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23 December 2003

The National Grid Company, BSC Signatories and
Other Interested Parties

Our Ref: MP No P141

Dear Colleague,

Modification to the Balancing and Settlement Code (“BSC”) - Decision and Notice in relation to Modification Proposal P141: “Removal of Unintentional Effects of Approved Modification P106 on Supplier Charges”

The Gas and Electricity Markets Authority (the “Authority”)¹ has carefully considered the issues raised in the Modification Report² in respect of Modification Proposal P141, “Removal of Unintentional Effects of Approved Modification P106 on Supplier Charges”.

The BSC Panel (the “Panel”) recommended to the Authority that Proposed Modification P141 should be made and that the implementation date should be backdated to 24 June 2003.

Having carefully considered the Modification Report, the Panel’s recommendation and having regard to the Applicable BSC Objectives in addition to the Authority’s wider statutory duties,³ the Authority has decided to direct a Modification to the BSC in line with Modification Proposal P141.

This letter explains the background and sets out the Authority’s reasons for its decision. In addition, the letter contains a direction to The National Grid Company plc (“NGC”) to modify the BSC in line with Modification Proposal P141, as set out in the Modification Report.

This letter constitutes notice by the Authority under section 49A Electricity Act 1989 in relation to the direction.

¹ Ofgem is the office of the Authority. The terms “Ofgem” and the “Authority” are used interchangeably in this letter.

² ELEXON document reference P141RR, Version No. 2.0, dated 17 November 2003.

³ Ofgem’s statutory duties are wider than the matters that the Panel must take into consideration and include amongst other things a duty to have regard to social and environmental guidance provided to Ofgem by the government.

Background

Under the Pooling and Settlement Arrangements (P&SA) a four character code, known as a Supplier ID, was used to uniquely identify a single supplier within a number of IT systems. The Supplier ID continues to be used within IT Systems such as the Performance Assurance Reporting and Monitoring System (PARMS) under the governance of the Balancing and Settlement Code (the Code). As a result of various company acquisitions, some following Defaults by Suppliers, the Supplier ID became an asset that identified groups of customers that were transferred from one company to another. This was seen as the most efficient mechanism of transferring such volumes of customers without having to undergo a Change of Supplier Process.

P106 "Amendment to the BSC to allow multiple Supplier IDs" sought to formally introduce the term Supplier ID into the Code for the purposes of settlement upon its implementation on 24 June 2003. The P106 legal text stated that all provisions in the Code apply with respect to a Supplier unless they are referred to in S1.3.4 in which case they apply separately to each Supplier ID. Following the P106 implementation date the Code is unambiguous that wherever the term Supplier is used it should not refer to Supplier IDs which are a subdivision of a Supplier's customer base. Section 1.3.4 does not reference Serials or Supplier Charges.

If left unchanged P106 will have several effects on the way in which Serials & Standards are reported and monitored, and Supplier Charges are levied, from being on a Supplier ID level to being on a Supplier basis. These include:

- The need to develop a revised PARMS to deal with the data from 24 June 2003.
- A possible requirement for a subsequent Modification Proposal to be brought to fully define how to apply the Supplier Charges cap, which was complicated by the implementation of P106 part way through a PARMS reporting month.
- Until a new PARMS system could be developed no monitoring of Serials or validation of submitted data would occur. This may result in Serial 10⁴ charges being incurred by parties. If a validation failure was to occur Parties would not become aware of this for a considerable amount of time and may have to resubmit the correct data at a later date.
- A need to change Party Agent systems to enable them to identify which Party ID corresponds to a particular Supplier ID.

At its meeting on 14 August the Panel suggested that a party may wish to raise a Modification Proposal in order to address these potential complications. EDF Energy submitted Modification Proposal P141, "Removal of Unintentional Effects of Approved Modification P106 on Supplier Charges" on 28 August 2003.

⁴ Serial 10 places an obligation on Suppliers to arrange the delivery of routine Performance Monitoring Reports to the Performance Assurance Board, by not later than 20 Business Days after the end of each month. This obligation is replaced on 1 May 2004 by Serial SP01.

The Panel considered the Initial Written Assessment at its meeting of 11 September 2003 and agreed to submit Modification Proposal P141 to the Assessment Procedure to be undertaken by the Volume Allocation Standing Modification Group (VASMGM). The VASMGM (the "Group") considered the Initial Written Assessment in its meeting on 18 September 2003 and a consultation document was issued with responses requested by 26 September 2003. These were discussed at the second VASMGM meeting on 30 September 2003. The Panel met on 9 October 2003 to consider the Assessment Report and the recommendations of the VASMGM. Responses to the Report Phase Consultations were requested by 21 October 2003. The Panel convened again on 13 November 2003 and in this meeting considered the contents of the Draft Modification Report and its provisional recommendations to the Authority.

The Modification Proposal

Modification Proposal P141 seeks to modify the BSC so as to redress the unintentional effects of Modification P106 which centre on a requirement to report on a Supplier basis rather than at Supplier ID level. It also intends to rectify the inconsistencies this caused with other provisions in Section S of the Code. The proposal suggests that, in order to completely redress the effect of P106 on the way in which Serials and Supplier Charges are administered, it is necessary to backdate the implementation of P141 to 24 June 2003 on the grounds that this would prevent systems having to be developed to cope with the P106 rules for a limited period. The Proposer considers that by ensuring the provision and reporting of data is carried out in a consistent manner unintended charges and associated costs will be avoided. The Proposal suggests that these changes will promote efficiency in the implementation and administration of the balancing and settlement arrangements and better facilitate Applicable BSC Objective⁵ C3 (3) (d).

The majority view of the VASMGM agreed with this assessment. It considered that the implementation and administration of the Balancing and Settlement arrangements would be better facilitated by ensuring that the process by which Serials and Standards are reported and monitored, and Supplier Charges are levied, remains on the basis of Supplier IDs rather than on a Supplier basis. Furthermore the Group considered that Modification Proposal P141 would decrease costs to the industry, as choosing not to implement the modification would require a new PARS system to be developed which would support a change in reporting to a Supplier rather than a Supplier ID basis.

⁵ The Applicable BSC Objectives, as contained in Standard Condition C3 (3) of National Grid Company's ("NGC's") Transmission Licence, are:

- a) the efficient discharge by the licensee of the obligations imposed upon it by this licence;
- b) the efficient, economic and co-ordinated operation by the licensee of the licensee's 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) 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.

One member of the Group felt that P141 would not better facilitate the achievement of the Applicable BSC Objectives on the grounds that P141 leaves a problem regarding the interpretation and application of Serials and Supplier Charges prior to the P106 implementation date. The same member also considered that the Proposed Modification may detract from applicable BSC Objective (c) since it would set Standards separately in relation to parts of certain Suppliers' demand in a GSP Group, which would act as an additional requirement or constraint on their performance or actions.

No Alternative Modification was developed, although there were discussions over a potential alternative with a purely prospective implementation date which, it was suggested, would solve the perceived defect in P141. The majority of the Group felt that a purely prospective modification would not facilitate the achievement of the Applicable BSC Objectives as efficiently as the Proposed Modification. In particular, it was considered that reporting at a Supplier level would have to be implemented for the interim period, thus not completely resolving the claimed unintended effects of P106.

A minority felt that the defect pointed out in relation to the Proposed Modification could be solved by making P141 purely prospective. In this case Supplier Charges for the period between P106 implementation and P141 implementation would need to be suspended (which it was acknowledged requires a degree of retrospection). The majority of the Group did not agree that this solution would better facilitate the achievement of the Applicable BSC Objectives and as a result an Alternative Modification was not developed.

ELEXON requested responses to the Report Phase Consultations by 21 October 2003.

Respondents' views

ELEXON received 5 (five) responses to the consultation on Modification Proposal P141. All 5 Responses (representing 42 (forty-two) Parties and 0 (zero) non-Parties) expressed support for the Proposed Modification.

P141 was considered to be a pragmatic solution to avoid unintentional side effects from the implementation of P106. The modification would ensure that PARMS will continue to run according to its current functionality, namely the application of Supplier Charges on a Supplier ID basis. One respondent added that it would also ensure that Party Agents did not have to worry about changes where Supplier consolidation takes place. One party based its support for the Proposed Modification on the implementation date being backdated to 24 June 2003.

A majority of respondents agreed that the legal text provided correctly addressed the defect outlined by P141. One of these respondents qualified its support as it believed the legal drafting may need to address the treatment of non compliance with obligations which have been retrospectively changed. One respondent had no comment.

Three respondents supported the Panel's provisional recommendation regarding an Implementation Date backdated to 24 June 2003. Two respondents did not. One of these qualified their lack of support with the proviso that it could be accepted on the basis that Parties would not be pursued for the consequences of actions taken on the basis of obligations that

were changed retrospectively. The other respondent did not support retrospective changes in general.

Several other comments were made by three respondents. One felt that a retrospective change was unnecessary since there has been no impact to date and a prospective change should have been considered further. Another respondent presented the view that P106 did not in fact change the basis on which Serials should be submitted since the Code has precedence over Code Subsidiary Documents. This respondent did however recognise that P106 changed the basis on which Supplier Charges were calculated centrally by BSCCo and that this was the unintentional error that is addressed by P141. One respondent did not think that it was clear that P106 intended Annex S-1 to apply on a Supplier ID basis and is concerned at P141 changing obligations and liabilities retrospectively.

The respondents' views are summarised in the Modification Report for Modification Proposal P141, which also includes the complete text of all respondents' replies.

Panel's recommendation

The Panel met on 13 November 2003 to consider Modification Proposal P141, the draft Modification Report, the views of the VASMG and the consultation responses received.

The Panel recommended that the Authority should approve Proposed Modification P141 with an Implementation Date backdated to 24 June 2003.

Ofgem's view

Having carefully considered the Modification Report and the Panel's recommendation, Ofgem considers, having regard to the Applicable BSC Objectives and its statutory duties, that Modification Proposal P141 will better facilitate achievement of Applicable BSC Objective (d).

The method for calculating Supplier Charges is defined in Annex S-1 of the Code. These provisions were not included among those stated as applying on a Supplier ID basis and the effect of P106 was to enunciate that Supplier Charges should be calculated on a Supplier basis. The clear definition of which provisions should apply on a Supplier ID basis meant that, following the implementation of P106, Supplier Charges could not be calculated in this way. Instead, the calculations would need to be altered to process Supplier Charges on a Supplier basis.

Ofgem notes that the majority of respondents to the VASMG's consultation considered that P141 would better facilitate Applicable BSC Objective (d). The Authority also notes that the majority of respondents had not anticipated any effects on Supplier Charges caused by P106 and that the majority view of the VASMG was that the effects of P106 were, as suggested in the Modification Proposal, unintentional. Further, Ofgem notes that none of the respondents to the consultation had taken any material action to change their systems or processes to report data for Supplier Charges on a Supplier basis.

Were P141 not implemented, Supplier Charges would need to be calculated on a Supplier basis from 24 June 2003. In addition the existing PARMS system would not be capable of delivering Supplier Charges calculations under P106 and so a new system, with its associated costs, would be required. The Authority is mindful of the fact that a new PARMS system is currently being procured by Elexon to monitor new serials to be introduced by Approved Modification P99. However Ofgem also notes that the scope of this system would need to be increased to accommodate processing Supplier Charges under P106. This would clearly have further associated costs for development. In addition, the systems and processes of market participants would need to be revised to accommodate the requirements of P106 on submitting data on a Supplier basis.

In order to achieve its intended effect, the implementation date of P141 must be retrospective in nature. As stated in Ofgem's decision letter for Modification Proposal P19, the Authority is, in general, opposed to approving modifications which have retrospective effects. Whilst this is the case Ofgem considers that there may be a small number of circumstances that could give rise to the need for a modification with retrospective effect. As stated in the P19 decision letter, Ofgem believes that it is appropriate to consider any retrospective modifications on a case by case basis.

In the case of P141 the following points are significant in considering the retrospective effects of the Modification Proposal:

First, as previously stated, none of the respondents to the consultation issued by the VASMG have taken any material action to implement P106. Approval of P141 with retrospective effect would therefore not disadvantage parties as none have taken steps and incurred costs to alter their processes.

Second, Ofgem notes that the processing of Supplier Charges under the BSC commenced in February 2003. This processing began levying Supplier Charges from April 2001 and is currently being run at an accelerated rate to 'catch up' so that they can be processed on a monthly basis during the calendar month following the reporting month. This catch up process means that Supplier Charges for dates following the implementation of P106 on 24 June 2003 have not yet been calculated and so there would be no re-running of charges should P141 be implemented.

It is stated in the Modification Report that the effects of P106 on Supplier Charges can only be removed completely, thereby avoiding the additional costs to process and systems changes, if P141 is approved with a retrospective implementation date. In addition, the possible requirement for a retrospective implementation date was highlighted to BSC Parties in the Initial Written Assessment. The Group and the Panel therefore were able to consider the implications of retrospective implementation in detail throughout the modification process.

Ofgem agrees with the Panel's recommendation that Modification P141 should be approved. In coming to this decision, Ofgem has considered that the effects of P106 on Supplier Charges, as determined by the majority of industry respondents, were unintentional, that no BSC party has initiated changes to reflect the effects of P106 and that there would be a significant impact and cost, with no clear benefit, for Elexon and BSC parties to modify systems and processes to enable processing of Supplier Charges in accordance with P106.

Ofgem considers that, in the case of Modification Proposal P141, a retrospective implementation date of 24 June 2003 is acceptable in order to facilitate the applicable BSC Objectives.

The Authority's decision

The Authority has therefore decided to direct that the Proposed Modification P141, as set out in the Modification Report, should be made and implemented.

Direction under Condition C3 (5) (a) of NGC's Transmission Licence

Having regard to the above, the Authority, in accordance with Condition C3 (5) (a) of the licence to transmit electricity granted to NGC under Section 6 of the Electricity Act 1989 as amended (the "Transmission Licence"), hereby directs NGC to modify the BSC as set out in the Modification Report.

The Implementation Date for Modification Proposal P141 is one of retrospective application and is to be considered as having been in force since 24 June 2003.

In accordance with Condition C3 (5) (b) of NGC's Transmission Licence, NGC shall modify the BSC in accordance with this direction of the Authority.

If you have any questions, please contact me on the above number.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'N. Simpson', written over a horizontal line.

Nick Simpson

Director of Industry Code Development

Signed on behalf of the Authority and authorised for that purpose by the Authority