

## MP Form

<b>Modification Proposal – BSCP40/06</b>	MP No: 207 (mandatory by BSCCo)
<b>Title of Modification Proposal</b> ( <i>mandatory by originator</i> ): Introduction of a new governance regime to allow a risk based Performance Assurance Framework (PAF) to be utilised and reinforce the effectiveness of the current PAF	
<b>Submission Date</b> ( <i>mandatory by originator</i> ): <b>29 September 2006</b>	
<b>Description of Proposed Modification</b> ( <i>mandatory by originator</i> )  This Modification proposes to introduce appropriate new governance arrangements to allow a risk based Performance Assurance Framework (PAF) to be utilised and to reinforce the effectiveness of the current PAF. It builds on the work undertaken in the recent PAF Review.  First the proposal requires a statement in the Code that defines the purpose of the SVA assurance arrangements. Such a statement is to be in the form of SVA Assurance Objectives and is to be effectively the same as points (A) and (B) below:  <i>The SVA Assurance regime should provide assurance that:</i>  <i>A) energy is allocated efficiently and equitably between Suppliers, to an acceptable level of accuracy, that is derived from the aggregated consumption of Metering Systems for which each Supplier is responsible; and</i>  <i>B) participants act as good stewards of Metering System data, delivering efficient and effective transfer of this data between Suppliers and Supplier Hubs and supporting the equitable allocation of energy.</i>  In addition, the proposal will introduce two new roles which could be called (and for the purposes of this proposal shall be called) the Risk Evaluation Group (REG) and the Risk Assurance Board (RAB). These roles may be performed by creating new Panel Committees or by modifying the role of an existing Panel Committee such as the Performance Assurance Board (PAB). Potentially the roles could be carried out by one or two different Panel Committees, however, if it is able to be one, the Panel Committee must have the two roles distinctly and separately detailed in the Code.  The REG would be responsible for identifying, assessing and prioritising the risks that occur in the SVA market on the basis of their potential impact on the achievement of the SVA Assurance Objectives set out above. The general nature of the REG's functions/roles shall be contained in the Code and this shall include a requirement for the REG to consult with the industry on its proposed conclusions. The methodology for identifying, assessing and prioritising risk will be devised by the REG at its discretion. The REG would also recommend the level of performance standards that are applicable to Suppliers and their Agents.	

## Modification Proposal – BSCP40/06

MP No: 207  
(mandatory by  
BSCCo)

The RAB would be responsible for developing and delivering an operational plan detailing which assurance techniques from the current assurance techniques are to be deployed as against those risks which have already been identified by the REG. The RAB will also be able to determine at its discretion those participants in respect of whom particular assurance techniques should be utilised. The general nature of the RAB's functions/roles shall be contained in the Code.

It would be for the Modification Group to consider whether the REG and the RAB ought to be two distinct bodies with different memberships and whether the current PAB could evolve into the RAB to provide continuity from the current arrangements.

The REG (and possibly in some circumstances the RAB) would be able to raise Modifications or make recommendations to the BSC Panel that changes to the Code or Code Subsidiary Documents (CSDs) should be made. Such proposals could be in respect of assurance matters, including but not limited to performance standards and/or in relation to the suite of assurance techniques which are to be deployed.

Given that a new governance regime is being proposed in respect of the PAF, changes will also be required to the Code to remove any incompatible existing governance arrangements relating to the current PAF, including those functions currently performed by the Performance Assurance Board (PAB).

This proposal also seeks to ensure that the effectiveness of the assurance framework would be evaluated and reported to BSC Parties on a regular basis (potentially annually).

The role of the BSC Panel under the proposed governance regime would, amongst other things, be to oversee the delivery of the regime and could act as a point of escalation in respect of participants who continuously breach the Code (i.e. are in continuous or repeated non-compliance).

A possible example of the practical application of the risk based assurance regime is attached to this proposal at Appendix A (this proposal was drafted by the Core Working Group (CWG) and was included in the PAF Final Report as Appendix F).

The new governance arrangements when introduced will utilise and apply the current assurance techniques available under the Code. Changes to such techniques will therefore be required only to the extent necessary to ensure that the current assurance techniques are compatible and are able to be deployed with the new governance arrangements and the risk based approach described in the proposal.

To avoid any doubt, it is not the intention that new assurance techniques or substantially amended current assurance techniques are introduced via this proposal. Any additional assurance techniques or substantially altered assurance techniques would need to be introduced via separate Modifications and Change Proposals.

## Modification Proposal – BSCP40/06

MP No: 207  
(mandatory by  
BSCCo)

It is envisaged that the performance assurance of CVA Systems would also fall under the remit of the new governance regime as to have two separate governance and assurance regimes would be less efficient and effective and would give rise to an element of duplication and inconsistency in the treatment of like situations. It may be that in order to define the purpose of the CVA Systems assurance a CVA Assurance Objective(s) will need to be developed to provide guidance.

### **Description of Issue or Defect that Modification Proposal Seeks to Address** (*mandatory by originator*)

Since 1998, considerable experience has been gained regarding the operation of the SVA arrangements. Over this time, however, there have still been a number of significant issues that have arisen which materially impact the accuracy of Settlement. In addition, there have been a multitude of non-compliances where the significance or materiality or risk in relation to Settlement is thought to be low.

A review of the PAF was launched in August 2005. The CWG carrying out this review concluded that there are weaknesses in the current PAF which justify change, particularly in the way assurance is governed.

By way of background, the circumstances within which the PAF operates have changed considerably since the SVA arrangements were originally designed. At that time there was a need to mitigate possible risks arising from the initial implementation of a completely new set of industry processes; there was also uncertainty over how Suppliers would operate under the new arrangements.

A comprehensive PAF was therefore put in place, with considerable emphasis on ensuring compliance with all aspects of the SVA arrangements by Suppliers and their Agents. With the advent of the New Electricity Trading Arrangements (NETA), this framework was transferred into the Code.

Consequently, the BSC Panel, the PAB and the associated PAF techniques are constrained in their operation by requirements set out in the Code and CSDs. These requirements oblige the BSC Panel and the PAB to monitor and audit compliance by participants with all aspects of the Code and to subsequently provide specific notifications and take defined actions in respect of all identified breaches of (i.e. non-compliance with) the Code. A governance regime and more tailored application of the assurance regime of the nature described in this proposal would be more efficient, effective and deliver better value as it would be able to take into account, as a priority, those significant or material issues and/or non-compliances and apply the relevant assurance techniques in a more focussed and productive way.

Further, the Code contains no clear objectives against which to assess, on a continuing basis, whether the various non-compliances are significant. As such, under the current PAF it can be difficult to establish the significance of identified non-compliances, and the PAB has little discretion in choosing to disregard non-compliances (or give them a lower priority) where the significance, materiality, or risk to Settlement is low.

<b>Modification Proposal – BSCP40/06</b>	MP No: 207 (mandatory by BSCCo)
<p>The existing PAF is therefore considered to be inflexible, and does not necessarily focus on the most important issues. The Proposer considers that one outcome of this is that a number of important issues have remained unresolved over several years.</p> <p>The governance arrangements therefore should not only be flexible enough so that they can identify those risk areas which are seen as a priority but also be flexible enough so that its governing authority is able to deploy a flexible set of assurance techniques in a proportionate manner against those risks. This could be seen as more adaptable, effective and efficient.</p> <p>It is noted though that participants would still be obliged to comply with the Code and CSDs.</p> <p>The performance assurance of the CVA Systems would be better facilitated if they fell under the remit of the REG and RAB as it is felt that it would be inappropriate to have two different governance arrangements under the Code for performance assurance. A consistent approach to the SVA and CVA assurance regimes would be more effective and efficient.</p>	
<p><b>Impact on Code</b> <i>(optional by originator)</i></p> <p>Changes are potentially required to the following sections of the Code:</p> <ul style="list-style-type: none"> <li>▪ Section B and Annex B-1</li> <li>▪ Section C</li> <li>▪ Section H</li> <li>▪ Section J</li> <li>▪ Section L</li> <li>▪ Section S and Annex S-1</li> <li>▪ Section W</li> </ul>	
<p><b>Impact on Core Industry Documents or System Operator-Transmission Owner Code</b> <i>(optional by originator)</i></p> <p>None Identified</p>	
<p><b>Impact on BSC Systems and Other Relevant Systems and Processes Used by Parties</b> <i>(optional by originator)</i></p> <p>None identified</p>	

## Modification Proposal – BSCP40/06

MP No: 207  
(mandatory by  
BSCCo)

### **Impact on other Configurable Items** (*optional by originator*)

Changes are potentially required to all assurance related CSDs to ensure that a new governance regime which utilises a risk based approach is able to be deployed and further given this the current assurance techniques will also need to be compatible with the risk based approach. The current assurance related CSDs identified to date are:

- BSCP533 ‘PARMS Data Provision’
- BSCP534 ‘PARMS Techniques’
- BSCP535 ‘Technical Assurance’
- BSCP536 ‘Supplier Charges’
- BSCP27 ‘Technical Assurance of Half Hourly Metering Systems for Settlement Purposes’.

Note that the CSDs relating to Entry Processes, Accreditation and Certification have not been included in this list since they are due to be withdrawn with the implementation of Approved Modification P197 ‘SVA Qualification Processes Review’.

It may also be necessary to include a reference to the effect that the new governance regime is to follow a risk based assurance approach in a new or existing CSD.

<b>Modification Proposal – BSCP40/06</b>	MP No: 207 (mandatory by BSCCo)
<p><b>Justification for Proposed Modification with Reference to Applicable BSC Objectives</b> <i>(mandatory by originator)</i></p> <p>The risk-based assurance regime to be governed by the REG and the RAB (as described above) is considered to better facilitate Applicable BSC Objective (c) ‘The promotion of 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’ by providing assurance that the REG and the RAB are able to identify and highlight risks which are seen as significant or material and hence that participants in the SVA arrangements concentrate efforts on resolving such risks such that:</p> <ul style="list-style-type: none"> <li>▪ the transfer of Metering Systems between Supplier Hubs is underpinned by improved data quality; and</li> <li>▪ energy is allocated equitably between Suppliers.</li> </ul> <p>Compliance with the requirements will be monitored by the REG/RAB. Over the course of time, addressing significant or material risks should make the Settlement process more efficient, reducing the overall costs of market operation. It should also encourage entry into the market of new participants with more robust systems and processes as their awareness of the materiality of existing risks would allow them to address, or, at the very least, mitigate those risks prior to market entry.</p> <p>Including the performance assurance of the CVA Systems under the REG and RAB would be seen to enhance its performance assurance as it would be consistent with the SVA arrangements and therefore be more effective and efficient. As a result it would promote more effective competition.</p>	
<p><b><u>Urgency Recommended: Yes / No</u></b> <i>(delete as appropriate) (optional by originator)</i> No</p>	
<p><b><u>Justification for Urgency Recommendation</u></b> <i>(mandatory by originator if recommending progression as an Urgent Modification Proposal)</i> N/A</p>	
<p><b>Details of Proposer:</b></p> <p><i>Name.....Carole Pitkeathley.....</i></p> <p><i>Organisation...energywatch.....</i></p> <p><i>Telephone Number.....0191 221 2072.....</i></p> <p><i>Email</i> <i>Address.....carole.pikeathley@energywatch.org.uk.....</i></p>	

**Modification Proposal – BSCP40/06**

MP No: 207  
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**Details of Representative’s Alternate:**

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...*

*Organisation.....  
.....*

*Telephone  
Number.....*

*Email  
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**Attachments: Yes / No** *(delete as appropriate) (mandatory by originator)*

**If Yes, Title and No. of Pages of Each Attachment:**

## APPENDIX A

### **Overview of Governance Arrangements of a Risk Based Assurance Regime**

#### **1. Governance Overview**

The proposed assurance framework is founded explicitly on the basis of ongoing risk identification, risk evaluation, and risk mitigation. The governance arrangements described below have been developed to enable an agreed set of assurance techniques to be deployed to mitigate the risk that SVA Assurance Objectives are not met.

Risk identification and evaluation would, in effect, provide a map of the level of risk across the SVA arrangements. A set of assurance techniques would then be chosen for deployment to mitigate the identified risks. Some of these techniques might be deployed across the SVA arrangements as a whole, whilst others, reflecting a further risk assessment, might focus on individual participants (or type of participant).

Transparency would be of particular importance in building confidence that the assurance framework was being operated impartially and efficiently. The outcome of the risk assurance programme would be monitored and the results fed back into the risk identification and evaluation process.

#### **BSC Panel**

The role of the Panel would be to oversee the delivery of the assurance framework and to approve the key deliverables produced. The Panel would also act as a point of escalation for resolving issues. It may be envisaged that the Panel would also deal with participants that:

- fail to comply with the assurance framework;
- make an unacceptable contribution to the risk to SVA Assurance Objectives;  
or
- impact the SVA Assurance Objectives in a material or persistent way.

The CWG noted that it might be valuable to distinguish between the role of a “Risk Evaluation Group” (REG), whose task would be to reach a view on the significance of risks facing the SVA arrangements, and the role of a “Risk Assurance Board” (RAB) whose task it would be to deploy the appropriate assurance techniques required to mitigate these identified risks. The CWG noted that it need not be assumed that two separate bodies would perform these roles, or that it would be necessary to establish, for example, new BSC Panel committees; these would be matters for further consideration.



### Risk Evaluation Group (REG)

This strategic role would be responsible for the identification and evaluation of key risks to the SVA Assurance Objectives that may arise from the processes set out in the BSC. The REG would be able to regularly assess the requirements for assurance, and would be able to take account of the views of Suppliers about the importance of particular issues.

The REG would be able to promote the development of the assurance regime by raising Modification Proposals or Change Requests, or at the very least be able to make recommendations to the Panel in this regard, for industry consideration as required. The CWG anticipates that this responsibility would be limited to matters of assurance rather than the Balancing and Settlement Arrangements as set out under the BSC. In this way the REG could adapt the techniques available for deployment by the RAB (see below) and the standards to which participants were measured in order to adapt the assurance regime to the changing needs of the industry.

It is envisaged that meetings of the REG would be held in open session and that industry participants would be able to comment on the work of the group through a process of formal consultation. The constitution of this group could comprise either:

- elected or Panel-appointed members that acted as independent experts reflecting an appropriate cross-section of industry participant functions; or
- Panel-appointed representatives from Trading Party organisations, each member representing his or her Trading Party.

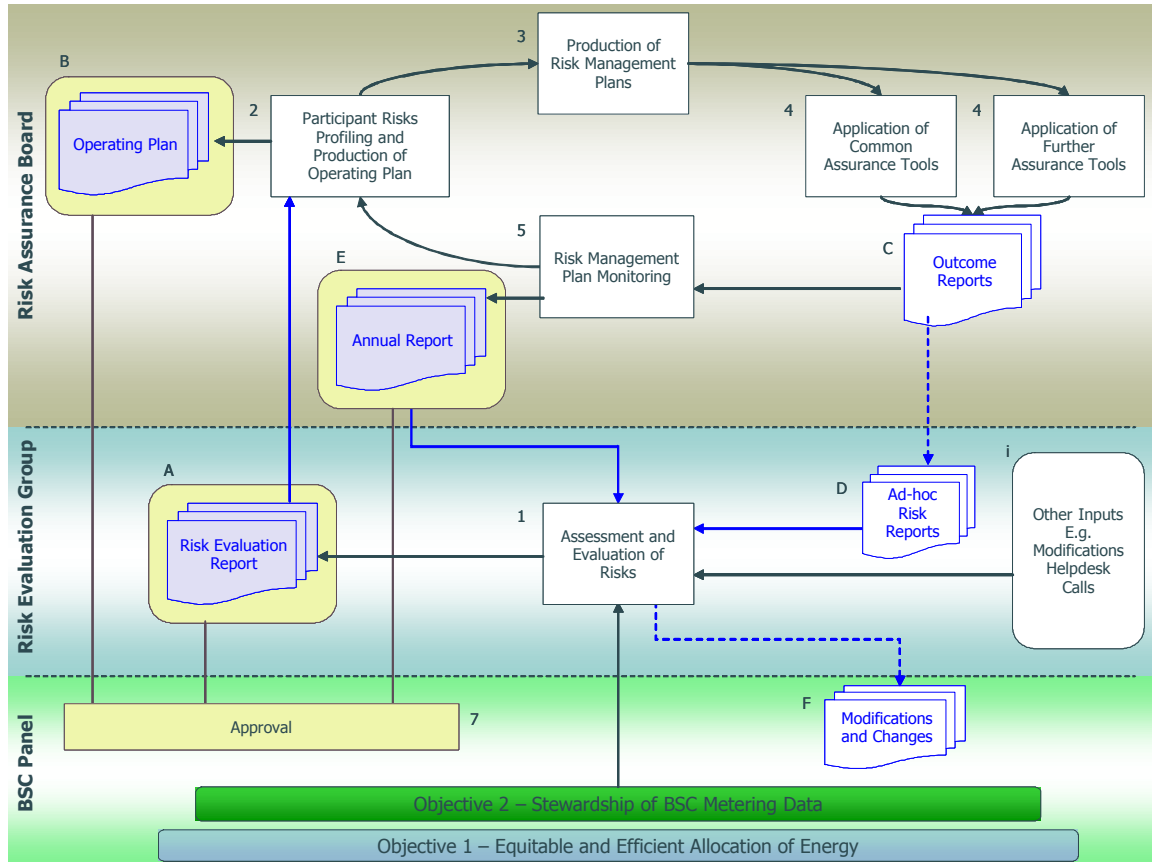
### Risk Assurance Board (RAB)

This operational role would be responsible for the development and delivery of an operational plan designed to manage the risks identified by the REG. This work would encompass the application of the assurance techniques. It is envisaged that the flexibility of the risk-based assurance regime would be founded in the RAB's ability to deploy assurance techniques according to risk and that these responsibilities would be enabled by the BSC.

Much of the RAB's work would be confidential and meetings would be held in closed session. Members would act independently; that is, when appointed to the board by the Panel their role is that of industry expert; members would not represent the interests of their employer.

## **2. Operation Overview**

The diagram below sets out one possibility for the practical application of a risk-based assurance regime under the governance set out above. Several key deliverables are referenced in this diagram. Each is described in the following section.



### Phase 1: Identification and Evaluation of Risks

This task would be performed by the REG and would result in the production of a Risk Evaluation Report (RER). The REG would be responsible for the production of this report. Members of the industry would have an opportunity to contribute to the report through the formal consultation that would take place (at least once every year). Any changes to the SVA arrangements that are introduced each year (either via a Modification or a Change Proposal) would be reviewed by the REG and their impact on the RER would be assessed. In addition, whenever an Ad-hoc Risk Report is produced its impact on the RER would also be assessed. This is because Ad-hoc Risk Reports would be generated whenever new information about a particular risk or issue is collected or whenever a potential new risk or issue is identified. It is therefore likely that as well as an annual periodic review the RER would be reviewed and potential updated at various points throughout the year (e.g. to coincide with the implementation of an SVA Release).

### Phase 2: Risk Assessment Decisions and Production of Operational Plan

This task would be performed by the RAB and would result in the production of the Operational Plan. This document is the RAB's formal response to the RER, setting out how the board intends to provide assurance for those risks and issues identified, that is, what assurance techniques will be applied and how they will

be applied; and the cost of providing that assurance (i.e. the anticipated costs of applying the assurance techniques). It is envisaged that the Operational Plan will be a non-confidential report that is approved by the Panel and published to the industry. The plan would be produced at least once annually but would also be reviewed whenever the RER was updated.

During this phase the RAB would determine the profile of risks for each participant. The participant risk profile would describe the extent to which the risks highlighted in the RER existed at that participant and would be based on:

- the participant's dimensions and portfolio of metering systems;
- an assessment of the participant's performance historically; and
- knowledge of the relevant control arrangements in place at the participant for each SVA process risk.

This information would be obtained from current market knowledge and the findings of any previously applied assurance techniques. For example, Qualification processes could provide information about an individual participant's control environment. Whilst the RAB may use this information to inform the development of its Operational Plan, it is not envisaged that the detail of participant risks would be published in the Operational Plan. Participant risk information would be considered further during phase 3 below. Appendix H provides further information regarding participant risks.

### Phase 3: Production of Risk Management Plans

Following the assignment of participants' risks profiles, the RAB would translate the Operational Plan into individual Risk Management Plans (RMPs) setting out in more detail how preventative, detective, incentive and remedial assurance techniques would be deployed at each participant.

### Phase 4: Application of Common and Further Assurance Tools

The application of common and further assurance techniques.

Common assurance techniques would be applied to all participants (or groups of participants, e.g. NHHDCs) in the same way and to the same extent. For example, the collection and reporting of Key Performance Indicator (KPI) data for specific business processes could be a common assurance tool, as all participants with the same role in that business process would have to provide the same monitoring data, e.g. all NHHDCs would have to provide data about the number of D0023 exceptions they received.

Further assurance techniques would only be applied where a participant significantly contributed to the existence of a risk or issue identified within the RER and may comprise targeted audits or escalation proceedings or similar.

It is anticipated that controls would be in place to ensure that the application of both common and further assurance techniques would be consistent, with participants in similar circumstances treated similarly by the RAB.

Whenever an assurance technique is applied, an Outcome Report would be produced detailing the findings. If new information is collected about an existing or potential new risk or issue then an Ad-hoc Risk Report would also be produced for review by the REG.

#### Phase 5: Risk Management Plan Monitoring

Performance against RMPs would be reported to the RAB. Where the application of an assurance tool provides further information about a participant's performance this would be used to update that participant's RMP. Where a participant is found to be failing against its agreed RMP, and this failing is significant, escalation processes could allow for the RAB and ultimately the BSC Panel to be informed of the participant's poor performance in order that further provisions set out under the BSC may be applied in accordance with the powers of the RAB and the BSC Panel.

At the year-end the RAB would prepare an annual report for presentation to the Panel and the industry. The report would contain the results of the work performed by the RAB, particularly how successful it had been at providing assurance that the risks identified in the RER had been successfully mitigated. The bulk of the report would be concerned with the findings of the different assurance techniques that had been applied during the period and the results that had been obtained from the application of those techniques. This report could include details of those participants who were contributing significantly to the manifestation of a particular risk or issue, as well as league tables of how different participants perform in different areas. In addition, the report would also contain details of the cost of the provision of the assurance framework over the course of the year and how these costs compare to the costs set out originally in the board's Operational Plan; any deviations would be explained.

#### Summary of Key Deliverables

A number of documents produced by either the RAB or the REG are key to the model. The purpose of these documents and their frequency of production are set out in the table below.

Deliverable	Description	Frequency	Author	Approver	Distribution
<b>(A)</b> Risk Evaluation Report (RER)	Details all key risks and their relative importance (see below)	At least annually	REG	BSC Panel	All
<b>(B)</b> Operational Plan	The RAB's response to the RER detailing what actions it will take to mitigate the risks identified (see below)	At least annually	RAB	BSC Panel	All

Deliverable	Description	Frequency	Author	Approver	Distribution
<b>(C)</b> Outcome Reports	The findings of the technique that has been applied (e.g. audit issue documents)	Following the application of a tool	ELEXON, BSC Agent or subcontract or	RAB	Impacted participants, associated Suppliers, OSMs
<b>(D)</b> Ad-hoc Risk Reports	Reports of new risks that have been identified or where further information has been obtained about a known risk	Only when new risks or information is identified following the application of a technique	ELEXON, BSC Agent or subcontract or	REG	All
<b>(E)</b> Annual Report	Details how effective the RAB has been at mitigating the risks identified in the RER (see below)	At least annually	RAB	BSC Panel	All
<b>(F)</b> Modifications and Change Proposals or Recommendation to the Panel for the same.	Changes to assurance techniques, standards etc. raised under BSC Section F.	As required when potential improvements identified by the REG or noted to the REG by the RAB via ad-hoc risk reports above.	REG	As per industry process	As per industry process
Risk Management Plans	Details the assurance techniques that will be deployed at a participant based upon an assessment of the risks that the participant presents to the SVA Assurance Objectives	At least annually and revised as necessary	RAB	RAB	Impacted participants, associated Suppliers, OSMs