswitch Agent <input type="checkbox"/> | T <input type="checkbox"/> | Distribution Use of System Agreements <input type="checkbox"/> |
| SVAA <input type="checkbox"/> | U <input type="checkbox"/> | Distribution Connection Agreements <input type="checkbox"/> |
| BSC Auditor <input type="checkbox"/> | V <input type="checkbox"/> | BSCCo |
| Profile Administrator <input type="checkbox"/> | W <input type="checkbox"/> | Internal Working Procedures <input checked="" type="checkbox"/> |
| Certification Agent <input type="checkbox"/> | X <input type="checkbox"/> | Other Documents |
| MIDP <input type="checkbox"/> | N <input type="checkbox"/> | Transmission Licence <input type="checkbox"/> |
| TLFA <input type="checkbox"/> | | |
| Other Agents | | |
| SMRA <input type="checkbox"/> | | |
| Data Transmission Provider <input type="checkbox"/> | | |

X = Identified in Report for last Procedure
 N = Newly identified in this Report

| | |
|--|--|
| Estimated cost for progressing P142 through Modification Procedures | £ 20,000 + 53 ELEXON man days |
| Cost of implementing Proposed Modification: | |
| Change specific | £62,379 |
| Standalone Release Cost | £252,933 |
| BSC Auditor Effort | £31,531 |
| Clarification of Solution | £15,766 |
| Additional ELEXON Release Costs | £80,000 |
| Operational/maintenance | £44,521 |
| Total: | £ 487,130 + 138 ELEXON man days |

1 DESCRIPTION OF PROPOSED MODIFICATION AND ASSESSMENT AGAINST THE APPLICABLE BSC OBJECTIVES

1.1 Modification Proposal

Modification Proposal P142 "Minor refinement to allow a Level 2 Default Cure period in defined circumstances" ('P142') was raised by Total Gas & Power Ltd on 29 August 2003 (reference 1).

P142 proposes that where a Trading Party's Credit Cover Percentage (CCP) exceeds 90% but remains below 100% outside normal business hours then a Level 2 Default Cure Period shall exist, and shall last until two hours into the next Business Day. Prior to the expiry of the Level 2 Default Cure Period, the Trading Party shall not be considered to be in Credit Default and the Credit Default Refusal and Rejection Periods shall not commence.

The purpose of the Level 2 Default Cure Period is to allow the Trading Party the opportunity to lodge additional Credit Cover during banking hours.

The Proposer contends that, due to restrictions on banking hours, it is currently not feasible for a Party to resolve a Level 2 Credit Default outside business hours by lodging additional Credit Cover. The Proposer further suggests that a lack of sufficient liquidity on the traded power exchanges at such times may reduce the opportunities available to the Party to trade out of Credit Default.

It is argued that this combination of restrictions may mean that a Party who breaches 90% CCP over a weekend or Public Holiday period may not be able to extricate themselves from this circumstance, even if they are financially sound and wish to resolve the breach. A consequence of this is that they may be exposed to significant imbalance charges should a Credit Default Rejection or Refusal Period commence. The consequences of a Credit Default Rejection Period or a Credit Default Refusal Period are prescribed in Section M3.3 of the Balancing and Settlement Code ('the Code'), and are also outlined in Section 1.3 of this document, but may be briefly summarised as a restriction on the ability of the Party to lodge new Volume Notifications that do not decrease CCP in the case of the former, and an ongoing rejection of components of existing Volume Notifications that do not decrease CCP in the case of the latter.

It is contended that the intention of Credit Default procedures, to provide protection for the market against exposure to the unpaid Trading Charges of a Party in genuine financial difficulties, needs to be pragmatically balanced against the ability of a financially sound BSC Party to resolve Credit Default circumstances without being exposed to significant imbalance charges. The Proposer suggested that P142 better achieves this balance and therefore better facilitates Applicable BSC Objectives (c) and (d).

1.2 Issues raised by the Proposed Modification

The following issues were considered during the Assessment of P142:

- Principles of Credit Cover and the Energy Indebtedness calculation;
- The Terms of Reference (see Annex 7); and
- Possible implementation solutions.

1.3 Assessment of how the Proposed Modification will better facilitate the Applicable BSC Objectives

1.3.1 Principles of Credit Cover and the Energy Indebtedness calculation

The current Credit Default provisions are detailed in Section M3 of the Code. The following summary is intended as a simplified high level explanation and not a definitive statement of the application of the rules to all circumstances.

Under the current trading arrangements, payments to and from Trading Parties in respect of Trading Charges arising on any particular Settlement Day are made, on average, twenty-nine calendar days later. Thus, at any given time, Trading Parties may have debts (or be due payments) in respect of Trading Charges incurred, on average, over the previous twenty-nine days. The purpose of Credit Cover is to ensure that, should a Trading Party default on payments, sufficient collateral is available to pay these debts.

Following Gate Closure for each Settlement Period, the Energy Contract Volume Aggregation Agent (ECVAA) calculates the CCP for each Party. The CCP expresses their Energy Indebtedness, which is an approximation of their expected Trading Charges for the last 29 days, as a percentage of the amount of Credit Cover they have lodged.

Should this CCP exceed defined thresholds then the Credit Default provisions specified in Section M3 of the Code will be triggered, in order to prevent the market from being exposed to unsecured liabilities.

Credit Default is split into two levels, which are separately explained below.

1.3.2 Level 1 Credit Default

Level 1 Credit Default provisions are triggered when a Party's CCP exceeds 80%.

The ECVAA will issue a level 1 default notice via email to the Trading Party indicating that this threshold has been breached and that a Query Period has commenced. This Query Period will expire 24 hours and 5 minutes after the time that the ECVAA records this email has been sent.

At any time during the Query Period, the Trading Party may give a default query notice to the ECVAA indicating that it considers that its CCP has been determined erroneously, providing information to support its view.

If a default query notice has been lodged, the ECVAA will review its calculation for the relevant Settlement Period and redetermine it at the end of the Query Period. If the CCP is recalculated and is found to be not greater than 80%, no further action will be taken.

If no default query notice has been lodged and the Party's CCP is not greater than 75% in relation to any Settlement Period during the Query Period, again no further action will be taken.

If neither of the preceding conditions are met, a Level 1 Credit Default Cure Period will commence upon the expiry of the Query Period and will expire at 24:00 hours on the first Business Day after the day on which the Query Period expired.

If the Party's CCP is not greater than 75% in relation to any Settlement Period during the default cure period, no further action will be taken.

If the CCP has been greater than 75% in relation to all Settlement Periods within the default cure period, then subject to an authorisation notice¹ being in force in relation to that Trading Party pursuant to M3.4 of the Code, the Trading Party shall be in Level 1 Credit Default. The ECVAA will notify the

¹ The BSCCo will not issue an authorisation notice if there is material doubt regarding the CCP calculation.

Party that it is in Level 1 Credit Default and post a notice on the Balancing Mechanism Reporting Service ('BMRS') stating this fact as soon as reasonably practicable.

1.3.3 Level 2 Credit Default

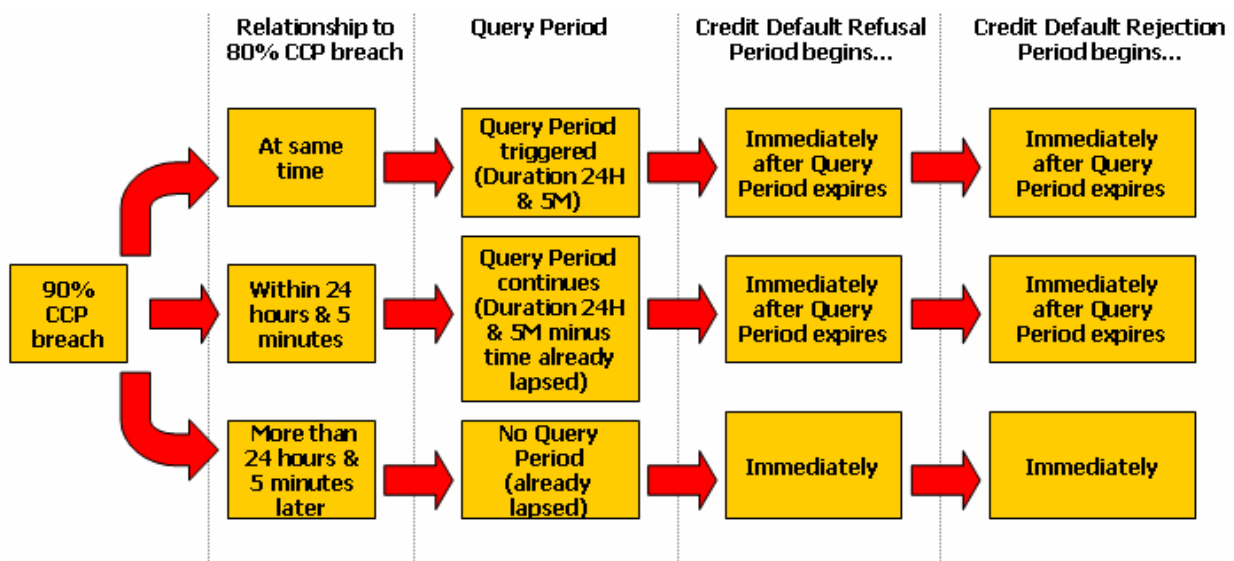
Level 2 Credit Default provisions are triggered when a Party's CCP exceeds 90%.

In this circumstance, subject to an authorisation notice being in force in relation to that Trading Party pursuant to M3.4 of the Code, the Trading Party shall be in Level 2 Credit Default. The ECVAA will notify the Party of this and post a Level 2 Credit Default statement on the BMRS as soon as practicable.

A Credit Default Refusal Period will commence immediately and will expire upon Gate Closure for the first subsequent Settlement Period where the CCP for the Trading Party becomes not greater than 90%. During the Credit Default Refusal Period any Volume Notification submitted that does not decrease the CCP of the Trading Party in any Settlement Period will be refused by the ECVAA in its entirety.

A Credit Default Rejection Period will commence at J+3, where J is the Settlement Period where the 90% CCP breach occurred, and will expire at Gate Closure for the third Settlement Period after the first subsequent Settlement Period in relation to which the CCP for the Trading Party becomes not greater than 90%. Any Volume Notification data already validated will be treated as rejected if it relates to Settlement Periods for which Gate Closure falls within the Credit Default Rejection Period.

Figure 1: Timings for the application of Credit Default Refusal and Rejection Periods under the current rules



This is shown diagrammatically in Figure 1. It should be noted that although the Credit Default Rejection Period criteria are met immediately, its provisions are applied with a short prospective time lag. The ECVAA will read all components of Volume Notifications that are applied to the Settlement Period that is three Settlement Periods after the one for which Gate Closure has just passed. The ECVAA will reject components for that Settlement Period that do not decrease the Energy Indebtedness of the Party in Credit Default. This means the counterparty has a three Settlement Period window in which to lodge an alternate notification to replace the volume rejected. Figure 1 assumes that there is no material doubt upon the calculation that would constrain the BSCCo from issuing an authorisation notice upon the expiry of the Query Period.

The reference to the Query Period lasting for 24 hours and 5 minutes results from the interaction of the Code and the Communications Requirement Document (reference 4), which is a Code Subsidiary Document. Clause M3.2 of the Code states that the Query Period ends 24 hours after the time at

which the level 1 default notice is treated as received by the Trading Party. Clause 3.2 of the Communications Requirement Document states that a level 1 default notice is treated as received 5 minutes after the ECVAA issues it.

1.3.4 Interaction between Level 1 and Level 2 Credit Default

Level 1 and Level 2 Credit Default constitute discrete provisions within the Code, however it should be noted that there is an element of mutual linkage when considering the actions that the ECVAA can take.

Parties breaching 90% CCP will have triggered a Level 1 Query Period in the course of reaching this CCP level and this Query Period may have expired or be ongoing at the time of the 90% CCP breach. This Query Period may overlap all, part or none of a Business Day dependent on the time it was triggered. M3.4 of the Code stipulates that a Trading Party cannot be in Credit Default unless BSCCo has issued an authorisation notice to the ECVAA in relation to them. M3.4.3 goes on to state that such authorisation may not be given earlier than the expiry of the Query Period.

A primary consequence of this is that a Party cannot enter authorised Level 2 Credit Default within 24 hours and 5 minutes of being notified that they have breached the Level 1 Credit Default threshold. This means that a Party breaching the 90% CCP threshold will always have had some prior external warning that their CCP had reached high levels prior to the commencement of Credit Default Refusal or Rejection Periods. They are guaranteed some opportunity to address the Level 1 Credit Default during a Business Day due to the default cure period. They may, or may not, have some opportunity to address the Level 2 Credit Default during a Business Day dependent on the time period covered by their Query Period.

It should be noted that ELEXON has found that in cases where CCP breaches 90%, this frequently occurs within 24 hours and 5 minutes of an 80% CCP breach, resulting in some or all of a Query Period being honoured before Credit Default Refusal or Rejection Periods commence. This may have resulted in an industry perception that an explicit Query Period exists for Level 2 Credit Default. This is not the case.

1.3.5 Definition of Business Hours

'Business hours' is not a defined term within the Code although Business Day and Working Day are. The definition of Business Day within the Code is that it 'Means a day (other than a Saturday or a Sunday) on which banks are open in London for general interbank business in Sterling and, in relation to payment in euro, any such day when in addition the Trans European Automated Real-time Gross Settlement Express Transfer System is operating'. Under the Code, Working Day 'shall have the same meaning as Business Day'.

The Funds Administration Agent (FAA) Service Description defines Working Day as 'the hours between 8:00am and 6:00pm Monday to Friday excluding bank or other public holidays in England and Wales'.

The Modification Group agreed that a two hour default cure period within business hours should be considered to expire at 11:00am on a Business Day. This was based upon common agreement that ordinary banking hours should be considered to be 09:00am to 17:00pm on a Business Day.

It should be noted that the Modification Group sought views upon the precise duration of the default cure period via the consultation questions, responses to which are summarised in section 5 and included in Annex 3 of this document.

1.3.6 Thresholds

The Modification Group agreed that P142 was specifically targeted at defined circumstances where CCP exceeds 90% but remains below 100% outside business hours.

No change is suggested to the treatment of >100% CCP breaches. The Modification Group was in agreement that there is a logical basis for different treatment of CCP breaches within the 90 - 100% bracket. This is because CCP breaches within this bracket may currently result in the refusal or rejection of Volume Notifications despite the affected Party having Credit Cover in excess of their estimated Trading Charges. This is not the case with 100% CCP breaches.

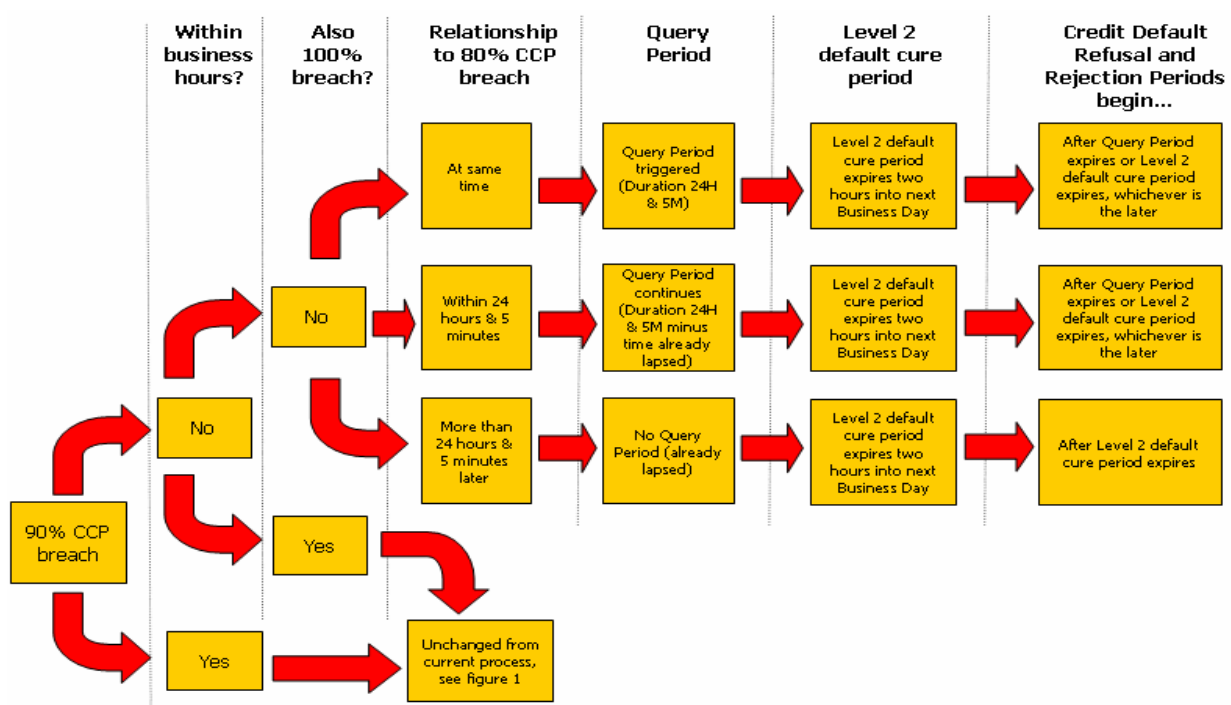
No change is proposed to Level 1 Credit Default provisions applied to 80% CCP breaches as it is not contended that a defect exists in their treatment.

1.3.7 Use of Query Period to address 90% CCP breaches

It was identified that Parties breaching 90% CCP will have triggered a Level 1 Query Period in the course of reaching this CCP level and that this Query Period may have expired or be ongoing at the time of the 90% CCP breach. It was further identified that this Query Period may overlap all, part or none of a Business Day dependent on the time it was triggered.

The Modification Group agreed that P142 is not intended to be applied where the Query Period overlaps an entire Business Day, as the Party breaching 90% CCP would have had an opportunity to lodge further Credit Cover prior to the expiry of the Query Period. The Modification Group further agreed that P142 would only be applied where the Query Period overlaps Business Hours in very limited circumstances. These would be where the Query Period commenced on a non Business Day and expired prior to 11:00 hours on the next Business Day. In such a circumstance, the Level 2 Credit Default Cure Period would be applied in order to ensure that the Party qualified for a two Business Hour window in which to post additional funds. The Modification Group did not support the application of a Level 2 Credit Default Cure Period where the Query Period commenced in Business Hours as it was believed that Parties should have appropriate CCP monitoring systems in place to avoid triggering Credit Default within a Business Day. The Modification Group also did not support the application of a Level 2 Credit Default Cure Period where the Query Period overlapped more than two Business Hours, as in such a circumstance the Party would have had more than two Business Hours during which they could have lodged Credit Cover to reduce their CCP.

Figure 2: Timings for the application of Credit Default Refusal and Rejection Periods under the proposed P142 rules



The principles outlined in this Section are shown diagrammatically in Figure 2. Explanations regarding application of Credit Default Rejection Period and Query Periods and the assumption of absence of material doubt remain in common with the Figure 1 scenario detailed in section 1.3.3 of this document.

1.3.8 Frequency of incidents

The Modification Group asked the BSCCo to check records of Credit Default breaches since NETA go-live to establish the likelihood of P142 scenario incidents arising.

The BSCCo identified 55 incidents of 90% CCP breach in this period. In all but six of these, 100% CCP has been breached. In four of these six, P142 would not appear to have made a difference in the treatment of the Credit Default as either the Query Period overlapped business hours or a material doubt existed which meant no authorisation notice was issued.

There were two incidents which fell within, or close, to the P142 scenario. In both, the Query Period did not overlap Business Hours and the Party entered authorised Level 2 Credit Default outside Business Hours whilst their CCP was below 100%. In both cases the Party subsequently lodged additional Credit Cover during the recommencement of Business Hours, prior to 11:30 am and 10:30 am for the two respective incidents.

1.3.9 Processing window

The Modification Group agreed that Detailed Level Impact Assessments should be sought after their first meeting in order to establish indicative costs and suggested solutions.

It was identified that the FAA Service Description currently requires that if the FAA receives Credit Cover substantially in a form approved by BSCCo, that they shall notify the ECVAA of the resultant Energy Credit Cover² (ECC) on the same Business Day (if received by 15:00 hours); or on the next Business Day (if received after 15:00 hours) and that P142 would require the FAA to notify the ECVAA significantly quicker than these timescales.

It was further noted that P142 was not prescriptive with regard to whether the Level 2 Default Cure Period is one within which the Party should lodge Credit Cover or within which the ECVAA should be using an updated ECC value for the Party. A further potential option was that the Party could have a two hour window within which to lodge funds, whilst the FAA and ECVAA have an additional window within which to process this payment.

Three options were considered, with Detailed Level Impact Assessments sought against three possible processing windows:

1.3.9.1 Option 1

Under this option, a Party would have been deemed to have made payment within the Level 2 Default Cure Period if the FAA were to have confirmed receipt of the additional Credit Cover with a minimum of five minutes remaining within the two hour window (eg 10:55 hours). These five minutes would serve as the minimum timescale within which the FAA and ECVAA would be obligated to take appropriate steps to ensure that the record of ECC held by the ECVAA was updated prior to the expiry of the two hour window (11:00 hours).

For the avoidance of doubt, if payment were to be received by the FAA with less than five minutes of the default cure period remaining (eg after 10:55 hours) there would be no obligation upon the FAA and ECVAA to update the record of ECC held by the ECVAA prior to the expiry of the two hour window (although no prohibition on ECC updates within this period would exist). In such a circumstance, the

² Energy Credit Cover is defined in K2.4.1 of the Code as the amount of the Trading Party's Credit Cover at that time divided by the prevailing Credit Assessment Price.

risk that it would not be possible to update the Party's ECC prior to the expiry of the Level 2 Credit Default Cure Period would rest with the Party.

The BSCCo would inform the FAA on the relevant Business Day that a Level 2 Default Cure Period is being applied to the specific Party.

For the avoidance of doubt, this would mean that the maximum possible window available to the FAA and ECVAAs in which to update the record of ECC held by the ECVAAs and used in the CCP check following Gate Closure would be two hours (eg the FAA received funds at 09:00 hours). The minimum possible window available would be a requirement that the ECC be updated in five minutes (eg the FAA received funds at 10:55 hours).

1.3.9.2 Option 2

Under this option, a Party would have been deemed to have made payment within the Level 2 Credit Default Cure Period if the ECVAAs were to have processed a revised ECC amount within the two hour window.

The FAA would be obligated to calculate revised ECC and notify the ECVAAs of this on a reasonable endeavours basis upon receipt of funds from the Party.

For the avoidance of doubt, the BSC Agents would try to update the ECC position of the Party within ECVAAs as soon as reasonably practicable but the risk that this is not done within the Level 2 Credit Default Cure Period would rest with the Party.

1.3.9.3 Option 3

Under this option, a Party would have been deemed to have made payment within the Level 2 Credit Default Cure Period if the FAA were to have confirmed receipt of the additional Credit Cover within the two hour window. In addition, the FAA and ECVAAs would have a further period within which to action the revised ECC for the Party.

The FAA and ECVAAs would have one hour from the time at which the FAA has confirmed receipt of additional Credit Cover from the Party in which to ensure that the ECVAAs record of ECC is updated.

1.3.10 Determination on which Option should be implemented

The Modification Group noted that both the ECVAAs and the FAA quoted identical change specific costs regardless of which Option was preferred³.

The FAA expressed a preference for Option 3 based upon shorter processing timescales being 'not ideally sufficient and cannot be guaranteed for thorough authorisation of an increase in Credit Cover being received, as Letter of Credit amendments must be fully checked before being authorised'⁴. The FAA also indicated that Option 3 would mitigate risks of failing to update Credit Cover in time within existing insurance liability, but that this might not be the case with the other options and would need to be investigated further were either Option 1 or Option 2 to be adopted.

The Modification Group agreed that Option 3 would be preferred. This option was considered preferable as it maximises the proportion of the two hour Level 2 Default Cure Period available to the Party in which to lodge additional Credit Cover whilst minimising the risk that the BSC Agents would not be able to update their systems in time to prevent the Party entering Credit Default.

It was extensively discussed how breaches of the 100% CCP threshold during this BSC Agent processing window should be treated. A minority opinion was that a Party should not be considered to

³ BSC Agent cost breakdowns are provided separately in section 1.4 of this document.

⁴ Quote from FAA Detailed Level Impact Assessment.

be within Level 2 Credit Default in such a circumstance given that they had taken steps to try to alleviate their Credit Default by lodging additional Credit Cover. The majority opinion within the Modification Group was that breaches of 100% CCP within the BSC Agent processing window should be treated the same as 100% CCP breaches outside this processing window in order to avoid creating inconsistencies in the legal baseline.

1.3.11 Determination on ECVAA solution

The ECVAA put forward two solutions for P142 which are detailed in more depth in their attached Impact Assessment (Annex 5).

The first of these (referred to as the 'Original Solution') was based around an automated solution that parameterised the Level 2 Credit Default Cure Period into ECVAA software.

The second ('Alternative Solution') was based around a semi-manual workaround that reduced ECVAA software changes to the issuing of a new data flow upon 100% CCP breaches and did not parameterise the Level 2 Credit Default Cure Period. The BSCCo would synthetically create the Level 2 Credit Default Cure Period by timing the issuing of authorisation notices such that ECVAA did not inadvertently put the qualifying Party into Credit Default.

The change specific costs attributed to these two solutions were £117,841 and £51,579 respectively in ECVAA costs. In addition, the Alternative Solution would incur a further £8,800 in BSCCo change specific costs.

The Modification Group agreed that the Alternative Solution should be used as this would reduce costs. The Group believed that Level 2 Credit Default Cure Periods would be triggered sufficiently infrequently that system robustness would not be comprised by adoption of a semi-manual workaround.

1.3.12 Analysis of benefits

The Modification Group agreed that P142 did not dilute the deterrent effect of Level 2 Credit Default as the treatment of 100% CCP breaches would remain unchanged, and Parties would therefore still be incentivised to reduce high levels of CCP to avoid the risk of Volume Notification refusal or rejection. Additionally, P142 provides that where a Level 2 default cure period lapsed without the Party taking action to reduce their CCP below 90% that they should be considered to be in Level 2 Credit Default with a Credit Default Rejection and Refusal Period triggered. The Modification Group therefore agreed that the market would not be unnecessarily exposed to risk by P142.

The Modification Group considered that P142 would facilitate competition in the market for several reasons.

It may reduce incentives for the over-provision of Credit Cover. P142 seeks to avoid the circumstance whereby a Party may enter authorised Level 2 Credit Default with a CCP of under 100% and without having had an opportunity to lodge additional Credit Cover. Parties may be providing excessive levels of Credit Cover in order to avoid the risk of this occurrence. P142 may provide assurance that will allow Parties to lodge Credit Cover at more realistic levels.

The easing of such incentivisation towards over-provision of Credit Cover may also remove a barrier to entry to the market by reducing the collateral needed by a new market entrant.

Additionally, the Modification Group considered that P142 may ameliorate perverse incentives on trading behaviour resulting from Level 2 Credit Default. It was considered that under the current baseline, where no default cure period exists for Level 2 Credit Default, a Party breaching 90% outside business hours may be left with no alternative but to trade out of their position. This may result in the Party adopting a non-optimal trading position purely to manage their CCP. The Modification Group considered that this would be unfair on a Party whose CCP remained below 100% as they would be

constricted in their ability to trade freely despite having Credit Cover in excess of their estimated outstanding Trading Charges.

The Modification Group further noted that the lack of an alternative to the Party beyond trading out of their position may impact upon System Buy and Sell Price (SBP/SSP) volatility as they may engage in trades with the Market Index Data Providers (MIDPs) with little flexibility on whether to accept energy prices quoted.

For the above reasons, the Modification Group concluded that P142 would better facilitate Applicable BSC Objective (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’

1.4 Modification Group’s cost benefit analysis of Proposed Modification

In assessing the Proposed Modification, the Modification Group identified that P142 would result in the following BSC Agent costs being incurred:

- Funds Administration Agent: £2,000 in change specific costs. Resulting from changes to the Interface Definition Document Part 1, the FAA Service Description and the FAA contract. Further maintenance charges are of £12,500 to cover the first 40 P142 Credit Cover changes plus ½ man day per change above 40 changes annually.
- Energy Contract Volume Aggregation Agent: £51,579 in change specific costs. Resulting from changes to the software; User Requirement Specification; System Specification; Design Specification; Manual System Specification; Operational Services Manual; procedures; and software testing.

The Modification Group believed these costs would be outweighed by the benefits detailed above in Section 1.3.12 of this document.

1.5 Alternative Modification

Neither the Modification Group, nor any of the respondents to the Consultation Document identified any Alternative Modifications that would, in their opinion, better address the perceived defect.

2 RATIONALE FOR MODIFICATION GROUP’S RECOMMENDATIONS TO THE PANEL

This section summarises the rationale for the SSMG recommendations, further detail can be found in the body of this report.

2.1 Proposed Modification

The SSMG has concluded that:

- P142 would not dilute the deterrent effect of Level 2 Credit Default or expose the market to unnecessary risk.
- P142 would facilitate more effective competition by:
 - reducing incentives for the over-provision of Credit Cover and therefore reduce the opportunity cost of excessive collateral being lodged for this purpose. This would not only benefit existing Parties but also potentially reduce barriers to entry through a decrease in the amount of collateral required for Credit Cover for new Parties; and
 - removing perverse incentives upon a Party whose Credit Cover exceeds their estimated Trading Charges, but who has breached 90% CCP outside business hours, to

potentially submit commercially undesirable Volume Notifications purely to reduce their CCP; and

- o reducing the necessity of a Party breaching 90% CCP to trade out of this position in defined circumstances. This may reduce the likelihood of trades to avert Credit Default being entered into with Market Index Data Providers, and therefore increase the likelihood that the Energy Imbalance Price calculated from Market Index Data (MID) is representative of short-term prices for energy ahead of Gate Closure in the forwards and spot markets.

For these reasons, the Modification Group concludes that P142 would better facilitate Applicable BSC Objective (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’.

The Modification Group acknowledged that the BSCCo had received legal advice stating that Applicable BSC Objective (d) – ‘Promoting efficiency in the implementation and administration of the balancing and settlement arrangements’ - is concerned with central BSCCo costs incurred in implementing and administering the Code. As no BSCCo cost savings were identified during the Assessment Procedure, P142 was not considered to better facilitate achievement of Applicable BSC Objective (d).

2.2 Implementation Dates

In accordance with responses to impact assessment, the recommended Implementation Date for Proposed Modification P142 allows a 32 week lead time following an Authority decision in order to progress the relevant changes through the industry review and approval process. Furthermore, the recommended Implementation Dates are consistent with the BSCCo’s CVA Release strategy.

3 IMPACT ON BSC SYSTEMS AND PARTIES

The development and implementation of P142 will incur costs of approximately £487,130. This encompasses BSC Central Service Agent development and implementation costs of £62,379, plus (standalone) release costs of £252,933. The annual maintenance cost for Proposed Modification P142 will be £44,251 p.a.

This includes additional BSCCo costs of:

- £31,531 (10% of the total BSC Agent cost for the BSC Auditor effort);
- £15,766 (5% of the total BSC Agent cost for any clarification to the solution during development); and
- £80,000 (fixed price for a BSCCo Release).

This excludes BSCCo effort of approximately 138 man days. There is an additional +/- 30% tolerance on the overall cost reflecting contingency against actual implementation resourcing deviating from that expected.

3.1 BSCCo

The following impacts upon BSCCo systems have been identified:

3.1.1 Resourcing for helpdesk calls

P142 would increase the complexity of Section M provisions. BSCCo Service Delivery may see an increase in both the number of helpdesk calls relating to the application of Credit processes and in the time spent addressing these calls.

3.1.2 Need to monitor 100% CCP breaches

Under the current BSC baseline, the BSCCo issues authorisation notices upon the expiry of the Query Period except where material doubt exists. This means the BSCCo can precisely forecast when an authorisation notice should be issued.

The proposed solution will require the BSCCo to delay issuing an authorisation notice where a Level 2 Credit Default Cure Period exists in order to avoid inadvertently triggering the Credit Default Refusal and Rejection Periods parameterised within ECVAA. The Level 2 Credit Default Cure Period could end at any time should the Party breach 100% CCP.

The BSCCo will need to have robust working practices in place to ensure authorisation notices can be issued instantaneously when this happens.

3.1.3 Local Working Instructions

Local Working Instructions ('LWIs') relating to Credit Cover and Credit Default processes will need to be modified.

3.1.4 Implementation effort

Internal Impact Assessments within BSCCo have suggested that a total of 138 man days effort plus £8,800 in change specific costs would be required to implement P142.

This is broken down as follows:

- 126 man days for CVA Programme activity. 100 of these relate to software testing activity applicable to a low complexity release and may be reduced by the presence of other Modifications or Change Proposals that require software changes within the same release. The remaining 26 days is for implementing changes to: the ECVAA User Requirement Specification; ECVAA System Specification; ECVAA Design Specification; ECVAA Service Description; ECVAA Operational Services Manual; Interface Definition Document (IDD) Part 1; IDD Part 2; Business Process Model; and FAA Service Description;
- 12 man days for Assurance activity, for providing required support services to the CVA Programme; and
- £8,800 in change specific costs for Service Delivery, for putting in place LWI changes, training, development of operational service and IT requirements (laptops plus ISDN lines) for out-of-hours duty managers to manage new processes. Service Delivery additionally estimates an annual maintenance cost of between £16,200 and £33,400 dependent on the degree of out of Business Hours management of Credit Defaults required in practice.

3.2 BSC Systems

| System / Process | Potential Impact of Proposed Modification |
|---------------------------------|--|
| Credit Checking Systems | <p>New dataflow identifying 100% CCP breaches</p> <p>ECVAA software will be changed such that a new flow will be sent to the BSCCo where a Party's CCP breaches the 100% CCP threshold. Operating procedures will need to be modified such that the ECVAA also telephones BSCCo to inform them this flow has been sent.</p> |
| Clearing, Invoicing and Payment | <p>Provision of Credit Cover</p> <p>Where a Party qualifies for a Level 2 Credit Default Cure Period and the</p> |

| System / Process | Potential Impact of Proposed Modification |
|------------------|---|
| | FAA receives additional Credit Cover from that Party prior to 11:00 am on the next Business Day, they would have to calculate the Party's Energy Credit Cover and update the ECVAA with this information within one hour. Processing timescales for other transactions would be unaffected. |

3.3 Parties and Party Agents

Six responses were received from Parties in response to the Requirements Specification, five of which indicated that P142 would have no impact in terms of costs, changes or implementation timescales.

The remaining response identified the following impacts:

- Requirement for minor changes to processes to recognise additional time available to post funds to resolve Credit Default;
- Implementation timescale of one week; and
- Minimal implementation costs.

4 IMPACT ON CODE AND DOCUMENTATION

4.1 Balancing and Settlement Code

Section M 'Credit Cover and Credit Default' would be modified to reflect the parameters of the new Level 2 Credit Default Cure Period.

Annex X-1 'General Glossary' would be amended to reflect new definitions of Business Hours and Level 2 Default Cure Period.

The draft legal text is contained within an attached document.

4.2 Code Subsidiary Documents

The following Code Subsidiary documents would need to be modified to reflect the changed BSC Systems and Processes detailed above:

- ECVAA Service Description;
- ECVAA System Specification; and
- FAA Service Description.

4.3 Configurable items

The following configurable items would need to be modified to reflect the changed BSC Systems and Processes detailed above:

- ECVAA User Requirements Specification;
- ECVAA Manual System Specification;
- ECVAA Design Specification;
- ECVAA Operational Services Manual;
- Interface Definition Document Part 1;

- Interface Definition Document Part 2; and
- Business Process Model.

4.4 BSCCo Memorandum and Articles of Association

No changes to the BSCCo Memorandum and Articles of Association have been identified as arising as a consequence of the Proposed Modification.

4.5 Impact on Core Industry Documents and supporting arrangements

No changes to Core Industry Documents or supporting arrangements have been identified as arising as a consequence of the Proposed Modification.

5 SUMMARY OF CONSULTATIONS

| Consultation question | Respondent agrees | Respondent disagrees | Opinion unexpressed |
|---|-------------------|----------------------|---------------------|
| 1) Do you believe Proposed Modification P142 better facilitates the achievement of the Applicable BSC Objectives? | 7 | 2 | 1 |
| 2) Do you believe that there are any alternative solutions that the Modification Group has not identified and that should be considered? | 0 | 9 | 1 |
| 3) Do you believe there are any issues that have not been identified thus far that should be considered as part of the Assessment Procedure? | 0 | 9 | 1 |
| 4) If you agree that a Level 2 default cure period should be put in place, do you believe this should end at 11:00 on the next Business Day, or should more or less time be given? ⁵ | 6 | 2 | 2 |
| 5) If you agree that a Level 2 default cure period should be put in place, do you believe this should only be applied to 90-100% CCP breaches where the Query Period does not overlap business hours at all, or should it also apply where the Query Period overlaps less than two business hours? ⁶ | 1 | 6 | 3 |

5.1 Modification Group's summary of the consultation responses

Ten consultation responses were received, representing the views of 45 BSC Parties.

Seven respondents believed that P142 would better facilitate achievement of the Applicable BSC Objectives, with four stating that it would better facilitate Applicable BSC Objective (c) and three stating that it would facilitate Applicable BSC Objective (d). The most prevalent rationale in support of P142, expressed by six respondents, is that it strikes an appropriate balance between protecting the market from risk and allowing a Party to lodge Credit Cover to alleviate limited breaches of the 90%

⁵ Question 4 was not phrased as a 'Yes/No' question. Where a respondent expressed support for the Level 2 Default Cure Period expiring at 11:00 this has been counted towards the 'Respondent Agrees' column.

⁶ Question 5 was not phrased as a 'Yes/No' question. Where a respondent expressed support for the Level 2 Credit Default Cure Period only applying where the Query Period does not overlap Business Hours, this has been counted towards the 'Respondent Agrees' column.

CCP threshold. Two respondents suggested that it reduced incentives for the over-provision of Credit Cover, with one suggesting that allowing companies to lodge Credit Cover commensurate with their trading activities will better facilitate competition. The two respondents who did not believe that P142 would better facilitate achievement of the Applicable BSC Objectives both expressed the view that it would disincentivise Parties from managing their Credit Cover position.

None of the respondents believed that there are any alternative solutions that the Modification Group had not identified and that should be considered, or that there are any issues that had not been identified that should be considered.

Six respondents agreed that the Level 2 Default Cure Period should end at 11:00 hours on the next Business Day. Within these six agreeing respondents there was a variety of different opinion. One believed there may be a case for the window being longer to take into account different companies ability to process Credit Cover payments to P142 timescales. Two supporting respondents expressed opinions that the window should not be extended for differing reasons, one because they believed two hours was sufficient, the other because they disagreed with the principle of P142 and therefore did not wish to see its scope extended. The two respondents who answered no to this question both expressed the opinion that 11:00 hours was too early within the Business Day for the Party to have lodged additional Credit Cover and that 12:00 hours would be more appropriate.

Six respondents believed that a Level 2 Credit Default Cure Period should be applied where a Query Period overlaps less than two business hours. One respondent cited consistency in application of Level 2 Default Cure Periods in support of this view. The respondent who opposed the extension of Level 2 Default Cure Periods did so on the grounds that it would complicate the solution and that a prudent Party that was not in financial difficulty would be aware of escalating Energy Indebtedness during Business Hours and therefore would not need a Level 2 Credit Default Cure Period. The remaining three respondents were either unsupportive of a Level 2 Credit Default Cure Period (two respondents) or did not express an opinion (one respondent).

5.2 Comments and views of the Modification Group

The Modification Group noted that two respondents had stated that P142 would disincentivise Parties from adequately managing their Credit Cover position. The Group determined that there would be no such disincentive because the Level 2 Default Cure Period would only be applied within strictly limited parameters, and the consequences of breaching 100% CCP, or remaining over 90% CCP at the expiry of a Level 2 Credit Default Cure Period, remained sufficiently severe that Parties would act to avoid them.

The Modification Group gave consideration to the responses to Questions 4 and 5.

It was noted that three respondents gave answers to Question 4 suggesting the Level 2 Default Cure Period should be longer. The Modification Group discussed these concerns whilst noting that an extension to this window would require an Alternative Modification. A consensus opinion was reached that although some respondents might wish the Level 2 Default Cure Period to be longer, no convincing case had been made that this would be a better solution to the perceived defect. In addition, the group believed that two business hours was sufficient time for a financially sound Party to lodge additional Credit Cover.

The Modification Group also gave consideration to the responses to Question 5 in the course of establishing whether there was a consistency issue arising because P142 would establish a deminimis resolution time for CCP breaches in the 90-100% bracket occurring outside business hours that was in excess of that available for breaches in this bracket that occurred shortly before close of business on the Business Day preceding a non Business Day. The Group reached a determination that it would be inappropriate for a number of reasons to extend qualification for a Level 2 Credit Default Cure Period to

such breaches. The Group noted that within Business Hours fluctuations in Energy Indebtedness are entirely driven by the Credited Energy Indebtedness calculation, which is based upon components that are visible to, and predictable⁷ by, the Party. As such a diligent Party would be aware within the Business Day that they would breach Credit Default thresholds and could act accordingly. Additionally it was considered that any attempt to modify the Proposed Modification such that the Level 2 Credit Default Cure Period could straddle a weekend or holiday period could lead to an unwieldy solution that would be hard to operate and understand.

6 SUMMARY OF TRANSMISSION COMPANY ANALYSIS

6.1 Analysis

No impact has been identified resulting from this Modification Proposal that would affect the ability of the Transmission Company to discharge its obligations under the Transmission Licence.

The Transmission Company did not express an opinion as to whether P142 better facilitates the Applicable BSC Objectives.

The Transmission Company did not believe that P142 would impact the computer systems and processes of the Transmission Company, have any implementation costs for them or require any consequential changes to Core Industry Documents.

The Transmission Company had no further comments.

Please see Annex 4 for the Transmission Company Analysis and Impact Assessment Pro-forma.

6.2 Comments and views of the Modification Group

The Modification Group had no comments on the Transmission Company analysis.

7 DOCUMENT CONTROL

7.1 Authorities

| Version | Date | Author | Reviewer | Change Reference |
|---------|----------|--------------|-----------------|----------------------------|
| 0.1 | 20/11/03 | Richard Hall | Roger Salomone | Peer Review |
| 0.2 | 24/11/03 | Richard Hall | SSMG | Modification Group Review |
| 0.3 | 01/12/03 | Richard Hall | SSMG | Modification Group Review |
| 0.4 | 04/12/03 | Richard Hall | Change Delivery | Technical & Quality Review |
| 1.0 | 05/12/03 | Richard Hall | Panel | For Decision |

7.2 References

| Ref | Document | Owner | Issue date | Version |
|-----|---|--------|------------|---------|
| 1 | Modification Proposal P142 | ELEXON | 29/08/03 | 1.0 |
| 2 | P142 Initial Written Assessment (IWA P142) | ELEXON | 05/09/03 | 1.0 |
| 3 | Requirement Specification for Modification Proposal P142 'Revised Credit Cover methodology for Interconnector BM Units' | SSMG | 03/10/03 | 1.0 |
| 4 | Communications Requirement Document | ELEXON | 24/06/03 | 7.0 |

⁷ Positive or negative Credited Energy Indebtedness is generated by the disparity between a Party's Credit Assessment Credited Energy Volume (CAQCE) and its Account Bilateral Contract Volume (QABC). CAQCE is calculated from GC/DC and CALF values, with the former declared by the Party and the latter calculated by the BSCCo and notified to the Party at least 20 Working Days before its effective date. QABC is based upon the Party's notified contractual position.

| | | | | |
|---|--|------|----------|-----|
| 5 | Modification Proposal P142 Consultation Document (P142AC10) | SSMG | 03/11/03 | 1.0 |
|---|--|------|----------|-----|

ANNEX 1 DRAFT LEGAL TEXT

- Text for Proposed Modification is in an attached document.

ANNEX 2 MODIFICATION GROUP DETAILS

| NAME | POSITION | MEMBER |
|-----------------|-------------------------|---------------|
| Roger Salomone | Chairman | Y |
| Richard Hall | Lead Analyst | Y |
| Steve Drummond | EdF Trading Ltd | Y |
| Mark Manley | British Gas Trading | Y |
| Paul Jones | Powergen | Y |
| Mark Pearce | National Grid Company | Y |
| Sharif Islam | Total Gas & Power Ltd | Y |
| Rob Barnett | Campbell Carr | Y |
| Joanne Ellis | Cornwall Consulting Ltd | Y |
| Jerome Williams | Ofgem | N |
| Steve Mackay | Ofgem | N |
| Sanjukta Round | Cornwall Consulting Ltd | N |
| Neil Smith | Powergen | N |

ANNEX 3 CONSULTATION RESPONSES

Consultation issued on 3 November 2003.

Representations were received from the following parties:

| No. | Company | File Number | No. BSC Parties Represented | No. Non-Parties Represented |
|------------|-----------------------|--------------------|------------------------------------|------------------------------------|
| 1. | Intergen | P142_ASS_001 | 4 | 1 |
| 2. | Powergen | P142_ASS_002 | 14 | 0 |
| 3. | EDF Energy | P142_ASS_003 | 9 | 0 |
| 4. | Aquila Networks | P142_ASS_004 | 1 | 0 |
| 5. | Goldman Sachs | P142_ASS_005 | 2 | 0 |
| 6. | Scottish Power | P142_ASS_006 | 6 | 0 |
| 7. | EDF Trading | P142_ASS_007 | 2 | 0 |
| 8. | British Gas Trading | P142_ASS_008 | 1 | 0 |
| 9. | Total Gas & Power Ltd | P142_ASS_009 | 1 | 0 |
| 10. | Scottish and Southern | P142_ASS_010 | 5 | 0 |

P142_ASS_001 – Intergen

| | |
|---------------------------------------|----------------------|
| Respondent: | <i>Murray Rennie</i> |
| No. of BSC Parties Represented | <i>4</i> |

| | |
|---|--|
| BSC Parties Represented | Coryton Energy Company Limited InterGen Trading and Shipping Limited Spalding Energy Company Limited Rocksavage Power Company Limited |
| No. of Non BSC Parties Represented | 1 |
| Non BSC Parties represented | InterGen UK LTD |
| Role of Respondent | <i>Generator</i> |

| Q | Question | Response | Rationale |
|----|---|----------|--|
| 1. | Do you believe Proposed Modification P142 better facilitates the achievement of the Applicable BSC Objectives ? <i>Please give rationale and state objective(s)</i> | Yes | The proposal should enable Trading Parties to have a controlled response to Credit Default procedures and to resolve any such circumstances without being exposed to significant imbalance charges. The proposal would therefore better facilitate BSC Objective d, where costs incurred by the BSCCo are spread between BSC parties. With the insufficient liquidity and credit limitations the opportunity to trade out of Credit Default may be reduced, impacting upon BSC Objective b(iii). |
| 2. | Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? <i>Please give rationale</i> | No | |
| 3. | Do you believe there are any issues that have not been identified thus far that should be considered as part of the Assessment Procedure? <i>If yes, please give rationale</i> | No | |
| 4. | If you agree that a Level 2 default cure period should be put in place, do you believe this should end at 11:00 on the next Business Day, or should more or less time be given? <i>Please give rationale</i> | Yes | 11:00 would allow the necessary time for relevant staff members to be informed and the correct action to be taken |

| Q | Question | Response | Rationale |
|----|---|----------|---|
| 5. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should be applied to 90-100% CCP breaches where the Query Period does not overlap business hours at all, or should it also apply where the Query Period overlaps less than two business hours?</p> <p><i>Please give rationale</i></p> | | <p>The default cure period should apply to 90-100% CCP breaches where the Query Period overlaps less than two business hours. This will enable a trading party to verify their own credit calculations and if appropriate give a default query notice. The additional time will also enable additional credit to be lodged if required.</p> |

P142_ASS_002 – Powergen

| | |
|---|--|
| Respondent: | Powergen |
| No. of BSC Parties Represented | 14 |
| 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 Limited |
| No. of Non BSC Parties Represented | - |
| Non BSC Parties represented | - |
| Role of Respondent | Supplier, Generator, Trader & Exemptable Generator. |

| Q | Question | Response | Rationale |
|----|---|----------|---|
| 1. | Do you believe Proposed Modification P142 better facilitates the achievement of the Applicable BSC Objectives ? <i>Please give rationale and state objective(s)</i> | Yes | It strikes an appropriate balance between allowing parties sufficient reasonable time to lodge credit cover in the event of Level 2 Credit Default and limiting BSC Parties' credit risk. |
| 2. | Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? <i>Please give rationale</i> | No | |
| 3. | Do you believe there are any issues that have not been identified thus far that should be considered as part of the Assessment Procedure? <i>If yes, please give rationale</i> | No | |
| 4. | If you agree that a Level 2 default cure period should be put in place, do you believe this should end at 11:00 on the next Business Day, or should more or less time be given? <i>Please give rationale</i> | No | 11.00 may be too early. It may be more realistic to give participants until 12.00 noon to lodge additional credit cover. This would still give other Parties comfort in terms of protection against situations where the Party concerned is not able to raise additional funds. |

| Q | Question | Response | Rationale |
|----|---|----------|---|
| 5. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should be applied to 90-100% CCP breaches where the Query Period does not overlap business hours at all, or should it also apply where the Query Period overlaps less than two business hours?</p> <p><i>Please give rationale</i></p> | No | <p>It would appear consistent to allow participants the same minimum time to lodge additional credit cover. Therefore, these provisions should come into force where the query period overlaps with a fewer number of hours in a business day, than is allowed for in the proposed cure period. This in the context of the proposed modification would mean an overlap of 2 hours. However, we would suggest that 3 hours would be more realistic as outlined in 4 above.</p> |

P142_ASS_003 – EDF Energy

| | |
|---|--|
| Respondent: | Paul Chesterman |
| 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 | |
| Non BSC Parties represented | |
| Role of Respondent | Supplier / Generator / Party Agent / Distribution Business |

| Q | Question | Response | Rationale |
|----------|---|-----------------|------------------|
| 1. | Do you believe Proposed Modification P142 better facilitates the achievement of the Applicable BSC Objectives ? <i>Please give rationale and state objective(s)</i> | Yes | |
| 2. | Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? <i>Please give rationale</i> | No | |
| 3. | Do you believe there are any issues that have not been identified thus far that should be considered as part of the Assessment Procedure? <i>If yes, please give rationale</i> | No | |
| 4. | If you agree that a Level 2 default cure period should be put in place, do you believe this should end at 11:00 on the next Business Day, or should more or less time be given? <i>Please give rationale</i> | Yes | |

| Q | Question | Response | Rationale |
|----------|---|-----------------|--|
| 5. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should be applied to 90-100% CCP breaches where the Query Period does not overlap business hours at all, or should it also apply where the Query Period overlaps less than two business hours?</p> <p><i>Please give rationale</i></p> | Yes | <p>EDF Energy believe that all Level 2 breaches should be allowed the Level 2 default cure period, regardless of whether the Query Period contains Business Hours or not. We believe that this would give Trading Parties time to lodge extra Credit Cover on the next occurring Business Day.</p> |

P142_ASS_004 – Aquila Networks

Please find that there is no impact to Aquila Networks Plc systems and/or processes

P142_ASS_005 – Goldman Sachs

| | |
|---|--|
| Respondent: | <i>Name Sana Habib</i> |
| No. of BSC Parties Represented | <i>2</i> |
| BSC Parties Represented | <i>J Aron & Company, The European Power Source CO UK Ltd</i> |
| No. of Non BSC Parties Represented | <i>None</i> |
| Non BSC Parties represented | <i>N/A</i> |
| Role of Respondent | <i>Trader</i> |

| Q | Question | Response | Rationale |
|----------|---|-----------------|---|
| 1. | Do you believe Proposed Modification P142 better facilitates the achievement of the Applicable BSC Objectives ? <i>Please give rationale and state objective(s)</i> | No | We do not support the introduction of a Level 2 default cure period. The current Credit Cover arrangements are structured to provide protection for the market against a Party defaulting with unsecured liabilities owing to Elexon. We feel that dilution of the deterrent effect of Level 2 default removes incentives for Parties to pro-actively manage their Credit Cover and may increase the occurrence of Level 2 defaults. This modification will also increase the risk of insufficient collateral being available at the time of default and hence the risk that other Parties may receive a share of these liabilities. Both of these factors discourage effective competition in the market and therefore the modification will not better facilitate achievement of BSC Objective (c). |
| 2. | Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? <i>Please give rationale</i> | No | |
| 3. | Do you believe there are any issues that have not been identified thus far that should be considered as part of the Assessment Procedure? <i>If yes, please give rationale</i> | No | |

| Q | Question | Response | Rationale |
|----|---|----------|---|
| 4. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should end at 11:00 on the next Business Day, or should more or less time be given?</p> <p><i>Please give rationale</i></p> | | Do not agree that this should be put in place |
| 5. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should be applied to 90-100% CCP breaches where the Query Period does not overlap business hours at all, or should it also apply where the Query Period overlaps less than two business hours?</p> <p><i>Please give rationale</i></p> | | Do not agree that this should be put in place |

P142_ASS_006 – Scottish Power

| | |
|---|--|
| Respondent: | Man Kwong Liu (SAIC Ltd) |
| No. of BSC Parties Represented | 6 |
| BSC Parties Represented | Scottish Power UK plc; ScottishPower Energy Management Ltd.; ScottishPower Generation Ltd; ScottishPower Energy Retail Ltd.; SP Transmission Ltd; SP Manweb plc. |
| No. of Non BSC Parties Represented | |
| Non BSC Parties represented | |
| Role of Respondent | Supplier / Generator / Trader / Consolidator / Exemptable Generator / Party Agent |

| Q | Question | Response | Rationale |
|----------|---|-----------------|--|
| 1. | <p>Do you believe Proposed Modification P142 better facilitates the achievement of the Applicable BSC Objectives ?</p> <p><i>Please give rationale and state objective(s)</i></p> | Yes | <p>We support P142 and agree with the argument that “the need for providing protection for the market against exposure to the unpaid Trading Charges of a Party needs to be pragmatically balanced against the ability of a financially sound BSC Party to resolve Credit Default circumstances without being exposed to significant imbalance charges”. As suggested, if credit level inadvertently deteriorates over the weekend or public holidays, there needs to be adequate time and practical arrangement for a party to resolve the situation.</p> <p>P144 enables Parties who are technically and inadvertently in breach of Level 2 credit limits the opportunity to correct this breach without damage to their reputation by publication of the “default” on the BMRA website.</p> <p>We therefore agree that P142 better achieves the above and better facilitates Applicable BSC Objectives (c) and (d).</p> <p>We also support Implementation Option 3 “<i>whereby the two hours specified for the default cure period is entirely for the party to lodge credit cover</i>”, when only confirmation of fund transferred is required. i.e. funds have left the parties accounts rather than funds actually lodged at destination account, as in practice transfer of funds could take a longer period of time.</p> |

| Q | Question | Response | Rationale |
|----|---|----------|---|
| 2. | <p>Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered?</p> <p><i>Please give rationale</i></p> | No | |
| 3. | <p>Do you believe there are any issues that have not been identified thus far that should be considered as part of the Assessment Procedure?</p> <p><i>If yes, please give rationale</i></p> | No | |
| 4. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should end at 11:00 on the next Business Day, or should more or less time be given?</p> <p><i>Please give rationale</i></p> | Yes | <p>As mentioned above, this modification will remove a great deal of uncertainty over the provision of credit cover and will provide a safety net for parties who inadvertently breach Level 2 outwith banking hours. There may be a case for a longer period, due to some companies' due process. However, we accept 2 hours probably is a good compromise between practicality and credit protection.</p> |
| 5. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should be applied to 90-100% CCP breaches where the Query Period does not overlap business hours at all, or should it also apply where the Query Period overlaps less than two business hours?</p> <p><i>Please give rationale</i></p> | Yes | <p>We believe that a minimum 2 hours (banking) should be available for parties to resolve this credit default situation.</p> |

P142_ASS_007 – EDF Trading

| | |
|---|---|
| Respondent: | <i>Name 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 | Rationale |
|----------|--|-----------------|---|
| 1. | <p>Do you believe Proposed Modification P142 better facilitates the achievement of the Applicable BSC Objectives ?</p> <p><i>Please give rationale and state objective(s)</i></p> | Yes | <p>The modification does better facilitate BSC Objective (c), because it reduces incentives for the over-provision of Credit Cover and therefore reduce the opportunity cost of excessive collateral being lodged for this purpose. Furthermore .a Party breaching 90% outside business hours may be left with no alternative but to trade out of their position. This may result in the Party adopting a non-optimal trading position purely to manage their CCP, despite having Credit Cover in excess of their estimated outstanding Trading Charges, which in turn may impact upon System Buy and Sell Price.</p> |
| 2. | <p>Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered?</p> <p><i>Please give rationale</i></p> | No | |
| 3. | <p>Do you believe there are any issues that have not been identified thus far that should be considered as part of the Assessment Procedure?</p> <p><i>If yes, please give rationale</i></p> | No | |

| Q | Question | Response | Rationale |
|----|---|----------|--|
| 4. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should end at 11:00 on the next Business Day, or should more or less time be given?</p> <p><i>Please give rationale</i></p> | No | 11 am may be a bit tight, depending on the internal management structures, especially on a Monday morning and so 12 noon would be preferred. |
| 5. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should be applied to 90-100% CCP breaches where the Query Period does not overlap business hours at all, or should it also apply where the Query Period overlaps less than two business hours?</p> <p><i>Please give rationale</i></p> | No | The proposed cure period should definitely be put in place for breaches outside business hours and it would not be unreasonable to have a lead in period prior to the close of business hours, perhaps 1 hour. Consideration should be given, if this was considered acceptable, as to whether this should apply generally or only prior to weekends or holiday periods. |

P142_ASS_008 – British Gas Trading

| | |
|---|---------------------|
| Respondent: | Mark Manley |
| No. of BSC Parties Represented | 1 |
| BSC Parties Represented | British Gas Trading |
| No. of Non BSC Parties Represented | |
| Non BSC Parties represented | |
| Role of Respondent | |

| Q | Question | Response | Rationale |
|----------|---|-----------------|--|
| 1. | <p>Do you believe Proposed Modification P142 better facilitates the achievement of the Applicable BSC Objectives ?</p> <p><i>Please give rationale and state objective(s)</i></p> | Yes | <p>BGT believes that Modification Proposal P142 does better facilitate Applicable BSC Objective (c). In a specific set of circumstances the proposed solution allows a financially sound entity more options than are currently available under the existing baseline whilst not increasing the risk for BSC Parties. BGT see the 'nuclear' option of rejecting Parties contract notifications as the final step. Therefore if Parties are allowed additional time to trade out of their position or lodge additional credit this is a positive step, as it will better facilitate competition in the sale and generation of electricity.</p> <p>Within the consultation document BGT note the other perceived benefit of the proposal. The document suggests that Parties are currently obligated to post excessive levels of credit cover and this modification may remove that requirement. Whilst BGT are supportive of developments that result in Parties lodging an appropriate amount of credit cover BGT do not believe this modification will have a significant effect on BSC Parties behaviour in respect of lodging credit cover. BGT believe this modification will have a negligible impact in this area and we are therefore unconvinced that this modification may remove a perceived barrier to entry.</p> |

| Q | Question | Response | Rationale |
|----|---|----------|--|
| 2. | <p>Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered?</p> <p><i>Please give rationale</i></p> | No | |
| 3. | <p>Do you believe there are any issues that have not been identified thus far that should be considered as part of the Assessment Procedure?</p> <p><i>If yes, please give rationale</i></p> | No | |
| 4. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should end at 11:00 on the next Business Day, or should more or less time be given?</p> <p><i>Please give rationale</i></p> | Yes | <p>BGT agrees the proposed timeframe seems sensible. The 2-hour default cure period provides some additional flexibility without introducing significant new risks for BSC Parties. BGT believes 2 hours will provide sufficient time for a financially sound entity to lodge additional credit cover. BGT would not support any extension to this window.</p> |
| 5. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should be applied to 90-100% CCP breaches where the Query Period does not overlap business hours at all, or should it also apply where the Query Period overlaps less than two business hours?</p> <p><i>Please give rationale</i></p> | Yes | <p>BGT support the inclusion of a Level 2-default cure period and believe the criteria proposed to be appropriate. BGT believe the default cure period should only be valid if there is no overlap of business hours at all. BGT note the defect within the modification report, which appears to relate to problems occurring outside of business hours. This approach appears to be consistent with the defect identified in the modification proposal.</p> <p>BGT recognises that this solution potentially introduces inconsistencies however from a simplicity perspective BGT believe this option to be preferable. BGT also believe that a prudent Party that was not in financial difficulty would be aware of their increasing indebtedness and would be undertaking contingency measures to manage their credit position. If this escalation was occurring during business hours this should negate the need for the out of hours Level 2-default cure period.</p> |

P142_ASS_009 – Total Gas & Power Ltd

| | |
|---|-----------------------|
| Respondent: | Total Gas & Power Ltd |
| No. of BSC Parties Represented | 1 |
| BSC Parties Represented | Total Gas & Power Ltd |
| No. of Non BSC Parties Represented | None |
| Non BSC Parties represented | N/A |
| Role of Respondent | Trader / Supplier |

| Q | Question | Response | Rationale |
|----------|---|-----------------|---|
| 1. | <p>Do you believe Proposed Modification P142 better facilitates the achievement of the Applicable BSC Objectives ?</p> <p><i>Please give rationale and state objective(s)</i></p> | Yes | <p>Across the Industry there is substantial over provision of security for imbalance and the long-term cost of this over provision is far greater than the expected credit losses.</p> <p>This proposal allows the Industry to place pragmatic credit levels and avoid credit default consequences due to mechanistic causes.</p> <p>It will enable companies to place credit levels commensurate with their trading activities and the better valuation of this risk will promote effective competition.</p> <p>This proposal will also promote the efficiency and credibility of the balancing and settlement by filtering out spurious technical credit defaults. It would therefore meet Applicable BSC objectives (c) and (d).</p> |
| 2. | <p>Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered?</p> <p><i>Please give rationale</i></p> | No | |

| Q | Question | Response | Rationale |
|----|---|----------|--|
| 3. | <p>Do you believe there are any issues that have not been identified thus far that should be considered as part of the Assessment Procedure?</p> <p><i>If yes, please give rationale</i></p> | No | |
| 4. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should end at 11:00 on the next Business Day, or should more or less time be given?</p> <p><i>Please give rationale</i></p> | Yes | <p>A minimum of two hours available from 09:00 hrs would enable sufficient levels of staffing and bank time to be made available to rectify the breach.</p> |
| 5. | <p>If you agree that a Level 2 default cure period should be put in place, do you believe this should be applied to 90-100% CCP breaches where the Query Period does not overlap business hours at all, or should it also apply where the Query Period overlaps less than two business hours?</p> <p><i>Please give rationale</i></p> | Yes | <p>The purpose of the modification proposal is to allow those parties who inadvertently breach 90%, and remain below 100% of their CCP, an opportunity to rectify the situation by utilising a default cure period once business hours become available. Should the relevant query period expire very soon after the start of business hours such a party would appear to be treated less equitably than a party whose period expired before this time. To ensure that the default cure period is equitable in its application TG&P recommend that the Default Cure period also apply to these breaches.</p> |

P142_ASS_010 – Scottish and Southern

| | |
|---|---|
| Respondent: | Scottish and Southern |
| No. of BSC Parties Represented | 5 |
| BSC Parties Represented | Scottish and Southern Energy, Southern Electric, Keadby Generation Ltd., SSE Energy Supply Ltd. and Medway Power Ltd. |
| No. of Non BSC Parties Represented | None |
| Non BSC Parties represented | N/A |
| Role of Respondent | |

| Q | Question | Response | Rationale |
|----------|--|-----------------|---|
| 1. | <p>Do you believe Proposed Modification P142 better facilitates the achievement of the Applicable BSC Objectives ?</p> <p><i>Please give rationale and state objective(s)</i></p> | No | <p>We do not believe that by allowing the default cure period to last until two hours into the next Business Day that this will better achieve the applicable BSC Objectives. In our view all that will happen is that the risk that the market is exposed to (from the Party in the Level 2 situation) will be extended by two hours into the next Business Day. Parties need to actively manage their risk position in order to minimise (a) their exposure and (b) their cost of credit cover. Allowing Level 2</p> <p>Parties a two hour 'grace' period will not incentives those Parties to manage their risk position and therefore cannot be said to better achieve the applicable BSC Objectives.</p> |
| 2. | <p>Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered?</p> <p><i>Please give rationale</i></p> | No | |
| 3. | <p>Do you believe there are any issues that have not been identified thus far that should be considered as part of the Assessment Procedure?</p> <p><i>If yes, please give rationale</i></p> | No | |

| Q | Question | Response | Rationale |
|----|--|----------|--|
| 4. | If you agree that a Level 2 default cure period should be put in place, do you believe this should end at 11:00 on the next Business Day, or should more or less time be given? <i>Please give rationale</i> | Yes | As noted in our response to Q1 above, we do not believe that a default cure period should be put in place, and therefore we certainly do not support this being 'extended' beyond 8am, let alone 11am. |
| 5. | If you agree that a Level 2 default cure period should be put in place, do you believe this should be applied to 90-100% CCP breaches where the Query Period does not overlap business hours at all, or should it also apply where the Query Period overlaps less than two business hours? <i>Please give rationale</i> | Yes | As noted in our response to Q1 above, we do not believe that a default cure period should be put in place. |

ANNEX 4 TRANSMISSION COMPANY ANALYSIS

| Q | Question | Response |
|---|--|---|
| 1 | Please outline any impact of the Proposed Modification (and, if applicable, any Alternative Modification) on the ability of the Transmission Company to discharge its obligations efficiently under the Transmission Licence and on its ability to operate an efficient, economical and co-ordinated transmission system. | We do not believe that the proposed modification has any impact on our ability to discharge our obligations under the Transmission Licence. |
| 2 | Please outline the views and rationale of the Transmission Company as to whether the Proposed Modification (and, if applicable, any Alternative Modification) would better facilitate achievement of the Applicable BSC Objectives. | Whilst we note the objectives of the proposal to provide for a more efficient and pragmatic approach to credit provisions, we would support the views of the SSMG that this needs to be assessed against the potential costs of implementing the modification. We feel that at this stage in the assessment process we are unable to comment on whether the proposal meets the BSC Applicable Objectives. Further information needs to be provided of the full impact on party systems and processes for lodging credit arising from the solution option that is chosen before we can express a final view. |
| 3 | Please outline the impact of the Proposed Modification (and, if applicable, any Alternative Modification) on the computer systems and processes of the Transmission Company, including details of any changes to such systems and processes that would be required as a result of the implementation of the Proposed Modification (and, if applicable, any Alternative Modification) | None identified. |
| 4 | Please provide an estimate of the development, capital and operating costs | None identified. |

| | | |
|---|--|----------------------|
| | (broken down in reasonable detail) which the Transmission Company anticipates that it would incur in, and as a result of, implementing the Proposed Modification (and, if applicable, any Alternative Modification). | |
| 5 | Please provide details of any consequential changes to Core Industry Documents that would be required as a result of the implementation of the Proposed Modification (and, if applicable, any Alternative Modification). | None identified. |
| 6 | Any other comments on the Proposed Modification (and Alternative Modification if applicable). | No further comments. |

ANNEX 5 BSC AGENT IMPACT ASSESSMENTS

Please see the attached documents provided by the NETA CSA and the FAA.

ANNEX 6 PARTY IMPACT ASSESSMENTS

| Organisation | Comments |
|--|---|
| Sue Macklin Scottish and Southern Energy; Southern Electric; Keadby Generation Ltd; and SSE Energy Supply Ltd. | <p>What impact, if any, will the Modification have on your organisation?</p> <p>We need to make minor changes to processes to recognise the additional time available to post funds to resolve the default.</p> <p>What implementation timescale, if applicable, would your organisation require to implement the changes associated with the Modification?</p> <p>1 week</p> <p>What costs, if any, would your organisation incur to implement the changes associated with the Modification?</p> <p>Minimal costs</p> |
| Roslyn Bucknall Npower Ltd, Npower Direct Ltd, Npower Yorkshire Ltd, Npower Yorkshire Supply Ltd | <p>What impact, if any, will the Modification have on your organisation?</p> <p>None.</p> <p>What implementation timescale, if applicable, would your organisation require to implement the changes associated with the Modification?</p> <p>N/A</p> <p>What costs, if any, would your organisation incur to implement the changes associated with the Modification?</p> <p>None.</p> |
| Margaret Brunton Npower Northern Ltd, Npower Northern Supply Ltd | <p>What impact, if any, will the Modification have on your organisation?</p> <p>None.</p> <p>What implementation timescale, if applicable, would your organisation require to implement the changes associated with the</p> |

| | |
|--|---|
| | <p>Modification?</p> <p>N/A</p> <p>What costs, if any, would your organisation incur to implement the changes associated with the Modification?</p> <p>None.</p> |
| <p>John W Russell Scottish Power UK plc ScottishPower Energy Management Ltd. ScottishPower Generation Ltd. ScottishPower Energy Retail Ltd. SP Manweb plc. SP Transmission Ltd</p> | <p>What impact, if any, will the Modification have on your organisation? ScottishPower support option 3 "whereby the two hours specified for the default cure period is entirely for the party to lodge credit cover". - Our least favoured option is 2. Whilst not impacting current practises (as our systems are sufficiently robust), this modification will remove a great deal of uncertainty over the provision of credit cover and will provide a safety net for parties who inadvertently breach Level 2 outwith banking hours.</p> <p>What implementation timescale, if applicable, would your organisation require to implement the changes associated with the Modification? The Implementation could be immediate.</p> <p>What costs, if any, would your organisation incur to implement the changes associated with the Modification? As stated above; No costs would be incurred.</p> <p>If the Modification is not applicable to your organisation, please indicate why. As stated above; the Modification is applicable</p> <p>Any other comments: ScottishPower strongly support the introduction of this Modification which enables Parties who are technically and inadvertently in breach of Level 2 credit limits the opportunity to correct this breach without damage to their reputation by publication of the "default" on the BMRA website.</p> |
| <p>Rachael Gardener Aquila Networks</p> | <p>No impact</p> |
| <p>Dave Morton EDF Energy Supply</p> | <p>What impact, if any, will the Modification have on your organisation?</p> <p>None.</p> <p>What implementation timescale, if applicable, would your organisation require to implement the changes associated with the Modification?</p> <p>None.</p> <p>What costs, if any, would your organisation incur to implement the changes associated with the Modification?</p> <p>None.</p> |

ANNEX 7 TERMS OF REFERENCE

- whether P142 would impact the number and type of 90% CCP breaches;
- If P142 will impact whether a Party chooses to actively manage its CCP position;

- whether P142 would increase the complexity of Section M provisions whilst decreasing the deterrent of Level 2 Credit Default;
- whether Parties should be allowed a default cure period to rectify instances of 90% CCP breaches in addition to their ongoing right to manage their positions so that they do not breach 90% CCP;
- whether changes will be required to the authorisation notice (pursuant to Section M3.4) in order to separate the application of Level 1 and Level 2 Credit Default conditions;
- the need to conduct a full impact assessment on BSC Agent systems and documents. In particular, to determine whether a manual solution to implementing P142 would be possible or if ECVAA system changes will be required;
- if there would be a need to change ECVAA and BMRA software, as well as the scope and likely cost of such changes;
- the need to conduct a full impact assessment on FAA systems and documents, in particular to determine whether the FAA/ECVAA interface can implement changes to Credit Cover within prescribed timescales;
- the need to establish whether the two hour period should be applied purely to payments through specified mechanisms; and
- how the Modification Proposal would affect Parties going into Level 2 Credit Default overnight or over the weekend.