



Direct Dial: 020-7901 7355

10 September 2003

The National Grid Company, BSC Signatories and
Other Interested Parties

Our Ref: MP No P122

Dear Colleague,

Modification to the Balancing and Settlement Code (“BSC”) - Decision and Direction in relation to Modification Proposal P122: “Assessment of Credit Cover during a Holiday Period”

The Gas and Electricity Markets Authority (the “Authority”)¹ has carefully considered the issues raised in the Modification Report² in respect of Modification Proposal P122, “Assessment of Credit Cover during a Holiday Period”.

The BSC Panel (the “Panel”) recommended to the Authority that the Proposed Modification P122 should be made and that the Implementation Date should be 19 September 2003, should the Authority determination be received on or before 12 September 2003. Should an Authority determination be received after this date, but prior to 9 January 2004 then the Implementation Date should be 16 January 2004

Having carefully considered the Modification Report and the Panel’s recommendation and having regard to the Applicable BSC Objectives and the Authority’s wider statutory duties³, the Authority has decided to direct a Modification to the BSC in line with the Modification Proposal P122.

This letter explains the background and sets out the Authority’s reasons for its decision. In addition, the letter contains a direction to The National Grid Company plc (“NGC”) to modify the BSC in line with Modification Proposal P122, as set out in the Modification Report.

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

² ELEXON document reference 122RR, Version No. 1.0, dated 15 August 2003.

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

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

Background

Energy Indebtedness is a megawatt-hour figure, which is translated into a percentage known as the Credit Cover Percentage. A calculation for Credit Cover Percentage is directly proportional to a Party's Energy Indebtedness. Energy Indebtedness is calculated from the approximated expected imbalance of the Party and an approximation of the Energy Imbalance Charges for that imbalance. The calculation is cumulative over 29 days and comprises two parts, Credited Energy Indebtedness and Actual Energy Indebtedness.

Credited Energy Indebtedness is calculated from the Balancing Mechanism (BM) Unit Credit Assessment Import or Export Capability which is based on Generation Capacity (GC) or Demand Capacity multiplied by the Credit Assessment Load Factor (CALF). This is used to calculate the average potential metered volume of the BM Unit. This is used for days for which there is no actual data available as the Interim Information Settlement Run⁴ data is not available. This is in general the first 9 days.

Actual Energy Indebtedness is calculated from the actual trading data available for the remaining 20 days of the calculation. Metered data for Supplier Volume Allocation⁵ BM Units is not available at the Interim Information Settlement Run stage and will not be available until the Initial Settlement Run.

The Initial Settlement Run is generally 15 Settlement Days after the Interim Information Settlement Run and therefore if there has been a change in load for that Party, it will not be reflected in the calculation. Also on days where Initial Settlement Run data is not available the metered volumes are calculated by using data from an "equivalent day" which is the most recent Settlement Day, which is the same day of the week for which the Initial Settlement Run data is available.

It is asserted that two issues emerge during holiday periods and in general during periods of lowered demand. The first relates to the use of a seasonal average CALF that, it is said, creates an unrealistically high Energy Indebtedness, and consequently a high Credit Cover Percentage, value for the days where settlement data is not used. The second issue is the use of the 'same day of the week', the equivalent day, at the point of the Interim Information Settlement Run to estimate supplier data. This would result in contract volumes for the bank holiday (they being lower than normal) being compared with metered volumes and trading charges for a 'normal'

⁴ A Settlement Run is a determination of amounts in respect of Trading Charges in relation to a Settlement Day (i.e. the period from 00.00 hours to 24.00 hours on each day) to be paid by Trading Parties and NGC or amounts to be paid to them. The BSC requires that the Settlement Administration Agent (SAA) be responsible for determining Trading Charges and intermediate calculations. The SAA is required to carry out an Interim Information Settlement Run, an Initial Settlement Run, four timetabled Reconciliation Settlement Runs for each Settlement Day as well as any Ad Hoc Settlement Runs required by the BSC Panel.

⁵ The Trading Party responsible for all Exports and Imports of electricity is responsible for ensuring that there is adequate metering and for registering the necessary Metering Systems in either the Central Metering Registration System or in one of the Supplier Metering Registration Systems provided by the Licensed Distribution System Operators. The BM Unit Metered volume will then be calculated in either Central Volume Allocation or in Supplier Volume Allocation.

weekday. This circumstance may result in a requirement for the Party to lodge an unrepresentatively high level of Credit Cover to avoid entry into Credit Default.

In order to rectify this situation, BizzEnergy submitted Modification Proposal P122, "Assessment of Credit Cover during a Holiday Period" on 26 March 2003.

The Modification Proposal

Modification Proposal P122 seeks to introduce the concept of a Holiday CALF for Supplier Base and Additional BM Units for periods during a BSC Year where demand differs as a consequence of bank and other public holidays namely Christmas, New Year and Easter.

Furthermore, Modification Proposal P122 seeks to amend the process whereby material doubt is applied to credit default situations so as to shorten the length of time between the Credit Default notices being issued by the Energy Contract Volume Aggregation Agent (ECVAA) and being either Authorised or cancelled by ELEXON, in order to provide BSC Parties with more certainty around the application of material doubt by ELEXON. The Panel will be obliged to establish and maintain a material doubt guideline that ELEXON will use when determining and applying material doubt to achieve this.

The justification for the Modification Proposal was that it would better facilitate achievement of the Applicable BSC Objectives⁶ C3 (3) (c) and (d).

The Panel considered the Initial Written Assessment at its meeting of 10 April 2003 and agreed to submit Modification Proposal P122 to the Assessment Procedure. The Settlement Standing Modification Group (the "Group") considered the Modification Proposal during four meetings, on 15 and 28 April 2003, 27 May 2003 and 24 June 2003. At these meetings the group reviewed a High Level Impact Assessment issued to the BSC Central Service Agent and ELEXON as well as an Assessment Consultation. The Assessment Consultation included the results of the High Level Impact Assessment of the potential solutions.

The Group agreed that if approved Modification Proposal P122 would better facilitate achievement of the Applicable BSC Objective C3 (3) (c) by removing barriers to entry for certain industrial and commercial Suppliers, allowing them to maintain a more appropriate level of credit cover. This would reduce their costs, thereby encouraging niche competitors and lowering the cost of market entry for new suppliers. The Group also agreed that to a lesser extent, Modification Proposal P122 better facilitate achievement of the Applicable BSC Objective C3 (3) (d) because the amendments to the Credit Default process identified by the Modification

⁶ The Applicable BSC Objectives, as contained in Standard Condition C3 (3) of NGC's Transmission Licence, are:

- a) the efficient discharge by the licensee of the obligations imposed upon it by this licence;
- b) the efficient, economic and co-ordinated operation by the licensee of the licensee's transmission system;
- c) promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity;
- d) promoting efficiency in the implementation and administration of the balancing and settlement arrangements
- e) the undertaking of work by BSCCo (as defined in the BSC) which is:
 - (i) necessary for the timely and effective implementation of the proposed British Electricity Trading and Transmission Arrangements (BETTA); and
 - (ii) relevant to the proposed GB wide balancing and settlement code; and does not prevent BSCCo performing its other functions under the BSC in accordance with its objectives.

Proposal may have the effect of improving efficiency in the Credit Cover and Credit Default arrangements, thus improving efficiency in BSCCo's handling of Credit Default.

ELEXON published a draft Modification Report on 18 July 2003, which invited respondents' views by 1 August 2003.

Respondents' views

ELEXON received six responses to the consultation on Modification Proposal P122. Five responses (representing 26 Parties) expressed support for the Proposed Modification, one response (representing 4 Parties) did not support the Proposed Modification.

The majority of responses also agreed that the legal drafting provided to give effect to the Proposed Modification addressed the defect identified by the Modification Proposal. One respondent (the proposer of Modification Proposal P122) indicated that whilst they supported the legal drafting, the rigidity of the dates caused them concern. However, this respondent further noted that review and amendments to the dates could be achieved at relatively low cost as no system changes were required.

The one response that did not express support for the Modification Proposal stated that it did not better facilitate achievement of the Applicable BSC Objectives. This respondent gave no further explanation for that view. Further this respondent did not believe that the proposed legal drafting addressed the defect of the Proposed Modification. This respondent provided an alternative definition of "Holiday period".

Having reviewed the proposed alternative definition of "Holiday Period" Elexon reported to the Modification Group that the current definition of Holiday Periods is consistent with the way in which CALF values are applied to BM Units, namely in terms of Settlement Days. Therefore the time constraints proposed by the alternative definition would be consistent with the approach of applying CALF for complete Settlement Days. Elexon further reported that the alternative definition provided no additional clarity or accuracy over the current definition of holiday periods. The Group noted that as a result of the respondent raising the issue, the legal drafting was amended to clarify the intent. i.e. that the Holiday Periods comprise complete Settlement Days.

The respondents' views are summarised in the Modification Report for Modification Proposal P122, which also includes the complete text of all respondents' replies.

Panel's recommendation

The Panel met on 14 August 2003 and considered the Modification Proposal P122, the draft Modification Report, the views of the Modification Group and the consultation responses received.

The Panel recommended that the Authority should approve the Proposed Modification and that, if approved, the Proposed Modification should be implemented on 19 September 2003, should the Authority determination be received on or before 12 September 2003. Should an Authority

determination be received after this date, but prior to 9 January 2004 then the Implementation Date should be 16 January 2004

Ofgem's view

Having carefully considered the Modification Report and the Panel's recommendation, Ofgem considers, having regard to the Applicable BSC Objectives and its statutory duties, that Proposed Modification P122 will better facilitate achievement of the Applicable BSC Objectives.

It is Ofgem's view that Modification Proposal P122 will better facilitate achievement of the Applicable BSC Objective (c) improving competition by removing barriers to entry for certain industrial and commercial Suppliers, allowing them to maintain a more appropriate level of credit cover. This will help in the reduction of their costs, thereby encouraging niche competitors and lowering the cost of market entry for new suppliers. It is Ofgem's view that Modification Proposal P122 better facilitates achievement of Applicable BSC Objective 3(d) by amending to the Credit Default process so as to improve efficiency in the Credit Cover and Credit Default arrangements. This in turn will help to improve efficiency in BSCCo's handling of Credit Default situations.

Modification Proposal P122 will enable Parties to apply for and have registered a CALF value specific to BSC defined holiday periods. The agreed Holiday Periods shall be the Christmas New Year period and the Easter Period. Prior to the start of the BSC Season containing a holiday period, BSCCo will issue a circular to BSC Parties, reminding them of the need to submit a request for calculation of a Holiday CALF value for any Supplier BM Units for which a value is required. Any BSC Party wishing to make use of a Holiday CALF value for a Supplier BM Unit will notify BSCCo prior to the calculation of the seasonal CALF values that they wish to use this mechanism for named Supplier BM Units. Parties will not be allowed to request the calculation of a Holiday CALF value at any other time. Upon receipt of a request BSCCo will calculate Holiday CALF values for those BM Units that requested a Holiday CALF value, following the same timescales and process as for seasonal CALF values. The Holiday CALF values will not necessarily be the same for all annual holiday periods and will be calculated in accordance with the CALF Guidelines.

It is Ofgem's view that Modification Proposal P122 provides a pragmatic solution to the current arrangements which may result in a requirement for Parties to lodge an unrepresentatively high level of Credit Cover during a holiday period. It will allow Parties to post more reflective levels of Credit Cover at a time where there is a drop in demand. On the issue of material doubt, Ofgem's welcomes the introduction of more formal guidelines as to the type of calculations that BSCCo should be using for verifying material doubt. This will provide further clarity to the process for determining material doubt and will make the process more transparent. It will further allow BSCCo more flexibility to deal with circumstances as they arise.

The Authority's decision

The Authority has therefore decided to direct that the Proposed Modification P122, as set out in the Modification Report, should be made and implemented.

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

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

The Implementation Date for Modification Proposal P122 is 19 September 2003.

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

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

Yours sincerely,

A handwritten signature in black ink, appearing to read 'D. Edward', written in a cursive style.

David Edward
Head of Electricity Code Development

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