

Phase

Initial Written Assessment

Definition Procedure

Assessment Procedure

Report Phase

Implementation

P362 'Introducing BSC arrangements to facilitate an electricity market sandbox'

This Modification proposes to enable Parties to be derogated from specific obligations in the Balancing and Settlement Code to enable pre-competitive and innovative products and services to be tested in the live environment for a limited period of time.

This Assessment Procedure Consultation for P362 closes:

5pm on 12 April 2018

The Workgroup may not be able to consider late responses.



The P362 Workgroup initially recommends **approval** of P362

This Modification is expected to impact:

- BSC Parties
- Party Agents
- BSC Panel
- Transmission Company
- Ofgem
- Non-BSC Parties
- ELEXON



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About This Document

The purpose of this P362 Assessment Procedure Consultation is to invite BSC Parties and other interested parties to provide their views on the merits of P362. The P362 Workgroup will then discuss the consultation responses, before making a recommendation to the BSC Panel at its meeting on **10 May 2018** on whether or not to approve P362.

There are five parts to this document:

- This is the main document. It provides details of the solution, impacts, costs, benefits/drawbacks and proposed implementation approach. It also summarises the Workgroup's key views on the areas set by the Panel in its Terms of Reference, and contains details of the Workgroup's membership and full Terms of Reference.
- Attachment A contains the draft redlined changes to the BSC for P362.
- Attachment B contains the specific questions on which the Workgroup seeks your views. Please use this form to provide your response to these questions, and to record any further views or comments you wish the Workgroup to consider.
- Attachment C contains the P362 business requirements.
- Attachment D contains the draft BSC subsidiary document for P362.
- Attachment E contains a high-level end to end process map.

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Why Change?

Appropriate provisions do not currently exist within the Balancing and Settlement Code (BSC) to enable pre-competitive or proof of concept testing for innovative products or services in the live BSC Settlement environment. The absence of an arrangement to facilitate such testing hinders the development and trialling of innovations within the electricity market. Therefore the current arrangements act as a barrier to innovation and competition.

Solution

P362 seeks to enable BSC Parties to be derogated against specific BSC obligations in order to trial pre-competitive and innovative products and services. Ofgem will act as the point of entry to co-ordinate applications across the industry. This is designed to improve the customer experience and reduce the burden for applicants, particularly where applications require derogation from more than one industry code.

ELEXON will receive applications via Ofgem and prepare relevant information for the Panel's consideration. The Panel will make a recommendation to Ofgem whether to approve or reject the derogation. Ofgem will decide whether to grant the derogation and synchronise derogations across the impacted codes and licences. Anyone can apply for derogation, but non-Parties will be required to accede to the Code and complete the relevant market entry processes before the derogation can be effective.

Impacts & Costs

P362 is a document only change that will directly impact the BSC Panel, Ofgem and ELEXON. They will need to implement new processes and products to operate the sandbox service. P362 will indirectly impact (no implementation effort) BSC Parties, non-BSC Parties and Party Agents who may choose to participate in the sandbox.

Implementation

P362 is proposed for implementation five Working Days after approval, as a standalone BSC Release.

Recommendation

The majority of the Workgroup believes that P362 **would** overall better facilitate the Applicable BSC Objectives and so should be **approved**.

The **majority** of the Workgroup initially believes that P362 **would better facilitate** Applicable BSC Objectives **(c)** compared to the current baseline, and so should be approved.

The **minority** of Workgroup members were **positive** against Applicable BSC Objective (d), and the remaining Workgroup members were neutral.

Background

The industry is experiencing levels of change not seen since privatisation. These changes are many and varied, originating from consumers and prosumers, from existing or new market entrants, from European or Government policy, or from technology and data driven solutions. In all cases ELEXON is determined to do what it can to ensure the BSC is not a barrier to innovation and change.

The Panel, at its meeting on 12 October 2017, noted that the BSC does not have an electricity market sandbox or derogation process ([Panel Paper 271/04](#)). ELEXON believes the absence of an electricity market sandbox and process hinders the development and trialling of innovations within the electricity market.

ELEXON recommended to the Panel, at its meeting on 9 November 2017, that P362 should be raised to introduce a sandbox and derogation process into the BSC. The Panel agreed and raised P362 at this meeting (in accordance with BSC Section F2.1.1(d)).

Existing sandboxes

Ofgem

Ofgem launched its [Innovation Link](#) in December 2016. It provides fast, frank feedback to help innovators understand the regulatory implications of their business propositions. As part of this initiative, Ofgem have established a [regulatory sandbox](#).

Currently, Ofgem's regulatory sandbox does not extend to the BSC. However, in January 2018, Ofgem agreed to co-ordinate sandbox applications, including working with ELEXON and other interested Code Administrators¹ to:

- Develop a single point of entry for applicants;
- Operate a sifting process ahead of applications being forwarded to relevant code administrators; and
- Coordinate the feedback process on early, valid application.

In its latest [sandbox application round](#) on 2 October 2017, Ofgem called for other industry bodies to adopt sandbox approaches to removing barriers.

Ofgem's regulatory sandbox has four eligibility criteria (innovation, consumer benefit, background research, and need for support). From its first sandbox round, Ofgem is currently in discussions with four innovators to grant regulatory sandbox access. The ideas put forward include peer-to-peer local energy trading platforms and trialling an innovative tariff supported by smart home technology.

Financial Conduct Authority (FCA)

Additionally, the FCA started operating a Regulatory sandbox in June 2016. The FCA have found after the first year of operating their sandbox that it has reduced time and cost of getting innovations to market and helped facilitate access to finance. The FCA's sandbox



What is a sandbox?

A sandbox is a term most often used in software development or computer security management.

For example, it may refer to a testing environment that isolates untested code changes and outright experimentation from the production environment or repository. In computer security, a sandbox is a security mechanism for separating running programs, usually in an effort to mitigate system failures or software vulnerabilities from spreading.

However, in a regulatory or code environment it means a time limited exemption or derogation from particular rules or obligations to achieve specific aims, subject to given criteria and process.

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¹ At the time of consultation Ofgem is working with a number of Code Administrators, including ELEXON, to develop a cross-code sandbox process. There is not currently a date by when this work should be complete.

offers guarantees of non-enforcement in place of derogations, and restricted authorisation in place of reduced market access requirements (which could be a type of requested derogation).

Existing BSC derogations

Whilst all BSC Parties must comply with the BSC, currently some obligations may be waived or met in a different way than that envisaged by the BSC. For example, the Metering Dispensation process, detailed in [Section L](#) of the BSC, allows Registrants of Metering Systems to apply for a Metering Dispensation if the associated Metering Equipment will not or does not comply with the applicable [Code of Practice](#) (a BSC Code Subsidiary Document). If granted, the Metering Dispensation allows the Registrant to deviate from the requirements in the relevant Code of Practice.

Similarly, where a Party wishes to register a Balancing Mechanism (BM) Unit that does not meet the conditions required by BSC Section K, the responsible Party can apply to the Panel (delegated to the Imbalance Settlement Group (ISG)) for an exemption from these conditions. This type of BM Unit application is referred to as a non-standard BM Unit application. Where granted, it allows the Party to derogate from the Standard BM Unit requirements.

What is the issue?

Under the current BSC framework, provisions do not exist to enable pre-competitive or proof of concept testing for innovative products/business models in the live BSC Settlement environment.

The current BSC arrangements can pose a barrier to innovative business ideas. The BSC rules are necessary for the robust operation of balancing and Settlement across the Total System. In order for the BSC to be enforced fairly to all Parties, all Parties are required to comply with the rules. However, small projects with little or no impact on Settlement might find the full BSC uneconomic to comply with for a proof of concept trial.

Currently, the only option open to participants, looking to test new ways of doing things under the BSC, is to raise a BSC Modification (with the exception of the limited derogation options already facilitated within the BSC arrangements, such as the Metering Dispensations and non-standard BM Unit applications processes).

Progressing Modifications would likely be more resource intensive for both industry and ELEXON given the prescribed BSC Change process and associated governance. The BSC Change Process was not designed for the trialling of new products or business ideas. These governance constraints limit the ability to trial in the live environment and evaluate the benefits that innovative projects may deliver. For the avoidance of doubt, the issue is not the current BSC Change process, which should remain unchanged and unaffected by this Modification.

Increasingly, market participants that have not acceded to the BSC arrangements wish to have the ability to test new ways of working to allow them to establish whether it is economically viable and efficient for them to become a full part of the BSC framework. ELEXON have already been approached by companies interested in electric vehicle charging solutions, peer to peer trading platforms and local community energy schemes to discuss how their projects interact with and could be accommodated by the BSC.

The BSC should be able to accommodate the trialling of innovative concepts and technological advances that could subsequently be incorporated into the BSC framework. A

new process is needed so that an individual BSC Party, class of Party, or non-BSC party can be exempted from specific BSC obligations to trial innovative products or ideas to test or prove the new product or idea for a fixed period of time.

Proposed solution

P362 '[Introducing BSC arrangements to facilitate an electricity market sandbox](#)' seeks to provide Parties with:

- The ability to test products and services in the live market;
- Reduced time to market at potentially lower cost; and
- Support in identifying and implementing new arrangements that can better facilitate the Applicable BSC Objectives.

P362 aims to enable industry participants, that have pre-competitive innovative products or services that are facing barriers to entry, to have the ability to be derogated from relevant obligations, in order to test and develop the product or service. Derogation will be subject to eligibility criteria being met.

Sandbox projects will be required to demonstrate how they will better facilitate the Applicable BSC Objectives. They are expected to be conducted on a small scale and for a limited duration. They should not have an adverse impact or pose a significant risk to Settlement or Parties.

P362 introduces a number of new defined terms, which can be found in the draft BSC legal text in Section Annex X-1 in Attachment A.

High level end-to-end process

In order to request derogation, applicants will submit an application to Ofgem, who will assess and evaluate the application against its eligibility criteria (innovation, consumer benefit, background research, and need for support). Those applications that meet the criteria will be passed to participating Code Administrators for assessment. Code Administrator will confirm if its respective code is impacted. If it is impacted, the Code Administrator will follow its own sandbox process (where available) to provide a recommendation to Ofgem on whether to grant derogation and any associated conditions. Ofgem will decide whether to derogate from the relevant codes and licences, and if so the conditions for that derogation. Where Ofgem want to amend the conditions, they will send the application back to the Panel for re-evaluation.

Attachment E contains a high-level process map for the proposed solution.

Role of the applicant and Derogated Party

Before the application is progressed by ELEXON, the applicant will be required to provide key information. For example, the proposed BSC obligations they seek derogation from, the Derogation Period, reporting and monitoring considerations and a Transition Plan.

The Transition Plan should provide a timeline of key activities needed to exit the sandbox. This plan is expected to be triggered following the agreed Trial Period. However, it may be triggered at any time due to project issues, failure or non-compliance.

The applicant may be asked to pay an application fee, set by the Panel from time to time. However, it is expected this fee will initially be set at zero. The applicant may also be asked to pay certain costs associated with the derogation, such as paying for additional

ELEXON resources or compliance checks. These will be agreed as part of the application process.

If Ofgem approve the application and derogate the Party they will become a 'Derogated Party'. The Derogated Party will be expected to provide updates throughout the Derogation Period, as agreed upfront. The updates will feed into a lessons learned report for that particular project.

Role of ELEXON and the BSC Panel

ELEXON will conduct an evaluation of the application received from Ofgem. The evaluation will be submitted to the Panel in a 'Sandbox Report', which will form the basis for the Panel recommending to Ofgem whether to derogate or not. ELEXON must evaluate:

- The risks and impacts;
- The 'Sandbox Eligibility Criteria';
- The sections of the Code that need to be derogated;
- The length of the derogated period; and
- The applicant's Derogation Period.

The Panel shall consider the Sandbox Report and determine whether to recommend to Ofgem:

- That the proposed derogation be granted or rejected;
- What, if any conditions should be set for the proposed derogation; and
- That the Derogation Period and the Transition Plan be approved or amended.

In making its recommendation the Panel will consider, as they do for BSC Modifications, whether the derogation would better facilitate the Applicable BSC Objectives. They will also consider the scope of the derogation and a number of further criteria detailed in a BSC subsidiary document.

Sandbox eligibility criteria

In assessing the derogation, ELEXON and the Panel will consider the impact and potential risk to Settlement and Parties. ELEXON will issue an impact assessment to industry for between 10 and 15 Working Days. Responses will be considered and included in the Sandbox Report and published on the BSC website. Other criteria that the Panel must consider are:

- The risks that granting the derogation poses to Settlement;
- The impact on other BSC Parties of granting the derogation;
- Whether the derogation request has reasonably assessed the minimum scope and timeline required to effectively trial the project;
- Whether the derogation being requested is materially similar to a derogation which is currently in force; and
- The impact of any imminent changes to the BSC.

Derogation conditions

The Panel may recommend to Ofgem conditions it believes are appropriate. These conditions will constrain the scope of the derogation to limit its impact and mitigate risks. Typically these will include:

- The total number of customers/ Metering System Identifiers (MSIDs) involved in the trial;
- The geographical area of the trial (e.g. single Grid Supply Point (GSP), single feeder, single site);
- The Meter classes that can be engaged in the trial;
- The total average consumption/generation of the MSIDs involved in the trial; and
- Any other parameters relevant to the derogation being requested.

Amendments to derogations

The Panel will also be able to recommend to Ofgem that derogations are amended or removed, following a similar approach taken for the original recommendation.

The Derogation Period

Derogations will be granted for two distinct periods: a 'Trial Period' and a 'Transition Period'. Together they will be known as the 'Derogation Period'. Diagram 1 below shows the Derogation Period timeline and limits.

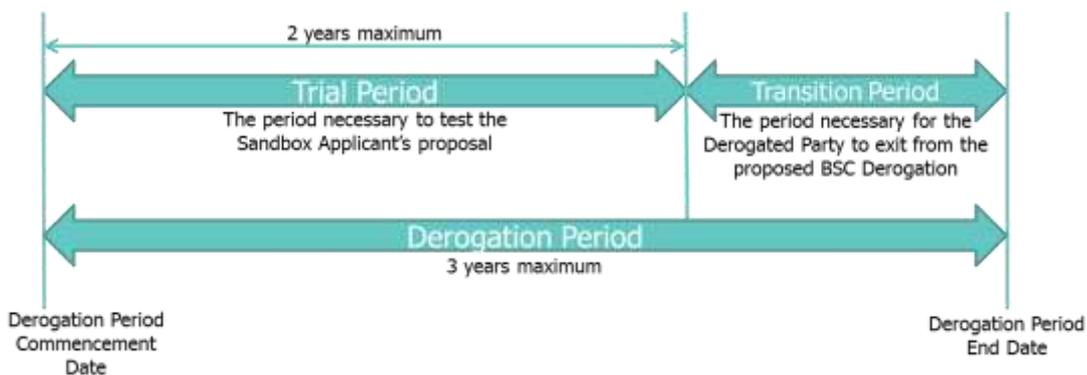
Applications must include the length of time needed to test or trial the product or service, along with a rationale. This should be the shortest amount of time necessary to test the proposal and raise a Modification. This Trial Period can be extended for exceptional circumstances, but cannot be extended beyond the maximum Trial Period allowed of **two years**. The Derogated Party will need to provide relevant information to inform the decision. Ofgem can extend the Trial Period. However, it is expected that the Panel, at the request of the Derogated Party or ELEXON, will recommend to Ofgem whether to extend the Trial Period or not, before Ofgem makes a decision.

The Transition Period is the period during which the Party exits from the sandbox, either returning to the previous state or putting in place permanent arrangements via a BSC Modification. The Transition Period can be extended for exceptional circumstances and using the same approach as the Trial Period extensions.

Modifications

Where a BSC Modification is raised during the Trial Period to address the barriers/issues faced by the Derogated Party, and is not yet implemented, rejected or withdrawn, the Derogation Period may be extended to a maximum of **three years**. If the Modification is rejected or withdrawn the exit provisions within the Transition Plan will be triggered. It will be the responsibility of the Derogated Party (or any other Party) to raise a BSC Modification. Where a Modification is not raised during the Trial Period, the Transition Period cannot be extended.

Diagram 1: Derogation Period



Appendix 3 contains further worked examples, including extension to Derogation Periods.

Reporting and monitoring

In addition to the pre-agreed monitoring and reporting for each Derogated Party, ELEXON will produce a report outlining lessons learned from the sandbox service. For example, metrics and statistics on the sandbox service, key themes that have emerged, or any changes that have been, or need to be, made to the sandbox service.

More detail on the solution can be found in Attachment C (business requirements) and Attachment A (draft legal text).

Self-Governance

The Workgroup unanimously believes that this Modification does not meet the Self-Governance Criteria due to it having a material impact on competition and the Code's governance and modification procedures (Self-Governance criteria (a) (ii) and (iv) respectively).

Assessment Consultation Question

Do you agree that P362 does not meet the Self-Governance Criteria and so should not be progressed as a Self-Governance Modification?

The Workgroup invites you to give your views using the response form in Attachment B

Alternative solution

At this stage, the Workgroup has not identified any alternative solutions, which it believes would better facilitate the Applicable BSC Objectives compared with the proposed solution.

Assessment Consultation Question

Do you agree with the Workgroup that there are no other potential Alternative Modifications within the scope of P362 which would better facilitate the Applicable BSC Objectives?

Please provide your rationale and if 'No' please provide full details of your Alternative Modification(s) and your rationale as to why it/they would better facilitate the Applicable BSC Objectives than the Proposed Modification.

The Workgroup invites you to give your views using the response form in Attachment B



What are the Self-Governance criteria?

A proposal that, if implemented:

- a) is unlikely to have a material effect on:
 - i. existing or future electricity consumers; and
 - ii. competition in the generation, distribution, or supply of electricity or any commercial activities connected with the generation, distribution, or supply of electricity; and
 - iii. the operation of the national electricity transmission system; and
 - iv. matters relating to sustainable development, safety or security of supply, or the management of market or network emergencies; and
 - v. the Code's governance procedures or modification procedures, and
- b) is unlikely to discriminate between different classes of Parties

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Legal text

The proposed redlined changes to the BSC to deliver P362 can be found in Attachment A.

Assessment Consultation Question

Do you agree with the Workgroup that the draft legal text in Attachment A delivers the intention of P362?

Please provide your rationale.

The Workgroup invites you to give your views using the response form in Attachment B

Are there any (other) alternative solutions?

The Workgroup discussed a number of variations of the proposed solution. These discussions are detailed in section six below.

4 Impacts & Costs

We invite participants to detail any impacts that the implementation of the P362 solution would have on their organisation, quantifying where possible the approximate lead time and estimated costs associated with the identified impacts.

Estimated central implementation costs of P362

The implementation costs of P362 are approximately £240 to make the required changes. These costs primarily relate to the delivery of products needed by ELEXON to operate the sandbox service.

Indicative industry costs of P362

We do not expect P362 to directly impact industry participants, but we seek clarification of this via this consultation. Rather it will enable parties to apply for BSC derogations.

P362 impacts

Impact on BSC Parties and Party Agents

Party/Party Agent	Impact
Parties and Agents	No implementation impacts anticipated. This Modification will allow Parties and Agents to participate in the sandbox process.

Impact on Transmission Company

No implementation impacts anticipated. Transmission Company will not be permitted to apply for BSC derogations.

Impact on BSCCo

Area of ELEXON	Impact
ELEXON	<p>Implement the P362 legal text and subsidiary documents. Implement products to operate the sandbox service:</p> <ul style="list-style-type: none">• Produce a suite of templates, such as impact and risk assessment templates.• Deliver local working instructions.• Produce guidance for applicants on the sandbox process.• Produce a sandbox webpage to provide an overview and support for applicants. <p>ELEXON will not be permitted to apply for BSC derogations.</p>

Impact on BSC Systems and process	
BSC System/Process	Impact
All	No implementation impacts anticipated. However, the Modification Proposal will allow participants to suggest ideas that could impact BSC systems and processes. These impacts would be considered as part of the sandbox process on a case by case basis, and applications could be rejected on the basis of these impacts.

Impact on BSC Agent/service provider contractual arrangements	
BSC Agent/service provider contract	Impact
All	No implementation impacts anticipated. However, the Modification Proposal will allow participants to suggest ideas that could impact BSC Agents. These impacts would be considered as part of the sandbox process on a case by case basis, and applications could be rejected on the basis of these impacts.

Impact on Code	
Code Section	Impact
Section B	Updated to expand the role and function of the BSC Panel to include consideration of sandbox applications.
Section H	Updated to include the sandbox provisions.
Section X	Updated to include new defined terms

Impact on Code Subsidiary Documents	
CSD	Impact
new – BSC Sandbox Procedure	A new subsidiary document providing further detail on the BSC sandbox process and requirements.

Impact on other Configurable Items	
Configurable Item	Impact
Guidance notes	New guidance notes to provide support for sandbox applicants.

Impact on Core Industry Documents and other documents	
Document	Impact
Ancillary Services Agreements	No direct impacts, although we understand that some codes may require changes to facilitate their own sandbox service.

Impact on Core Industry Documents and other documents	
Document	Impact
Connection and Use of System Code	
Data Transfer Services Agreement	
Distribution Code	
Distribution Connection and Use of System Agreement	
Grid Code	
Master Registration Agreement	
Supplemental Agreements	
System Operator-Transmission Owner Code	
Transmission Licence	
Use of Interconnector Agreement	

Impact on a Significant Code Review (SCR) or other significant industry change projects
P362 has been exempted from existing SCRs by Ofgem.

Assessment Consultation Question

Will the implementation of P362 impact your organisation?

If 'Yes', please provide a description of the impact(s) and any activities which you will need to undertake between Ofgem's approval of P362 and the P362 Implementation Date (including any necessary changes to your systems, documents and processes). Where applicable, please state any difference in impacts between the Workgroup's proposed solutions.

The Workgroup invites you to give your views using the response form in Attachment B

Assessment Consultation Question

Will your organisation incur any costs in implementing P362?

If 'Yes', please provide details of these costs, how they arise and whether they are one-off or on-going costs. Please also state whether it makes any difference to these costs whether P362 is implemented as part of or outside of a normal BSC Systems Release. Where applicable, please state any difference in costs between the Workgroup's proposed solutions.

The Workgroup invites you to give your views using the response form in Attachment B

5 Implementation

Recommended Implementation Date

The Workgroup recommends an Implementation Date for P362 of:

- **Five Working Days after the Authority's decision.**

As this is a document only change, the Workgroup believe it is important to put in place the BSC sandbox service as soon as reasonably practicable. ELEXON will not receive applications directly from applicants. Rather, Ofgem will control the application rounds and when to pass applications onto ELEXON.

Assessment Consultation Question

Do you agree with the Workgroup's recommended implementation approach?

Please provide your rationale.

The Workgroup invites you to give your views using the response form in Attachment B

Assessment Consultation Question

How long (from the point of Ofgem approval) would you need to implement P362?

Please provide an explanation of your required lead time, and which of the activities are the key drivers behind the timescale. Please also state whether it makes any difference to this lead time whether P362 is implemented as part of or outside of a normal BSC Systems Release. Where applicable, please state any difference in lead times between the Workgroup's proposed solutions.

The Workgroup invites you to give your views using the response form in Attachment B

Cross-code working

The Workgroup highlighted that many innovative products or services would likely have cross-code impacts. Whilst some projects may only impact one code, they believed these would be the minority of cases. The Workgroup believed that the BSC sandbox would add the most value to industry if other codes had a sandbox service too. Ideally there would be a way to co-ordinate these sandboxes across the different electricity and gas codes, with a single point of entry for applicants. Many members believed Ofgem should be leading and co-ordinating applications across industry. The Workgroup views were consistent with those of the BSC Panel when the Initial Written Assessment was presented at the [November Panel meeting](#). The Workgroup were therefore pleased when Ofgem agreed to fulfil this role.

Ofgem are continuing to hold cross-code meetings to agree and put in place the cross-code arrangements. A member suggested that a cross-code group or the Code Administration Code of Practice (CACoP) group would be well placed to facilitate sandbox applications across-codes.

The role of Ofgem

It was not until after the first P362 Workgroup meeting (held on 13 December 2017) that Ofgem agreed to co-ordinate the sandbox user journey. Ofgem held a meeting with Code Administrators in January 2018 to seek support for industry sandboxes. Code Administrators agreed in principle to work with Ofgem on implementing industry sandboxes. Ofgem agreed to:

- Develop a single point of access, removing the need to apply to multiple codes;
- Operate a sifting process ahead of applications being forwarded to relevant parties; and
- Co-ordinate the feedback process for valid applications.

Existing Ofgem derogation powers

Some members believed that Ofgem should be raising BSC Modifications, using powers gained from [P351 'Align the BSC with changes to the SCR requirements'](#), to address any barriers in the market that it is aware of.

The Workgroup explored whether existing Ofgem powers would forgo the need for a BSC sandbox. [Electricity supply licence condition 11.3](#) provides the Authority with the power to relieve a licensee of obligations (in whole or in part) under the BSC (and Master Registration Agreement (MRA), Distribution Connection and Use of System Agreement (DCUSA), Connection and Use of System Code (CUSC)). Similarly, [electricity generation licence conditions 5.2 and 6.2](#) provide the Authority with the power to relieve a licensee of obligation in respect of parts of the Grid Code and Distribution Codes respectively.

For **licensees**, Ofgem could treat derogations against codes on a case by case basis after careful consideration of the evidence provided by the supplier or third parties. These powers can only apply to licensees, and therefore do not extend a solution to parties who are not required to be licensed (e.g. Party Agents, licence exempt generators and

Suppliers). Additionally one member believed that a BSC sandbox would ensure that the experts of the BSC, ELEXON and the Panel, were involved in the decision making process.

The Workgroup therefore agreed that it was still necessary to proceed with a process described in the BSC.

P362 Ofgem derogation powers

The Workgroup discussed whether Ofgem can remove conditions from recommended derogations, and agree to derogations which the BSC Panel has recommended be rejected. The Workgroup agreed that the BSC Panel is best placed to consider the risks and impacts with regards to Settlement but also acknowledged that Ofgem's ability to coordinate between Codes is diminished if they can't make amendments for incompatible conditions. Additionally, Ofgem are able to make value judgements not obliged to the BSC Panel (e.g. benefit to consumers).

Three options were considered by the Workgroup:

1. Include provisions in the cross-code process for Ofgem to consult with Panel(s) when conditions are incompatible or subject to differing value judgement;
2. Include send-back provisions in BSC legal text to enable Ofgem to request Panel remove/alter conditions; or
3. Include provisions in the BSC removing the effect of any Ofgem decision to remove or alter a condition of derogation, or approving a recommendation to reject.

The Workgroup rejected option three as it would devalue the decision making role of Ofgem and could jeopardise coordination with other sandboxes. Legally the BSC cannot directly empower or restrict Ofgem, as it is not a Party. Moreover, the Workgroup supported Ofgem's role as a decision maker, but believed any reasons for the decision should be transparent. The Modification process has been used as a basis for the derogation process and option three would be inconsistent with this approach.

Under the Modification process, Ofgem cannot amend a solution. Where Ofgem want an amendment to the solution, they must send the Modification back to the Panel (as per [Section F2.7A](#)). A member believed the derogation process should follow a similar approach. If the Panel have set conditions to alleviate particular concerns or risks, any changes to these conditions could change the Panel's view. Where Ofgem wish to amend the conditions, the Panel should therefore re-evaluate the derogation and make a new set of recommendations to Ofgem.

A member did not believe this approach would reduce the ability of Ofgem to co-ordinate with other sandboxes. Rather it ensures the basis for any recommendations and decisions are robust and will stand up to judicial review. In addition, it was important for transparency and for industry to understand the basis on which decisions are made. The decision does not have to agree with the Panel, but they should have to consult the Panel on any changes to the conditions.

Ofgem commented that they fully support a collaborative approach with Code Administrators. They agreed they would need to evaluate the Panel's concerns and conditions and could not disregard them, but could disagree with them.

A member wondered if Ofgem sitting on the Panel could negate the need for option two and support option one instead. However, another Workgroup member highlighted that Ofgem does not vote at the Panel and would not be able to fetter its discretion or offer binding decisions at the Panel. The member commented that Ofgem attends the Panel to provide an important link back to decision makers at Ofgem by reporting back on the Panel discussions and providing appropriate updates to the Panel. In addition, the Ofgem representative would likely need to seek expertise from colleagues.

A member was concerned that the back and forth nature of option two may add time to the derogation process. The Workgroup considered hard coding a fixed response time for the Panel re-evaluating derogations. Where a fixed approach is taken, it may result in more 'no' decisions, as there may not have been time to sufficiently consider the derogation.

The Workgroup agreed instead to adopt a similar approach taken for Urgent Modifications. The Panel Chairman will decide whether an ad-hoc Panel meeting is required, having regard for the circumstances and request of the applicant.

The Workgroup agreed to progress with option two as the conditions set could have been fundamental to the Panel's recommendation. One member believed sending derogations back should be the exception and could be further reduced by building robust cross-code processes. The Workgroup believed option two gave the right balance between transparency, protection for Parties and supporting innovators. They agreed that Ofgem have the final decision.

Assessment Consultation Question
Do you agree with the send back provisions?
Please provide your rationale.
The Workgroup invites you to give your views using the response form in Attachment B

The BSC Sandbox Process

The Workgroup believed that a key success criterion for P362 would be that the sandbox process is quicker and less burdensome than the Modifications process to enable ideas to be tested and brought to market.

Strong concerns were initially raised about the appropriateness of BSC Parties funding the sandbox service. The concerns focussed on ELEXON spending Parties' money to progress non-Parties applications and on funding research and development of other Parties. There was a concern that the nature of trialling innovative ideas is that most of them will fail, so why should Parties money be used to fund something that does not work. These concerns were alleviated by clarifying the intention of P362 and in the design of P362, as elaborated on below.

Contrary views were also expressed by the Workgroup. Successful trials should result in BSC Modifications that will remove barriers and bring opportunities to all Parties. ELEXON believed any support provided prior to the applicant becoming a Party was comparable to the [market entry service](#). ELEXON already provides guidance to potential Parties looking to enter the market, including some that have applied to Ofgem's sandbox.

ELEXON expects to resource the sandbox service using existing resource. Successful applicants will need to accede to the Code (if they are not already a Party) and so should

be entitled to the normal BSC services at that point. The Workgroup believed it to be important for ELEXON to be transparent about how it was funding the sandbox service. One Workgroup member did not believe it appropriate for ELEXON to be ramping up resources to operate the sandbox service. ELEXON agreed to provide details of sandbox service in its annual BSCCo Business Plan.

ELEXON confirmed that the sandbox is not appropriate for trialling unproven technology, large scale products or services that would be better facilitated via a Modification, or products or services that would not provide any benefits to the wider industry. The application should demonstrate how it will provide benefits to the wider industry and if it cannot, it should be rejected. Any applications posing significant risk to Settlement should be rejected. The scale of the derogation should be constrained to mitigate risk to Settlement and kept at a level needed to test the idea but not to scale it. The Workgroup acknowledged that successful applicants would get a first mover advantage, but should not be making significant commercial gains as a result.

The derogation should apply only to pre-competitive products and services that would not be cost-effective to trial otherwise. Whilst the BSC change process allows for different options and solutions to be considered, it does not allow for these different options to be tested in the live market environment. The sandbox service will provide real life data and evidence to support decision making and is inherently more powerful than a paper based assessment. It was suggested that a halfway house, between paper based and real market testing, would be for a virtual test environment to be available to Parties. ELEXON agreed this could bring many benefits, and should be re-considered following the planned architectural changes to BSC central systems. ELEXON also noted that there is always a difference between a test environment and a live environment.

The Workgroup noted that it would be helpful if there were an example project for how a derogation might be applied. The solution was developed without consideration of any specific derogation that might be requested by an applicant.

Charges to applicants and Derogated Parties

Application fee

There was some concern raised around the volume of additional work the sandbox service may require from ELEXON. The Workgroup agreed that the solution should allow for the Panel to set an application fee. This would deter speculative applications. ELEXON confirmed that the fee could not be a BSC Section D Charge as these charges applied only to BSC Parties. As non-Parties can apply to the sandbox, Section D charging was not appropriate. The fee would defray BSC Costs for Parties.

The Workgroup noted that they would expect the fee to be set at zero initially and only increased if the volume of work exceeded that expressed in the ELEXON business plan. Innovators within the Workgroup were content with this approach, on the basis that the fee would be fixed and known upfront so that it could be factored into business plans and costs.

The Workgroup also discussed removing the fee, given that Ofgem would act as the 'gate keeper' for applications, which should result in fewer applications reaching ELEXON. However, they agreed to keep the fee, as it would enable ELEXON to recover some costs if the volume of work became more significant and built flexibility into the solution. ELEXON agreed with the Workgroup that the fee should be published and easy to find on the BSC Website.

Additional fees

The Workgroup agreed that ELEXON should be able to charge a Derogated Party additional fees associated with the administration of the derogation, if applicable. The charges should be agreed as part of the application process, so that it is clear to the Party what they will be expected to pay and when. For example, if the derogation requires ELEXON to operate a workaround, the Workgroup believed it reasonable for the Derogated Party to pay for this. Furthermore, they agreed any extensions to the Trial or Transition Period could result in an extension to recovery of these costs also.

The Derogation Period

The Workgroup felt strongly that derogation should be for a limited period of time and should not be subject to continuous extensions as is the case for Metering Dispensations. The purpose of the sandbox derogation is to test and trial products or services. It is not intended to put in place a permanent arrangement that would give individual Parties special benefits and exemptions to rules that everyone else is expected to adhere to.

The maximum Derogation Period

The Workgroup discussed the maximum period needed to trial the product or service ('the Derogation Period'). Many members shared the view that most products or services should get the data they need within six to 12 months to prove the concept. One member highlighted that if the project involved trialling solar technology you may need two summer seasons of data. The Workgroup therefore agreed that no more than **two years** should be needed to trial the product or service.

Transition vs. Derogation Period

A member suggested that it would be unreasonable for a Derogated Party to be required to exit the sandbox if they were trying to put in place permanent arrangements via a BSC Modification or the Modification is delayed. If a Party is forced to exit, they may lose financial backing and no longer be able to operate. A member therefore suggested that a 'transition period', in addition to the Derogation Period, should be created to allow the Party time to put in place the enduring arrangements.

The Workgroup considered allowing the transition period to be open until the Modification was implemented, rejected or withdrawn, at which time the Derogation Period would be triggered, if needed. However, many members felt uneasy about this prospect as it could result in prolonged derogations. It may even be in the Derogated Party's interest to drag the Modification process out. The Workgroup identified the following solution requirements for this area:

- Parties should be incentivised to raise Modifications in a timely manner;
- Parties should not be given an unfair advantage from having an extended derogation;
- An extension should not increase the risk to Settlement or Parties; and
- Extensions should not be able to be continually extended.

The Workgroup believed so long as the transition period did not allow the Party to extend its scope or scale of operation, and the risk and impact to Settlement and Parties remained acceptable, then it was reasonable to allow the transition period to be extended to allow for Modifications to be put in place. Any payment of costs agreed as part of the application, may be continued to cover the extension.

A member suggested that three years should be plenty of time to trial the product or service and put in place a Modification. The Workgroup agreed a **three year** maximum for both the trial and transition period would meet the solution requirements listed above. The three year period should be subject to a Modification being raised (and not implemented, rejected or withdrawn) during the Derogation Period. A member commented that if more than three years was required to test an innovative product and service and put new arrangements in place, then the sandbox process is probably not the appropriate mechanism. A **Derogation Period** is the trial and transition period together.

The Workgroup also believed the maximum trial and Derogation Period should be placed in the BSC and not a subsidiary document. Given the critical nature of this aspect, the Workgroup agreed to seek industry views on this proposal.

Assessment Consultation Question

Do you agree with the Workgroup's proposal for a maximum two year trial period and a maximum three year derogation period if an associated Modification has been raised within the Derogation Period?

Please provide your rationale, and if 'no', please provide an alternative approach or period.

The Workgroup invites you to give your views using the response form in Attachment B

Minimum Derogation Period

The Workgroup wondered whether there should be a minimum Derogation Period to avoid frivolous or gaming behaviour, such as seeking a derogation to get an advantage from not having to comply with the normal rules. However, the Workgroup were satisfied that this would likely be identified and rejected as part of the process and could be dealt with if it happened.

Conditional start dates

The Workgroup discussed when derogation should start. They agreed that the Panel should be able to set a conditional start date, for example the derogation must start between 'x' and 'y', for a period of 'z' months. One member commented that contingency should be built into the plans by applicants. Another member suggested that a date could be agreed in principle and finalised in a meeting.

Extensions

The Workgroup considered the circumstances that might justify an extension to a Derogation Period, such as illness or significant technical failures (e.g. fire). One member suggested that allowing for extensions sent the wrong message, but accepted there may be a need for it. If a new barrier emerged, the Workgroup believed this should require a

new derogation and this was not a valid reason to request an extension. A new barrier requires a new derogation. The Workgroup agreed that extensions could be sought for the Derogation Period, up to the maximum two years, and for the transition period, up to the maximum 3 years. Ofgem could direct these extensions, or preferably, the Derogated Party would request the extension, providing justification, and the Panel would make a recommendation to Ofgem whether to extend the derogation or not.

Criteria

The Workgroup believed that adopting Ofgem's eligibility criteria would be sensible. However, this was determined to be redundant after Ofgem agreed to act as the point of entry, on the assumption they would only pass on applications to ELEXON that met their eligibility criteria, which are:

1. **Innovation:** The proposition must be ground-breaking or significantly different to what is currently in the market. It could include either technological or business model innovation.
2. **Consumer benefit:** It should be clear how the proposition would benefit consumers. This could be, for example, because it would lead to direct benefits such as lower energy bills or better customer service, or indirect benefits such as increased competition in the market.
3. **Background research:** You should have researched the concept and be able to show that you have attempted to find out about the regulatory implications.
4. **Need for support:** The Innovation Link provides information on the regulation in the energy sector. It does not provide business advice on the commercial viability of a project. You should be able to tell us why you need Link support. For example, what it is that you wish to understand from a regulatory perspective or how you think Link support would benefit you.

The Workgroup were quick to agree that all applications would need to demonstrate that they better facilitate the Applicable BSC Objectives as these are the basis on which changes to the BSC are made.

Some members, more familiar with the Panel, believed the Panel's assessment of applications should be similar to Modifications. The Panel would need to take a balanced view, including short and long term impacts, which may differ, and be able to defer its decision if they require further information to inform its decision. The Workgroup concluded that the Panel should have broad discretion to make its decisions on a case by case basis.

The Workgroup discussed the extent to which compliance with other codes and licences should impact the Panel's decision. ELEXON's legal counsel confirmed that the Panel could only make recommendations for BSC derogations. It is not the role of ELEXON or the Panel to consider compliance with anything other than the BSC. However, the Workgroup believed that if ELEXON or the Panel were aware that consideration of other codes and licences was required this should be flagged in the Panel report to Ofgem. ELEXON agreed with this approach.

The Workgroup considered requiring the applicant to provide a self-declaration of compliance statement signed by a director. However, this was rejected once Ofgem

agreed to act as the 'gate keeper' for applications, noting that the responsibility to ensure compliance lies wholly with the applicant.

Consider totality

The Workgroup believed that, in order to protect the integrity of Settlement, the Panel should consider the totality of derogations. For example, the risk posed by one application that impacts 1000 MSIDs may be acceptable, but the risk posed by a second application with an additional 1000 MSIDs may not be acceptable.

The Workgroup noted that Ofgem would need to carefully consider how it would handle applications to ensure it treated them fairly. For example, is a simple first in first out the right approach, or would a 'currency pool' of risk be more appropriate?

Subsidiary document

The Workgroup were of the view that a subsidiary document would be required to detail further eligibility criteria and considerations. This approach was seen to offer a more efficient way to maintain the provisions, rather than including the text in the BSC. However, the Workgroup believed associated procedures did not need to be under change control, but instead could be published on the BSC Website, if needed. ELEXON noted this was less likely now Ofgem were leading the process.

The Workgroup believed that key parts of the subsidiary document should be available as part of the Assessment Procedure Consultation to provide comfort to Parties on how the process would work. Attachment D contains the draft subsidiary document.

Assessment Consultation Question

Do you agree with the content of Attachment D, with specific consideration of the application approach, eligibility criteria and monitoring approach described?

Please provide your rationale. If 'no', please provide details of the areas you would like to see covered in the document.

The Workgroup invites you to give your views using the response form in Attachment B

Risks

One Workgroup member commented that the purpose of the BSC is to ensure volumes and funds are allocated and settled accurately, equitably and efficiently. Any derogation that allows participants to side step this principal or undermines it should not be acceptable.

Another Workgroup member was concerned that there was a risk that new BSC Parties with limited experience are more likely to mismanage their trading positions, resulting in them going bust and abandoning customers. Any financial defaults will have to be paid for by BSC Parties.

One member suggested that applicants should provide some working capital to cover any costs incurred in the event of failure or issues. However, this was seen to be overly complex. Furthermore, Parties requirements to lodge Credit Cover for Trading Charges should not be derogated.

Any risks should relate to the derogation and not to the technology. Only projects with sufficiently mature technology and products should be allowed to participate.

The Workgroup agreed that constraining the scope of the application in terms of time and scale will help reduce the risk and impact. The applicant and ELEXON should be required to conduct risk assessments for each application and present the findings to the Panel and Ofgem.

Impacts

Derogations should not adversely impact Parties or Settlement. The Workgroup agreed that ELEXON must conduct an impact assessment, supported by the applicant. There may be impacts or operating models that ELEXON is not aware of in the industry. There may also be cases where the industry is already trialling the idea in compliance with the Code, which ELEXON is not aware of. These can only be identified by asking industry. This will help ensure the idea is truly innovative.

The Workgroup therefore agreed that ELEXON must consult industry. The consultation will increase the chances of identifying all likely impacts and better inform the Panel and Ofgem in its decision making.

The Workgroup discussed how long the consultation should be for. They recognised that different organisations will require different timescales. They did not believe any more than 15 Working Days should be needed, but thought less than 10 Working Days may not be enough.

The Workgroup believed it important for ELEXON to conduct its own impact assessment. This will form the basis for the industry consultation. The Workgroup and ELEXON believed transparency was an important design principle to ensure trust in the process. It was agreed that all consultation responses will be published, save for any redactions for confidential information. The impact assessment responses and ELEXON's action in regard to any response will be included in the report to the Panel and Ofgem to maintain the history of the impacts identified. This approach is similar to that taken for Modifications.

Who should be able to participate?

One Workgroup member believed the need for a sandbox was exacerbated because non-parties were not able to raise Modifications without Ofgem designation. ELEXON pointed out that the sandbox service was designed for testing pre-competitive and innovative products or services that met a given set of criteria. It is not appropriate to compare the Modification and sandbox services. Moreover, non-Parties would be able to apply to Ofgem for derogation. If derogated they could raise a consequential Modification to address the barrier being faced.

Only Parties can be derogated – you cannot be derogated against a code you are not a party to. Therefore, if a non-Party applies to enter the sandbox, they would need to accede to the Code before the derogation became effective. It was noted that the derogation could include provisions related to Market Entry and Qualification. For example, if they needed to accede as a Supplier, but did not need to carry out the majority of the Supplier functions, they could seek derogation for those areas too.

The Workgroup agreed with ELEXON that BSCCo should not be able to apply for derogation. The Workgroup also believe Transmission Company² should not be permitted to apply for derogation. The Workgroup believed it would be inappropriate for these organisations to seek derogation from rules that they are bound to administer.

The Workgroup agreed that multiple Parties can be linked with derogation. For example, two Parties may be in a partnership, with both providing different functions that require derogation. Both Parties could therefore be derogated.

What can be subject to BSC derogation?

The Workgroup agreed that the following should not be eligible for derogation:

- The Electricity Market Reform (EMR) provisions protected in BSC Section F1.1.9;
- The European Union law provisions; and
- The sandbox provisions.

The Workgroup was concerned that any provisions related to requirements that have originated from outside the BSC, such as EMR legislation and European Network Codes that have a higher legal standing, should be protected. In addition, the Secretary of State has powers of veto for the EMR provisions. The Workgroup was concerned that unless the EMR provisions were protected, there was a risk these powers of veto may be evoked, increasing the risk that P362 is rejected. The EU law provisions in the P362 draft legal text have been drafted so as to work following Brexit.

ELEXON clarified that the existing provisions around indemnity and the ability to claim damages and other liabilities against the Panel and ELEXON would apply. Any support provided by ELEXON could not be considered legal advice. However, ELEXON would play the 'critical friend' role with applicants and Derogated Parties.

The Workgroup discussed how a Derogated Party's responsibility for reconciliations should be treated. The Workgroup believe that there are certain areas and principles of the BSC that cannot be derogated in practice, such as the requirements to register Metering Systems or pay Settlement and trading charges.

The Workgroup believed that Settlement Reconciliations would be one such area. One member suggested that a Derogated Party could arrange for responsibility for reconciliations to be passed to another Party or for sufficient credit cover to be lodged to cover any shortfalls following a subsequent reconciliation.

The Workgroup believed it would be important to include some guidance for applicants on what would likely be unacceptable risk to Settlement. They noted that as applications are progressed, knowledge of the areas less and more likely to be derogated would be learnt. Attachment D contains some areas that ELEXON initially believes would likely result in unacceptable risks to Settlement.

Transition Plan

The Workgroup agreed that the Party should request a Derogation Period as part of its application. This plan must detail how they will exit the sandbox and return to its previous

² This includes National Grid as Transmission System Operator and System Operator, but excludes its Interconnector businesses.

state. The plan will automatically be applied at the end of the Trial Period, unless the derogated period has been extended, either for exceptional circumstances or for allowing a Modification to be put into place. The Party may also choose to exit early. The Panel (or Ofgem) may also trigger the plan. For example, if the derogation has an unexpected material impact on Settlement, the derogation may be withdrawn.

Panel Role

The Workgroup discussed how the Panel voting should work. They considered the existing voting rules in BSC Section B, the voting rules used for Modifications or requiring a unanimous decision.

The current derogation provisions in the BSC, such as for Metering Dispensations, require a unanimous decision. These decisions are made by the ISG and Supplier Volume Allocation Group, where all decisions are required to be made by a unanimous vote of members. The only other unanimous voting in the BSC is required for Fast Track Self-Governance Modification Proposals considered by the Panel. All other Panel decisions (including Modifications), and those of the Performance Assurance Board (PAB) and Trading Disputes Committee (TDC) are made by simple majority voting.

The Workgroup believed that a unanimous decision would have been more appropriate if the Panel were the decision maker. Conversely, if they are making a recommendation, or there is a route for appeal, a simple majority would be better suited.

The Workgroup supported Ofgem being the decision maker, as this was seen to be the most efficient way for cross-code decisions to be made. The Workgroup discussed alternatives to Panel making recommendations to Ofgem, such as the Panel deciding, with the Party having a right to appeal to Ofgem. Any self-governance type concepts were seen to be adding unnecessary complexity.

Given that the Panel are making recommendations to Ofgem and are not deciding whether to derogate, the Workgroup believed that unanimous voting would be too restrictive and decided to adopt the general voting provisions in BSC Section B. The Workgroup did not believe the Modification voting provisions added any value; rather they were overly restrictive (requiring meetings to be held in person) and therefore should not be adopted.

Reporting and monitoring

The Workgroup believed that applicants would require support from ELEXON and Ofgem to understand the type and level of detail required to be reported on. The Workgroup reiterated the importance of transparency and reporting meaningful information that would be of benefit for other Parties, without exposing commercially sensitive or intellectual property information. A member commented that innovators are often keen to share their experiences and learn from one another and this should be the ethos for the reporting and monitoring of BSC derogations.

A Workgroup member believed that the project outcomes should be known and defined up front. Key milestones should be identified and these could form the basis to report against. Other areas the Workgroup expected to be reported against were any impacts on Settlement and key learnings. The Workgroup agreed that the Derogated Party should be required to report back to ELEXON, who would publish the update, save for any redactions for confidentiality reasons. In practice the Party may only need to report once, to Ofgem, and copy the relevant codes in.

The Workgroup also agreed that ELEXON should report to the Panel periodically on the sandbox service, in a lessons learned report. This should also be published and may lead to changes to the process.

New Party Role

A Workgroup member wondered if a new Party role would help make the process more efficient, such as a 'sandbox role'. ELEXON noted that they are aware Ofgem is considering moving the market away from roles and towards functions. One benefit of the new role would be to allow Parties to enter and exit more quickly. However, the Workgroup believed that the derogation process should inform what a new role or function may need to look like and would be best addressed in a subsequent Modification.

Further considerations

A member brought to the attention of the Workgroup a set of legal questions that a CUSC Panel Member had raised. The Workgroup noted that the key take away for P362 was that any BSC derogations would be to avoid creating distortions or impacting other schemes and laws, such as EU State Aid. The Panel would need to keep in mind these areas when considering whether to recommend derogation or not.

Appendix 4 contains the questions and Ofgem's response to these.

Workgroup's initial recommendations

At this stage, the majority of the Workgroup believes that P362 **would** overall better facilitate the Applicable BSC Objectives and so should be **approved**.

P362 was raised by the Panel (in accordance with Section F2.1.1(d)(i)), who appointed a BSCCo representative as the Proposer's representative. In this circumstance, the Proposer's representative is not allowed to vote (see Section F2.4.5C).

Applicable BSC Objective (c)

The **majority** of the Workgroup **agree** that P362 would better facilitate Applicable BSC Objective (c) as it will enable the trialling of innovative ideas and for more companies to offer alternative solutions to consumers, and therefore increase competition.

By enabling innovative businesses to test their new products and ways of working, P362 makes it possible to introduce more disruptions to the existing ways of doing business. Greater numbers of firms offering greater numbers of alternative solutions will provide consumers with more choice as a result of an increased competitive market.

The industry is rapidly changing and P362 will help to foster an environment to support this rapid change. By sharing lessons learned, the whole industry can benefit. P362 will encourage new ideas to be brought forward and encourage innovators to enter a market which is perceived to be slow and difficult to enter.

The **minority** of Workgroup members were **neutral** against Applicable BSC Objective (c) as they believed any benefits to competition were balanced out by penalising Parties who have invested time and money in complying with the existing BSC rules. One member commented that it is difficult to say until examples come forward.

Whilst innovation should be supported, some members felt uncomfortable 'letting people off the hook'. Some members also commented that there is a rule book for a reason and there will be inherent risks from deviating from those rules. However, they believed that appropriate checks and balances had been put in place to mitigate these risks, particularly with Ofgem acting as the 'gatekeeper' and the send back provisions.

Applicable BSC Objective (d)

The **majority** of Workgroup members were **neutral** against Applicable BSC Objective (d) as any efficiency gained was balanced out by the costs of administering the sandbox service.

The **minority** of Workgroup members believed P362 **would** better facilitate Applicable BSC Objective (d) as by negating the need for future Modifications to enable small scale product tests with no material impact on the rest of the industry, ELEXON and industry resource can be focussed elsewhere. Additionally, if enduring Modifications should become necessary following a successful trial, more information about the solution and any impacts will be known in advance, facilitating a more efficient Modification process.

Innovators will see the sandbox process as less intimidating than a Modifications process and will welcome the support that comes with the process. A member was pleased that

the sandbox process has been brought forward as a Modification to give Parties an opportunity to assess and contribute towards it.

Applicable BSC Objectives (a), (b), (e), (f) and (g)

At this stage, the Proposer and all Workgroup members believe that P362 is neutral against Applicable BSC Objectives (a), (b), (e), (f) and (g).

Assessment Consultation Question

Do you agree with the Workgroup's initial majority view that P362 does better facilitate the Applicable BSC Objectives than the current baseline, and so should be approved?

Please provide your rationale.

The Workgroup invites you to give your views using the response form in Attachment B

Assessment Consultation Question

Do you have any further comments on P362?

The Workgroup invites you to give your views using the response form in Attachment B



What are the Applicable BSC Objectives?

(a) The efficient discharge by the Transmission Company of the obligations imposed upon it by the Transmission Licence

(b) The efficient, economic and co-ordinated operation of the National Electricity 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 of the balancing and settlement arrangements

(e) Compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency [for the Co-operation of Energy Regulators]

(f) Implementing and administering the arrangements for the operation of contracts for difference and arrangements that facilitate the operation of a capacity market pursuant to EMR legislation

(g) Compliance with the Transmission Losses Principle

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Workgroup's Terms of Reference

Specific areas set by the BSC Panel in the P362 Terms of Reference

- a) What conditions, principles or criteria should the Panel consider when determining whether to grant derogation?
 - i. What checks and balances are needed?
 - ii. What decision making power should the Panel be granted and what should the voting mechanism be e.g. simple majority, unanimous or recommendation to Ofgem?
 - iii. How will the solution assess the impact on other Codes and schemes such as CFDs?
- b) What should the scope of derogations and conditions in the BSC be?
- c) Who should be able to participate in the electricity market sandbox?
- d) What process, if any, should applicants go through prior to formally requesting derogation?
 - i. How often should ELEXON run its sandbox process?
- e) How should the solution ensure the processes and derogated projects are transparent to industry?
 - i. How often should any reporting be and where should it be published?
- f) How should the risk to Settlement, the BSC and other industry participants of derogated projects be managed and mitigated?
 - i. Should the BSC Auditor provide a view on the risk to Settlement?
- g) What role should ELEXON have in supporting derogation requests?
 - i. How can the costs of running a BSC sandbox be fair and consistent to BSC Parties?
 - ii. What is the legal status of any support provided by ELEXON?
 - iii. What is the legal status of any derogation provided by the BSC Panel?
- h) How should the transitional process from tested/proved derogated projects to a new permanent baseline be handled?
 - i. How should useful Modifications identified as a result of sandbox projects be progressed?
- i) How can the P362 solution accommodate other electricity industry sandboxes, for example to avoid duplication and provide a common process?
 - i. What cross-code impacts are there?
- j) What changes are needed to BSC documents, systems and processes to support P362 and what are the related costs and lead times?
- k) Are there any Alternative Modifications?
- l) Should P362 be progressed as a Self-Governance Modification?
- m) Does P362 better facilitate the Applicable BSC Objectives than the current baseline?

Assessment Procedure timetable

P362 Assessment Timetable	
Event	Date
Panel submits P362 to Assessment Procedure	9 Nov 17
Workgroup Meeting 1	13 Dec 17
Workgroup Meeting 2	24 Jan 18
Workgroup Meeting 3	26 Feb 18
Workgroup Meeting 4	7 Mar 18
Assessment Procedure Consultation and Industry Impact Assessment	21 Mar to 12 Apr (15WDs)
Workgroup Meeting 5	W/B 16 Apr 18
Panel considers Workgroup's Assessment Report	10 May 18

Workgroup membership and attendance

Name	Release Letter	Organisation	13/12/17	24/01/18	26/02/18	7/03/18
Non-voting members						
Claire Kerr	n/a	ELEXON (<i>Chair</i>)	✓	✓	✓	✓
Lawrence Jones	n/a	ELEXON (<i>Lead Analyst</i>)	✓	✓	✓	✓
Voting members						
Andy Colley	✓	SSE	✓	✓	✓	✓
Derek Weaving	✓	Centrica	✓	✓	☎	☎
Kenneth Skou	✓	NEAS Energy	✗	✓	✓	✗
Chris Smith	✓	Kingscote Enterprises	✓	✓	☎	☎
Pam Liu	✓	Inventev Technology Limited	✓	✓	✓	☎
Aaron Dickinson	✓	Utiligroup	✓	✓	✗	✗
Lisa Waters	✓	Waters Wye Associates	✓	✓	✓	☎
Richard Vernon	✓	Npower Group PLC	✓	✓	✓	☎
Dan Bentham	✓	EDF Energy	✓	✓	✗	✗
Michael Oxenham	✓	National Grid	✓	✓	☎	☎
Non-voting participants						
Peter Frampton	n/a	P362 (<i>Proposer Representative</i>) & ELEXON (<i>Design Authority</i>)	✓	✓	✓	✓
David Stephens	n/a	ELEXON (<i>Lead Lawyer</i>)	✓	✓	✓	✓
Jemma Williams	n/a	ELEXON (<i>Change Team</i>)	✗	✗	✓	✓
Scott Laczay	n/a	Ofgem	✓	✓	✓	☎
Jamie McRorie	n/a	Ofgem	✗	✗	☎	☎
Karsten Mandrup Nielsen	n/a	NEAS Energy	✗	✓	✗	✗
Derek Walker	n/a	Inventev Technology Limited	✓	☎	✓	☎

Appendix 2: Glossary & References

Acronyms

Acronyms used in this document are listed in the table below.

Acronyms	
Acronym	Definition
BEIS	Department for Business, Energy & Industrial Strategy
BM	Balancing Mechanism
BSC	Balancing and Settlement Code
BSCCo	Balancing and Settlement Code Company
CACoP	Code Administrators Code of Practice
CFD	Contracts for Difference
CSD	Code Subsidiary Document
CUSC	Connection and Use of System Code
DCC	Data Communications Company
DCUSA	Distribution Connection and Use of System Agreement
EMR	Electricity market Reform
EU	European Union
FCA	Financial Conduct Authority
GB	Great Britain
GCRP	Grid Code Review Panel
GEMA	Gas and Electricity Markets Authority
GSP	Grid Supply Point
HVDC	High Voltage Direct Current
ISG	Imbalance Settlement Group
MRA	Master Registration Agreement
MSID	Metering System Identifier
NETS	National Electricity Transmission System
NGET	National Grid Electricity Transmission plc
NRA	National Regulatory Authority
PAB	Performance Assurance Board
RfG	Requirements for Generators
SCR	Significant Code Review
TDC	Trading Disputes Company
TFEU	Treaty on the Functioning of the European Union
UK	United kingdom

External links

A summary of all hyperlinks used in this document are listed in the table below.

All external documents and URL links listed are correct as of the date of this document.

External Links		
Page(s)	Description	URL
5	Code of Practice page on the ELEXON website	https://www.elexon.co.uk/bsc-and-codes/bsc-related-documents/codes-of-practice/
7	P362 page on the ELEXON website	https://www.elexon.co.uk/mod-proposal/p362/
5	Panel Paper 271/04 on proposal for BSC sandbox	https://www.elexon.co.uk/meeting/bsc-panel-270/
5	Ofgem Innovation Link	https://www.ofgem.gov.uk/about-us/how-we-engage/innovation-link
5	Ofgem regulatory sandbox	https://www.ofgem.gov.uk/publications-and-updates/update-regulatory-sandbox
5	Ofgem sandbox application round	https://www.ofgem.gov.uk/publications-and-updates/regulatory-sandbox-2-calling-expressions-interest
6	BSC Section L	https://www.elexon.co.uk/bsc-and-codes/balancing-settlement-code/bsc-sections/
6	Code of Practice	https://www.elexon.co.uk/bsc-and-codes/bsc-related-documents/codes-of-practice/
16	November Panel meeting	https://www.elexon.co.uk/meeting/bsc-panel-271/
16	P351 'Align the BSC with changes to the SCR requirements'	https://www.elexon.co.uk/mod-proposal/p351/
16	Electricity supply licence conditions	https://www.ofgem.gov.uk/licences-codes-and-standards/licences/licence-conditions
16	Electricity generation licence conditions	https://www.ofgem.gov.uk/licences-codes-and-standards/licences/licence-conditions
17	Section F2.7A	https://www.elexon.co.uk/bsc-and-codes/balancing-settlement-code/bsc-sections/
19	Market entry service	https://www.elexon.co.uk/reference/market-entry/
39	State Aid	https://www.gov.uk/guidance/state-aid
39	State Aid manuals	https://www.gov.uk/government/uplo

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External Links		
Page(s)	Description	URL
		ads/system/uploads/attachment_data/file/607691/bis-15-148-state-aid-manual-update.pdf
40	European Commission's factsheet	http://ec.europa.eu/competition/publications/factsheets/antitrust_procedures_102_en.pdf
40	Commission Guideline	http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=LEGISSUM:l26113&from=EN

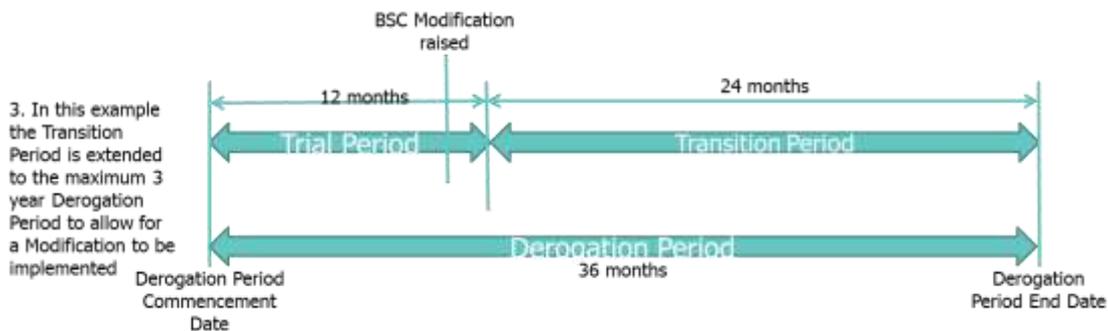
Approved Derogation Period example 1



Approved Derogation Period example 2



Approved Derogation Period example 3



Appendix 4: Further legal considerations

At the December CUSC Panel meeting a member asked the Ofgem representative whether a number of items had been considered by Ofgem for their sandbox, namely:

1. State Aid;
2. Competition law; and
3. Affect on cross border trade; [and EU derogation process].

The member took an action to write to the Ofgem representative on these items. An extract of this email is below:

1. State Aid

In respect of State Aid, I was thinking in terms of where "State aid is any advantage granted by public authorities through state resources on a selective basis to any organizations that could potentially distort competition and trade in the European Union (EU)." [emphasis added] as defined via the UK Government website.

<https://www.gov.uk/guidance/state-aid>

Further clarification can also be found in the 'State Aid Manual' published by BEIS:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/607691/bis-15-148-state-aid-manual-update.pdf

It sets out at paragraph 1.10 (and further details in Annex A) the four tests that should be applied.

Would you or your colleagues be able to confirm if: (a) the Ofgem sandbox arrangements have already been explicitly assessed in terms of State Aid; (b) that the those four test in Annex A of the BEIS document have been performed in this case by Ofgem; and (c) that as a result Ofgem have certified that the sandbox arrangements are not 'State Aid'?

I was wondering if what is being proposed, in terms of the 'sandbox', could amount to a conferring of an advantage, on a selective basis, to some organisations (by, for example, them avoiding the need to comply with some Code obligations that similar organisations have to comply with) might be considered to fall within the definition of 'state aid'?

If this was the case then there could, it seems, be an ability for parties adversely affected by such aid to seek recompense etc., under EU and national law - presumably from the public authority concerned?

In regard to the definition of 'public authority' I recall engaging with your colleagues (plus National Grid and others) about ten years ago on whether Code Administrator(s) / NGET, by virtue of the functions they perform (namely the legal / mandatory nature and the role of Ofgem in their work) display the characteristics, in law, of a 'public authority' or not. I attach a paper from the Ministry of Justice from around that time that may be helpful in that regard. Suggestions at that time were that a case could be made that Code Administrators could be considered as a 'public authority'.

2. Competition Law

In respect of competition law, I was thinking in terms of the distorting (and discriminatory) effect on competition that could arise where a company is applying to some parties mandatory obligations whilst not applying those same mandatory obligations to other parties where both sets of parties are identical.

I'm not certain that the respective approval of this by a Panel (or indeed GEMA?) can overwrite the need for the Code Administrator (such as Elexon or NGET) to comply with competition law generally, and Article 102 (TFEU) specifically.

One of the potential competition law concerns might include the possibility of 'an abuse of a dominate position' arising. Further information on this can be found by reference to the European Commission's factsheet –

http://ec.europa.eu/competition/publications/factsheets/antitrust_procedures_102_en.pdf

See, for example , the statement on page 1 of the factsheet about 'What is an Abuse':

"To be in a dominant position is not in itself illegal. A dominant company is entitled to compete on the merits as any other company. However, a dominant company has a special responsibility to ensure that its conduct does not distort competition. Examples of behaviour that may amount to an abuse include requiring that buyers purchase all units of a particular product only from the dominant company (exclusive purchasing); setting prices at a loss-making level (predation); refusing to supply input indispensable for competition in an ancillary market; charging excessive prices."

In this context I note the statement on page 2 of the factsheet which maybe relevant:-

"Victims' claims for damages: Any citizen or business which suffers harm as a result of a breach of the EU competition rules should be entitled to claim compensation from the party who caused it. This means that the victims of competition law infringements can bring an action for damages before the national courts."

In this regard, if such a situation occurred, then it would seem that the party who caused it could be NGET for the CUSC and Grid Code (plus Elexon for the BSC).

3. Affect on Cross Border trade

In respect of trade (noted under (1) above) on the face of it there is the potential risk, with the sandbox approach, that in offering a difference in approach to certain parties (be they generators, demand side response providers or demand) than other parties (who are the same type of undertakings) that this could have an affect on cross border trade; both with other Member States but also within the (UK) Member State (GB / Northern Ireland).

As I'm sure you appreciate, there are overarching requirements to ensure that there is no affect on cross border trade under EU law. This is helpfully summarised in a Commission Guideline, which can be found at:

<http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=LEGISSUM:l26113&from=EN>

In terms of the national codes (such as the CUSC, BSC, Grid Code, Distribution Code etc.,) and the need not to affect cross border trade; this legal obligation is, for example, set out in Regulation 714/2009 (the 'Third Package') at Article 8(7) in the following terms:

*"The network codes shall be developed for cross-border network issues and market integration issues and shall be without prejudice to the Member States' right to establish national network codes which do not affect cross-border trade."
[emphasis added]*

In addition to the three points I mentioned at the December Panel meeting I've also thought of another relevant item, namely in terms of the compatibility with the EU Network Codes / Guidelines.

4. EU derogation process

I notice that Elexon prepared some slides for the December GCRP (see attached). There are a number of references to 'derogations' in those slides, such as at Slides 3 and 5 (I've emphasised the text below):

"Regulatory sandboxes typically offer advice on innovative business models to help understand the frameworks within which they must operate, and derogations to specific aspects of the rules that could be deemed overly burdensome"

"The sandbox is not a thing or a place or a system – it is conceptual, a set of processes to facilitate the provision of advice or obtaining a derogation "

"Providing derogations requires a Modification to add provisions to the BSC"

"Subject to the approval of the workgroup, the derogations will be the responsibility of the BSC Panel, and ELEXON will support applications to derogation if necessary"

However, the CUSC deals (at a very high level) with two principle items, namely (i) the contractual arrangements for the connection etc., to the GB transmission system (NETS) and (ii) the 'connection' and 'use of system' charging arrangements for the GB transmission system (NETS).

Given the introduction of the new RfG Guideline connection regime from 18th May 2018 onwards (plus DCC and HVDC to follow) I cannot see how, for example, either the CUSC Panel (or the GCRP for that matter) can provide, legally, any derogation(s) for new connecting parties (or for existing parties who substantially modify) in terms of the RfG (of DCC or HVDC) requirements as this can only be granted by the NRA (Ofgem in the case of GB) and this power cannot be delegated (by the NRA) - in the sandbox case to either the CUSC or Grid Code Panel(s).

Furthermore, in terms of supporting innovation, the RfG was specifically drafted to take that into account. As you maybe aware, the RfG included a specific 'carve out' which permitted emerging (generator) technology providers to apply to the NRA to be allowed to sell their equipment based on the 'status quo' (pre RfG) connection conditions. Ofgem consulted on their approach, for GB, to dealing with emerging technology applications etc., in the autumn of last year. Therefore, it seems to me that the CUSC Panel would not be able to offer relief from the harmonised connection rules for new entrants via a sandbox approach.

As an aside, with respect to the Balancing Guideline, a similar derogation arrangement (as those for the three connection related Guidelines) is set out (in Article 62) which would, it seems, preclude the BSC Panel likewise being able to issue derogations to obligations arising from that Guideline. In this context, I know that my colleague Andy Colley (who I've copied into the email) is involved with the P362 BSC Workgroup which is considering

this and he may also be interested in your answers to the questions I've posed in this email.

Finally, in regard to this fourth item, I'll not dwell on the charging aspects of CUSC (as set out in the two methodologies contained in Section 14) as I assume; given Ofgem's duties under Article 37 (1) (a) and (6) (a) of Directive 2009/72; that any 'sandbox' type change(s) to charges to be paid could only be implemented by a CUSC Modification being raised in each case (rather than either the CUSC Panel or the Code Administrator or NGET directly themselves dis-applying the part(s) of Section 14 to certain parties) and being approved by Ofgem accordingly.

I'm sure that all these four items (and others) will have been considered in depth already by Ofgem prior to its sandbox initiative being presented and therefore the questions I'm asking can be quickly answered and my concerns allayed.

Ofgem Response

The below is an extract of Ofgem's response to the points raised by the CUSC panel member:

1. State aid

Under European Union rules it is illegal for EU countries to give financial help to some companies and not others in a way which would distort fair competition. This help is called "state aid", and the rules barring it are enforced by the European Commission and national courts. State aid is governed by the Treaty on the Functioning of the European Union (TFEU). Article 107(1) of TFEU states that "any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market".

This expression is often broken down into a four step test to help work out if an action will be "state aid". The CUSC Panel member email refers to government guidance which reiterates the four-part test. For State aid to exist, all four parts of the following test must be satisfied:

1. aid is granted by the transfer of state resources;
2. to a certain undertaking;
3. thereby creating a selective advantage; and
4. the transfer of resources distorts or has the potential to distort competition and trade between EU countries.

In the present circumstances the sandbox proposals would appear to fail the first of these four tests. To qualify as State aid the transfer in question must involve 'State resources'. This includes resources controlled by central and all local governments together with public or private bodies which use state resources. However, private funds do not normally constitute "state resources"; there must be a direct or indirect transfer of State resources for Art. 107 TFEU to apply. This general principle is obviously applicable to any derogation the BSC code may entail. Should that derogation result in a benefit to an undertaking that would not entail advantage of state resources; to the extent there is any relief from regulatory burden whatsoever the funds which underpin the Balancing Mechanism are generated by Elexon's customers, namely BSC Parties which are either Electricity

Generation or Supply Licence holders. For the first test to be satisfied there must also be a "transfer of resources". This can be positive, such as a grant or negative, such as a tax rebate or loan at less than market rates of interest. In either case the transfer improves the beneficiary's net financial position and has an impact on the state balance sheet. However, on the face of the facts the proposed sandbox neither positively distributes State resources nor does it imply that the State will forego resources that it would otherwise have benefitted from. The State bears no budgetary burden by reason of the Sandbox proposals and so the first limb or the four part test is not satisfied.

However, the position in respect of any additional government-based incentives will need to be considered on a case by case basis. The BSC includes provisions dealing with additional funds in the market which come directly from Government and which have been cleared by the EU Commission to ensure they are State aid compliant. For example, Capacity Market funds are "state resources" but are lawful (and not State aid) because they have been approved by the EU Commission. Should any application for a derogation have an appreciable impact on such pre-existing State aid clearance then each will need to be carefully considered on a case by case basis to determine if it would be compatible.

However, we understand that the Sandbox would contemplate temporary relief from an obligation of the BSC which, while relieving the undertaking in question of a burden, does not relate in any difference to the net financial position for the State and so does not, in principle, involve State aid. For the avoidance of doubt, having determined that that Regulatory Sandbox does not satisfy the first of the four parts of the test for the presence of State aid it is not necessary to consider the remaining elements of the test.

2. Competition Law

The CUSC Panel member email refers to Article 102 which relates to the abuse of a dominant market position. Both UK and EU competition law prohibit businesses with significant market power unfairly exploiting their strong market positions. To be in a position of dominance, a business must have the ability to act independently of its customers, competitors and consumers. Establishing if a company is dominant requires a complex assessment of a number of elements. However "dominance" means, generally, that a party has a dominant trading position in relation to a particular market. i.e that it is in a trading position of economic strength which enables it to prevent effective competition being maintained on the relevant market by affording it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers. Given the composition of the Panel, the balance that it seeks to achieve and Ofgem's ultimate oversight it does not appear that any one party would be in a position to exert its dominance through the derogations process (any more than it would in the normal conduct of the BSC).

3. Distortion of trade - Effect on cross border trade

It is unclear what the CUSC Panel member email is asserting under this heading. The guidelines which are referred and linked to in the email set out "guidelines on the effect on trade", but this is in respect of the application of that concept to breaches of competition law under Article 101 or 102 of the TFEU. In order to establish a breach of competition law under either Articles 101 (anti-competitive agreement) or 102 (dominance) it is necessary to have regard to whether the behaviour in question has an effect on cross-border trade. However if there is no anti-competitive agreement or abuse of dominant position there is no contravention which would have an appreciable effect on international trade. For the sake of completeness it is our view that there is little, if any, risk that the Ofgem sandbox or proposed P362 would appreciably affect intra-community trade. The UK market will remain open to that intra-community trade and the derogations process will be available

to those participating in the market. The derogations in question are understood to be short term and for specific purposes that will have no impact on cross –border trade or discriminate between EU operators.

4. EU Derogation Process

During our call it became apparent that there were 2 aspects of concern expressed under this heading:

Firstly, there was a concern that any derogation might seek to exempt one or more parties from requirements that were binding as a result of, for example, EU law. Derogations could not be permitted in circumstances where that would be outside the Panel's or Ofgem's authority. There will indeed be limitations to the extent of what a Sandbox can achieve. As observed it may not be within the gift of Elexon or CUSC or even Ofgem to issue derogations from any particular requirement, particularly if these are set by EU law or primary legislation. The example given in the email of "RfG Guideline connection regime from 18th May 2018" seems to be a reference, for example, to the implementation arrangements in place for EU Commission Regulation 2016/631 establishing network code on the requirement for grid connection of generators. Any derogation to the requirements of that EU regulation would need to be carefully considered and may well be outside what a derogation process can achieve. It is anticipated that, to the extent it would be possible to do so, parties would explore alternatives on order to make sure a derogation (if granted) still enabled compliance with the EU regulation or equivalent which was at stake.

Secondly, during the meeting, we touched on whether a code, in this case the BSC, could operate a derogation process without Ofgem (the Authority) becoming involved and/or ultimately approving of any particular derogation. From a policy perspective I do not think that Ofgem would welcome enabling an industry panel to permit derogations without a degree of control from Ofgem. From a legal perspective my preliminary thoughts are that to permit such an approach may be unlawful on the basis that it would fetter the Authority's discretion and/or purport to delegate the Authority's functions to a 3rd party. The Authority is given statutory authority to issue and modify the transmission licence. The licence itself obligates to licence holder to create the code and tightly controls the circumstance within which those codes may be modified, with the Authority ultimately approving modifications in each case. Whilst a derogation may be time-limited, for a set period of time and directed for the benefit of one or more parties it nevertheless would modify the effect of the code for that party for the duration of the derogation. There is an argument therefore that a "derogation" is a type of modification, the delegation of which to 3rd party would be to delegate an important part of the Authority's functions. We think that from a policy and legal perspective it is important that the Authority retains ultimate direction over the derogations process. We have since seen a draft of p362, which would appear to recognise these principles at 10.1.1 which would give the Authority ultimate control over derogations.

To conclude, the CUSC panel member's email sets out several relevant considerations which will need to be borne in mind when the Panel, and the Authority, considers any derogation. However these legal considerations need not, in principle, imply that a "sandbox" approach to the BSC is impermissible. Such derogations will be considered on a case by case basis, not just to ensure that the relevant policy considerations are taken into consideration but to ensure that the derogation does not contravene the relevant legal considerations.