



Stage 04: Final Mod Report

What stage is this document in the process?

01 Initial Written Assessment

02 Definition Procedure

03 Assessment Procedure

▶ 04 Report Phase

P248:

Aligning BSC interest calculation requirements with the FAA calculation method and P235 principles

P248 proposes to bring the BSC requirements for four FAA interest calculations in line with the principles of accuracy and fairness established by P235.



The BSC Panel recommends:
P248 should be approved with a retrospective Implementation Date of 27 March 2001



Impact of approving this modification: **Low**
This modification will align the Code with the calculation which the Funds Administration Agent already uses



Impact of rejecting this modification: **High**
Rejection could result in system and process changes for the Funds Administration Agent and for BSC Parties

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Any questions?

Contact:
Bu-Ke Qian



bu-
ke.qian@elexon.co.uk



020 7380 4146

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About this document:

This document is a **Final Modification Report**, which ELEXON has submitted to the Authority on the Panel's behalf. The Authority will consider the Panel's recommendations which are set out in this report and will issue a decision letter to either approve or reject the change.

You can download further P248 documents [here](#), including the Initial Written Assessment Report and copies of the full industry responses to Report Phase Consultation.

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Why Change?

The Authority approved Modification Proposal [P235](#) on 30 June 2009, with a retrospective Implementation Date of 27 March 2001 (NETA¹ Go-Live).

Although Modification P235 removed the uncertainty over the method used by the Funds Administration Agent (FAA) to calculate interest on **Reconciliation Charges**, its scope was limited to that one calculation. ELEXON has therefore been investigating whether any of the other interest calculations specified in the BSC require clarification.

Solution

The proposed solution is to amend the affected interest calculations in the relevant BSC sections. For the exact Code drafting please refer to Attachment B of this document.

Impacts & Costs

Approving this Modification Proposal will have no impact on BSC Agents' or BSC Parties' systems and processes. This is because it will align the BSC with the calculations which the FAA already uses. The FAA's impact assessment results confirm that there is no cost associated with the change if Modification P248 is approved.

However, rejecting this Modification Proposal could result in costs to the FAA (and possibly to Parties) to align systems and processes with the BSC. It could also result in the risk and costs of calculations being challenged through the Trading Disputes process. The FAA have estimated such costs to be around **£82K**. Detailed costs can be found in Section 4 of this document.

The only costs of implementing P248 will therefore be **3 man days** of ELEXON effort (equating to £720) to update the Code and the FAA Service Description (based on the Code drafting).

Implementation

The Panel recommends that the modification should be implemented **retrospectively** back to NETA Go-Live on 27 March 2001.

The Case for Change

To align the BSC with the actual method undertaken by the FAA will remove any confusion over how interest is calculated, and will provide clarity to participants. This will promote transparency and efficiency, thereby better facilitating Applicable BSC Objective (d).

Recommendations

The Panel unanimously recommends that P248 should be approved.

¹ The New Electricity Trading Arrangements (NETA) replaced the previous Electricity Pool arrangements in 2001.

2 Why Change?

Background

Modification P235

The Authority approved Modification Proposal [P235](#) on 30 June 2009, with a retrospective Implementation Date of 27 March 2001 (NETA² Go-Live).

P235 brought the BSC requirements for calculating interest on **Reconciliation Charges** in line with the actual calculations which the Funds Administration Agent (FAA) has used since NETA Go-Live.

The BSC was amended to clarify that interest on Reconciliation Charges should be calculated:

- Over the period from (and including) the Payment Date of the corresponding Initial Settlement Run, up to (but excluding) the Payment Date of the current Reconciliation Run;
- On a daily compound basis (i.e. the amount on which interest is calculated for each day in the above period includes the accumulated interest levied on previous days); and
- Using the applicable Base Rate for each day in the calculation period (thereby taking account of any changes in the Base Rate during this period).

The P235 Modification Group considered in detail the principles underlying the calculation of reconciliation interest and concluded that:

- The calculation of interest should reflect the principle behind the BSC's Reconciliation process (that Reconciliation Charges should adjust BSC Parties' payments as if the 'correct' monies had been exchanged on the Payment Date of the Initial Settlement Run), and the **time value** of money to Parties³; and
- The actual FAA calculations more fairly and/or accurately reflected this principle.

Although Modification P235 removed the uncertainty over the method used by FAA to calculate interest on **Reconciliation Charges**, its scope was limited to that one calculation. ELEXON has therefore been investigating whether any of the other interest calculations specified in the BSC require clarification.

Interest Calculation Issues

We have identified a further 4 calculations that are unclear on how interest is calculated. These calculations are for:

- 1) Interest on Ad-Hoc Trading Charges relating to **Extra-Settlement Determinations** (ESDs). In particular, Section U2.2.3(i) of the BSC requires interest to be calculated if an ESD is followed by a subsequent Settlement Run for the same Settlement Day;
- 2) Interest on payments relating to Contingency Provisions (i.e. Black Start, Manifest Errors, and Q8 compensation);
- 3) Interest relating to Initial Settlement Runs for which the Payment Date is delayed by more than a week; and
- 4) Interest relating to late payment of Trading Charges ('Payment Defaults').

² The New Electricity Trading Arrangements (NETA) replaced the previous Electricity Pool arrangements in 2001.

³ The 'time value' (sometimes called the 'earning value') of money means the principle that it is better to receive an amount of money today rather than an equal amount in the future, because of the interest that can be earned on it between now and then. So Parties who have overpaid at the Initial Settlement Run or subsequent runs should be compensated (through interest) for the loss of use of their money during the period of overpayment. Similarly, Parties who have initially underpaid should pay interest for the period of the underpayment, to reflect their ability to use money which they would not otherwise have had.



Reconciliation Charges

Reconciliation Charges are the adjustments made to a Party's Trading Charges following a Reconciliation Run. These adjustments are intended to make it as if the metered data determined at that Reconciliation Run had been submitted at the Initial Settlement Run.



What is an ESD?

An ESD is a determination, outside Volume Allocation Runs and Settlement Runs, of Trading Charges (or adjustment and apportionment in respect thereof), required to be carried out by the Panel.

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Although the identified calculations are varied in nature, they all arise as a result of Trading Charges being amended and/or paid after the Payment Date of the Initial Settlement Run. The principles agreed by the P235 Modification Group for interest on Reconciliation Charges should therefore also apply to these calculations.

The following two aspects of the current BSC requirements for these calculations do not reflect the P235 principles of fairness and/or accuracy:

1) The BSC does not make it clear that interest should be calculated on a daily compound basis, using the interest rate applicable to each day.

This issue affects the:

- ESD provisions in U2.2.3(i);
- Contingency Provisions for Black Start in G3.3.6(a), Manifest Errors in Q7.6.5(a) and Outage Compensation in Q8.3.1(b);
- Postponed Initial Settlement Run provisions in N6.6.2; and
- Non-paying BSC Debtors provisions in N9.4.1.

The current BSC wording could be read as implying the use of 'simple interest'. This would mean that the amount on which interest is charged would remain the same for each day in the calculation period, ignoring any interest accumulated on previous days. The BSC could also be read as implying (although it is somewhat ambiguous) that a single Base Rate should be applied to the whole calculation period, ignoring any changes in the Base Rate during that period.

This would not accurately reflect the principle behind adjusting Trading Charges or the time value of money to BSC Parties.

2) The ESD provisions in U2.2.3(i) state that, where an ESD is followed by a subsequent Settlement Run for the same Settlement Day, interest should be calculated for the period from the Payment Date of the ESD 'to the Payment Date in respect of such Settlement Run'.

When interpreted in conjunction with X2.3.1⁴ this implies that the period for which interest is calculated includes, rather than excludes, the Payment Date of the current Reconciliation Run.

While the materiality of this issue is small, the BSC requirement represents an (albeit minimal) over-calculation of interest. This is because Parties have until the end of the Payment Date to make payment, and any payment does not become overdue until the following day.

⁴ X2.3.1 says that where any period under the BSC is to run to a given day, such period shall run to the end of that day.

Overview

The Panel raised Modification P248 to bring the BSC's requirements for these four further FAA interest calculations in line with the principles of accuracy and fairness established by the P235 Modification Group.

The FAA's actual calculations are already consistent with the P235 principles. This Modification Proposal will therefore **not impact current processes**. Rather it will, like P235, bring the BSC in line with established industry practice.

The Panel recommends that P248 should have a **retrospective Implementation Date** of NETA Go-Live, for the same reasons as the Modification Group and the Panel put forward for P235. These are that calculating interest on a compound basis has always been the intended and correct method, and that confirming this retrospectively would protect Parties from the risk and cost of calculations being challenged through the Trading Disputes process. The P235 Group and the Panel agreed that, while retrospective changes are normally to be avoided, in these specific circumstances retrospection would remove (rather than create) uncertainty.

Proposed Solution

Modification P248 seeks to amend the interest calculations set out below.

Provisions affected by issues identified in Section 2	Solution
ESD provisions	Amend Section U2.2.3(i) of the BSC
Contingency Provisions for Black Start, Manifest Errors and Outage Compensation	Amend Section G3.3.6(a), Q7.6.5(a) and Q8.3.1(b) of the BSC
Postponed Initial Settlement Run	Amend Section N6.6.2 of the BSC
Non-paying BSC Debtors	Amend Section N9.4.1 of the BSC

For more information, please refer to the Proposed Draft Legal Text in Attachment B to this document.

Materiality

Given the relatively low materiality of the issues described in Section 2 (compared to that addressed by P235), they have been seen until now as low priority.

Interest Calculations	Frequency
1) Ad-Hoc Trading Charges relating to ESDs	Seldom exercised
2) Payments relating to Contingency Provisions (i.e. Black Start, Q8 Compensation)	Infrequent (less than 4 times a year)
3) Initial Settlement Runs for which the Payment Date is delayed by more than a week	Seldom exercised
4) Late payment of Trading Charges ('Payment Defaults')	Any frequency The value of interest incurred is minimal ⁵

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⁵ The values of interest incurred in the March 09 Quarter and September 09 Quarter are equal to £260 and £1,250 respectively across all Parties.

Self-evident change

The BSC Panel has the ability to progress a Modification straight to the Report Phase where the recommendation which the Panel should make to the Authority in relation to such Modification Proposal would generally be considered to be self evident (BSC paragraph F2.2.4).

The Panel believes Modification P248 is a self-evident change on this basis because:

- The principle of aligning BSC interest calculation requirements with FAA calculation methods was agreed under Modification P235, which aligned the BSC requirements and interest calculation methods with regard to Reconciliation Settlement Runs;
- P248 seeks to address the remaining interest provisions in the Code using the same calculation principles established by P235;
- The material impact of P248 is minimal due to the infrequent use of the remaining interest provisions; and
- The retrospective implementation approach utilised by P235 was unanimously supported by the industry (click [here](#) for a copy of the P235 Report Phase Consultation Responses).

The Panel has therefore submitted this Modification directly to the Report Phase under paragraph F2.2.3(b)(iii) of the Code.



What is a self-evident change?

The Panel would usually proceed a change directly to the Report Phase where the Modification Proposal is of a minor or inconsequential nature and/or where the recommendation which the Panel should make to the Authority in relation to such Modification Proposal would generally be considered to be **self-evident**.

4 Impacts & Costs

Impacts

Impact on BSC Systems and process

None identified, as P248 will align the BSC with the FAA's existing calculations.

Impact on BSC Agent/service provider contractual arrangements

None identified (if P248 approved).

Impact on BSC Parties and Party Agents

Approving this Modification Proposal will have no impact on BSC Parties' systems and processes. This is because it will align the BSC with the calculations which the FAA already uses.

However, rejecting this Modification Proposal could result in costs to the FAA (and possibly to Parties) to align systems and processes with the BSC. It could also result in the risk and costs of calculations being challenged through the Trading Disputes process.

Impact on Transmission Company

None identified.

Impact on ELEXON

None identified.

Impact on Code

- ESD provisions in **U2.2.3(i)**;
- Contingency Provisions for Black Start in **G3.3.6(a)**, Manifest Errors in **Q7.6.5(a)** and Outage Compensation in **Q8.3.1(b)**;
- Postponed Initial Settlement Run provisions in **N6.6.2**;
- Non-paying BSC Debtors provisions in **N9.4.1**

Impact on Code Subsidiary Documents

Changes will also be needed to the FAA Service Description, which is based on the current BSC wording.

Impact on Core Industry Documents and other documents

None identified.

Impact on other Configurable Items

None identified.

Costs

Estimated implementation costs	
Service Provider impact assessment costs	£0
ELEXON resource	3 man days, equating to £720

FAA's Impact Assessment Results

Breakdown	Costs if P248 is <u>approved</u>	Costs if P248 is <u>rejected</u>
BPO	zero	£17.5K (indicative)
AMD	zero	£65.1K (indicative)

The FAA's Impact Assessment indicated that:

- **Approval** of P248 will not impact any of the FAA systems or processes as approval will align the BSC with the calculations that FAA already uses. Therefore no Application Management and Development (AMD) work would be required. There will be no BPO or AMD costs if P248 is approved;
- **Rejection** of P248 will require system changes to interest calculations, imply a retrospective recalculation of billed interest payments, and an exercise to re-bill interest overpayments and underpayments. The total cost associated with work required is £82K (indicative).

5 Implementation

The Panel agreed with ELEXON's recommendation that the modification would be implemented **retrospectively** back to NETA Go-Live on 27 March 2001.

Under this approach it would be as if the inconsistencies between the FAA interest calculations and the Code had never occurred. If approved, Parties could not raise Trading Disputes against these interest calculations (past or future).

For changes to the FAA Service Description, we will update the Service Description in the next available Release to follow the Authority's approval of the modification. The Service Description is not a priority, as the provisions of the Code take precedence and we would simply be amend the document to mirror the Code.

6 The Case for Change

This Modification would align the BSC with the actual calculation method undertaken by the FAA, whose method of calculating interest is fairer and/or more accurate than the method detailed in the BSC.

To align the BSC with the actual method undertaken by the FAA will remove any confusion over how interest is calculated, and will provide clarity to participants. This will promote transparency and efficiency, thereby better facilitating Applicable BSC Objective (d).

The Panel unanimously agrees that P248 will better facilitate the achievement of Applicable BSC Objectives (d).



Description of BSC Objectives

- a) Efficient discharge of the obligations of the Transmission Licence.
- b) Efficient, economic and co-ordinated operation of the national electricity transmission system.
- c) Promoting effective competition in the generation and supply of electricity and in the sale and purchase of electricity.
- d) Promoting efficiency in the implementation and administration of the balancing and settlement arrangements.

Panel's consideration of Initial Written Assessment

The Panel considered the recommendation to raise P248 at its meeting on 10 December 2009. (You can find a copy of the P248 IWA [here](#))

The Panel **unanimously** agreed that:

- P248 will better facilitate the achievement of **Applicable BSC Objective (d)**;
- A retrospective Implementation Date of NETA 'Go-Live' is appropriate, as it will protect Parties from the risk and cost of calculations being challenged through the Trading Disputes process; and
- The draft Legal Text delivers the P248 solution.

The Panel's initial unanimous recommendation was therefore that P248 should be approved.

The Panel did not raise any additional views or comments.

8 Report Phase Consultation Responses

ELEXON consulted on the Panel's initial recommendations during the Report Phase.

The following table summarises the consultation responses which ELEXON received. You can download the full individual responses to this Report Phase Consultation, [here](#).

Question		Responses
1	Do you agree with the Panel's initial recommendation that P248 will better facilitate the achievement of Applicable BSC Objectives (d) when compared with the existing BSC requirements, and that P248 should therefore be approved?	4 Yes - Unanimous 0 No
2	Do you agree with the Panel's suggestion that P248 should be implemented retrospectively back to NETA Go-Live on 27 March 2001?	4 Yes - Unanimous 0 No
3	Do you agree that the Legal Text delivers the intention of P248?	3 Yes - Unanimous 1 Neutral ⁶
4	Do you have any further comments on P248?	0 Yes 4 No - Unanimous

Did respondents support the Panel's recommendations?

Yes, all respondents unanimously supported the Panel's initial recommendations. No new arguments were raised.

Additional Clarifications on Proposed Legal Text

One respondent agreed with the intention of the P248 Legal Text, but raised some queries on how certain areas of the text deliver this intention. ELEXON has clarified each of these areas with the respondent, and the respondent is happy to accept ELEXON's view that the text delivers the intention of the modification. A summary of these discussions are provided below.

- Is there any difference between the "Default Rate" (proposed to be eliminated) and the "Default Interest Rate" in relation to interest payments?

We confirmed the existing text has two definitions of a default interest rate and the new P248 text rationalises this to a single definition consistent with the application of default interest.

- Should proposed U2.2.3(i)(i)(2) make clear that the interest is in relation to the amount originally transferred in an ESD(which is being effectively undone because a subsequent settlement reconciliation r has fully accounted for the relevant correction and interest), and not the amount being transferred referred to in paragraph (1)?

We confirmed that the interest is paid on the amount transferred pursuant to the Extra Settlement Determination on the basis that interest is paid on the 'extra-settlement amount' which is the amount payable pursuant to an Extra Settlement Determination.

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⁶ The respondent who feels neutral about the Legal Text agrees with the intention of the text.

We further confirmed that the intention of the Legal Text is that interest assumed to be foregone by a Party as a result of an initial ESD payment, shall be received by the Party with any subsequent reversal of the ESD payment. Any interest assumed to be earned by a Party as a result of an initial ESD receipt by it shall be paid by the Party with any subsequent reversal of the ESD receipt.

- Should the clause specify interest from the actual payment date rather than the date on which the payment was due?

We responded that if a Party does not pay on the due date and therefore defaults on payment, interest on the amount in default will be calculated separately using the Default Interest Rate under Section N9.4. With respect to the FAA, it has never made a late payment and any such late payment would fall outside the scope of P248.

The respondent is happy with the clarifications above. All the other respondents all support that the Proposed Legal Text aligns the BSC with current commercially correct practice.

During the industry consultation, we also took the opportunity to review the proposed Legal Text and identified one minor numbering error. Please note the only changes are to the numbering 6.6.2A that was an error in the drafting. The updated Proposed Legal Text can be found in Attachment B.

9 Panel's Final Views and Recommendations

The Panel considered the Report Phase Consultation responses and the Draft Modification Report at its meeting on 14 January 2010.

The Panel:

- Noted the comments from respondents and that there were no new arguments; and
- Continued to unanimously support the Proposed Modification.

The Panel therefore unanimously recommends to the Authority:

- That Proposed Modification P248 **should** be made;
- An Implementation Date for Proposed Modification P248 to be:
 - 27 March 2001 (NETA Go-Live) for BSC changes
 - Next available Release follow the Authority's approval for changes to FAA Service Description; and
- The Legal Text for Proposed Modification P248 (as contained in Attachment B).



Recommendation

The Panel's final unanimous recommendation is that the Proposed Modification P248 should be made with an implementation date of 27 March 2001.

10 Further Information

More information is available in:

Attachment **A**: Modification Proposal

Attachment **B**: Legal Text Proposed

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