

## P268 'Clarify the P/C status process for exempt BM Units' – Report Phase Consultation Responses

Consultation issued on 20 July 2011

We received responses from the following Parties:

Company	Number of BSC Parties / Non-Parties Represented	Role of Parties/non-Parties represented
E.ON UK	6/0	Supplier/ Generator/ Trader/ Consolidator/ Exemptable Generator
IBM (UK) Ltd. (for and on behalf of ScottishPower)	7/0	Supplier/ Generator/ Trader/ Consolidator/ Exemptable Generator/ Distributor
Nigel Cornwall	0/1	
National Grid	1/0	Transmission Company
EDF Energy	10/0	Supplier/ Generator/ Trader/ Consolidator/ Exemptable Generator/ Party Agent

What stage is this document in the process?

01 Initial Written Assessment

02 Definition Procedure

03 Assessment Procedure

04 Report Phase

Question 1 - Do you agree with the Panel's provisional recommendation to **reject** the retrospective Proposed Modification?

**Summary**

Yes	No
4	1

**Responses**

Respondent	Response	Rationale
E.ON UK	Yes	We support P268, but the negative impacts of implementing it retrospectively in terms of greater administration and cost for little benefit and more fundamentally of increasing uncertainty in the market, would outweigh the benefits. This would be negative primarily under Objective (c), not encouraging competition, and also (d), being inefficient. We note that as observed by a Panel member, in addition to the stipulation that any cost/loss incurred due to prevailing rules must be material, Ofgem guidance suggests that potentially only one of three criteria has to be met to justify retrospection. In the case of P268 this would be the case if one accepts the argument that the incident prompting P268 to be raised was directly attributable to central arrangements. The existence of a discrepancy between the Code and a CSD means that this can be argued; however overall we do not feel in this case that the argument in favour is strong enough to justify a retrospective implementation which would inherently undermine confidence in the market.
IBM (UK) Ltd. (for and on behalf of ScottishPower)	Yes	<p>We do not believe that the Proposed Modification better facilitates the BSC Objectives when compared to the current baseline for the following reasons:</p> <p>Objective a) Neutral</p> <p>Objective b) Neutral</p> <p>Objective c) In general the retrospective implementation of changes does not propagate a stable and safe marketplace which allows competition to flourish. Whilst it is true that clarifying rules brings certainty for new and existing market participants, in this case, it is outweighed by the uncertainty caused by the retrospective implementation.</p> <p>Objective d) There is a benefit to the operation of the BSC with this change in that it reduces the chances of future disputes which are time consuming and costly going forward, however this is washed out by the</p>

Respondent	Response	Rationale
		retrospective implementation, the effect of which needs to be managed.
Nigel Cornwall	No	<i>See Appendix 1.</i>
National Grid	Yes	National Grid agrees with the majority of the Group's views that there is no defect regarding the clarity of the BSC's provision for Exempt Export BM units.
EDF Energy	Yes	<p>As stated in our response to the P268 assessment phase consultation:</p> <p>Retrospective application of rule changes, particularly material ones, can reduce the incentive to understand rules and act accordingly, can create uncertainty and can undermine prudent investment decisions. Using such changes to rectify material mistakes made as a result of insufficient investment removes the benefit obtained by those that do make investment.</p> <p>In our view, the current rules on P/C status set out in the BSC are unambiguous. All parties should be aware that the BSC itself takes priority over subsidiary documents in the case of inconsistency. In this case, an oversight/mistake that could have been avoided by more prudent operation by the party has had a material impact on settlement and the proposal seeks to rectify this oversight by retrospective implementation.</p> <p>For these reasons, retrospective implementation would not help achieve BSC objective (c) concerning efficient competition, and would set a bad precedent for the future.</p>

Question 2 - Do you agree with the Panel's provisional recommendation to **approve** the prospective Alternative Modification?

#### Summary

Yes	No
4	1

## Responses

Respondent	Response	Rationale
E.ON UK	Yes	P268 is a practical solution to avoid Parties being exposed to imbalance charges from inadvertently nominating against the wrong account; we agree that an exempt BMU's P/C status should not 'flip' without the Lead Party's knowledge. Prospective implementation will clarify this for existing and prospective parties without any of the disbenefits that retrospective implementation would bring. Clarification of the Code and CSDs and a reduction in the notice period required for a Lead Party to change its P/C Status is also desirable. Thus P268 Alternative supports Objectives (c) and (d).
IBM (UK) Ltd. (for and on behalf of ScottishPower)	Yes	We agree that a prospective Alternative is better when compared to the retrospective Proposed Modification and baseline for the following reasons:  Objective a) Neutral  Objective b) Neutral  Objective c) Positive. The Alternative has all the good traits of the Proposed – i.e. it clarifies the rules for all Parties and brings more certainty to the arrangements, which in turn provides for a stable marketplace, without the uncertainty of retrospection.  Objective d) Positive. The Alternative reduces the likelihood of future disputes, which put a financial and operational burden on the operation of the BSC.
Nigel Cornwall	No	<i>See Appendix 1.</i>
National Grid	Yes	-
EDF Energy	Yes	Although we consider the current BSC provisions to be clear on the issue of P/C status and the current arrangements provide full flexibility for Exempt Export BM Units, we acknowledge that more effort is required to understand and manage a default P/C status, whether it is actively requested or occurs by default. We note that only one other BM Unit is subject to the dynamic P/C rules, and that is by default rather than explicit request. We also note that a P/C status set by default may change at short notice for reasons beyond a party's direct control, although that is a situation faced by all BM Units in "multi-party" Trading Units (and not the situation specifically experienced by the proposer). Taking into consideration these points, on balance we support the alternative prospective modification to simplify

Respondent	Response	Rationale
		the rules by requiring and allowing only explicit declarations of P/C status by an Exempt Export BM Unit registrant.

### Question 3 - Do you agree with the Panel's recommended Implementation Date?

#### Summary

Yes	No	Other
4	0	1

#### Responses

Respondent	Response	Rationale
E.ON UK	Yes	P268 should be implemented as soon as possible however implementation on 23 February 2012 or 5 April 2012 in parallel with P269 if approved would be efficient.
IBM (UK) Ltd. (for and on behalf of ScottishPower)	Yes	-
Nigel Cornwall	<i>Did not comment</i>	<i>See Appendix 1.</i>
National Grid	Yes	-
EDF Energy	Yes	Although an earlier date might have been expected for what appears to be a relatively simple change, we accept the 23 February 2012 or 5 April 2012 dates proposed in the modification report. There is minimal expectation of material impact on any parties in the intervening period, and implementation with P269 would achieve small cost savings.

Question 4 - Do you agree with the Panel that the redlined changes to the Code, BSCP15, BSCP31 and CRA Service Description deliver the intention of P268?

**Summary**

Yes	No	Other
3	0	2

**Responses**

Respondent	Response	Rationale
E.ON UK	Yes	The legal text changes to the Code for both the Proposed and Alternative and changes to BSCP15, BSCP31 and the CRA Service description all look appropriate.
IBM (UK) Ltd. (for and on behalf of ScottishPower)	Yes	-
Nigel Cornwall	<i>Did not comment</i>	<i>See Appendix 1.</i>
National Grid	Yes	-
EDF Energy	Yes/No	<p>The draft legal texts for the proposed and alternative proposals appear to deliver the intention of P268.</p> <p>The notice period for changes to Exempt Export BM Unit P/C status would no longer be explicit in the Code, and this could be considered to reduce certainty for parties. At the same time, the notice period for such changes would reduce from 28 days (as currently in the Code) to 2 Working Days, or less with agreement of CRA/BSCCo (in proposed subsidiary document BSCP15 3.12). The draft report mentions that no assessment consultation respondents objected to transferring the notice period from the Code to subsidiary documents. However, this was not part of the original proposal, and was not an explicit question highlighted in assessment consultation.</p> <p>We have not examined the proposed changes to subsidiary documents in detail at this stage, but note that a number of changes not directly related to the modification proposal are proposed. At BSCP15 3.8.1, the required notice period for changes to GC/DC would be reduced from 10 days to 1 Working</p>

Respondent	Response	Rationale
		<p>Day (WD), and the period before changes could be used in settlement consequently appears to be 1 WD (3.8.5/3). However, CRA checks at 3.8.4 and subsequent steps require at least 6 WD.</p> <p>We note that the term "Exemptable status" is used with a particular meaning in BSC subsidiary documents and is not necessarily the same as the more general status of being exemptable from the requirement to hold a generation licence under licensing legislation. A generating plant that is exemptable under licensing legislation might not have exemptable status under the BSC because its registrant has not explicitly applied for such status.</p>

## Question 5 - Do you have any further comments on P268?

### Summary

Yes	No
1	4

### Responses

Respondent	Response	Rationale
E.ON UK	No	-
IBM (UK) Ltd. (for and on behalf of ScottishPower)	No	-
Nigel Cornwall	Yes	<i>See Appendix 1.</i>
National Grid	No	-
EDF Energy	No	-



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26 July 2011

## **BSC modification proposal P268 Clarify the P/C status process for exempt BM units**

This modification proposal seeks to require that all exempt export BM units to have an elected Production/Consumption status in place of the current optional process. The BSC Panel is set to consider the DMR at its August meeting after having made a provisional recommendation that the original proposal, which includes a retrospective element between 1 March 2010 and the implementation date, should not be implemented. It has provisionally recommended implementation of the identical proposal that would apply prospectively.

I have not been party to the Panel's discussions on these matters, and will not vote on the matter at the August meeting. However, as the author of the modification on Statkraft's behalf, I thought I should set out the reasons why, in my view, retrospective implementation should be applied in this unique case, should the Authority decide to approve the modification.

The proposed solution, aside from consideration of implementation dates, would provide more clarity in the BSC to parties of what to expect when becoming an exempt generator. It would also remove discrepancies between code documents and, crucially, ensure the flag status cannot change without the specific election of the party. The solution addresses all the defects identified in the proposal in a simple, cost-effective way and will lead to a more efficient market (BSC objective (d)) and increase parity between new entrants and those more aware of how the market works (objective (c)). The fact the working group unanimously supports change to the rules, albeit on a prospective basis, illustrates that there is recognition that a clear deficiency exists in the rules as they stand.

Statkraft is seeking retrospection back to 1 March 2010 in order to recover the imbalance charges it incurred as a result of a unique set of circumstances. I note that, while Ofgem in general considers retrospective modifications are to be avoided as they undermine market confidence, it also considers that there are circumstances where this may be appropriate. In the regulator's [guidance](#) on urgent code modification these include: a situation where the fault or error giving rise to additional costs or losses was

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directly attributable to central arrangements; combinations of circumstances that could not have been reasonably been foreseen; or where the possibility of retrospective action had been clearly flagged so the detail and process of the change can be finalised with retrospective effect. Any cost/ loss incurred due to the prevailing rules would also need to be material. We believe that there are arguments to support all these criteria, except on flagging retrospective action.

Firstly we consider the fault was directly attributable to central arrangements. In this case it is material that the central arrangements are acknowledged to include code subsidiary documents.

The protracted debate over the trading dispute that proceeded this rule change proposal seems only to have resolved that in the event of a conflict between different code documentation the provisions of the code takes precedence. It placed no emphasis on the fact that the terms of the service description, which placed explicit requirements on the Central Registration Agent (CRA), were not followed. In other words the CRA breached the Code Subsidiary Documents in a manner that changed Statkraft's imbalance exposure but this was not considered to be a settlement error simply because the provisions of the code were deemed to have precedence. However, as the modification group has acknowledged the provisions in the code were unclear and are in need of revision. The trading dispute seems to have established that given the code documentation as a whole Statkraft's interpretation was not an unreasonable one, and in the light of this there should be redress.

We understand that it is difficult for the modification group to fully understand the circumstances that have given rise to this change, especially as the assessment had no remit to address inconsistencies within code documentation. But the fact remains that the CRA breached the provisions of its service agreement and Statkraft had a reasonable expectation that the terms set out explicitly for it would be complied with. It follows that agreeing the change on a restricted retrospective basis is the only fair outcome.

Secondly it is clear that the combination of circumstances could not have been reasonably been foreseen. In this context we note the assessment report's comment that Statkraft's understanding of the BSC requirements is the only known occurrence of this particular interpretation of these rules. However the report also states that most of these exempt generators are owned by the Big Six, with their wider market experience and who anyway have authorisations in place against both production and consumption accounts. The dispute never got to the bottom of whether notes from Elexon constituted guidance, but it was established that Statkraft made clear it held Production status for the BMUs and it did not wish to change that status.

The deficiency has endured since the P100 changes and has been shown in the case of DA375 to act to a particular trading party's financial disadvantage. But analysis has shown that, in practice, there would be no additional exempt generators impacted by the change between March 2010 and the P100 implementation date in 2003. This emphasises the uniqueness of this situation and adds weight to the argument that it could not have reasonably been foreseen.

Finally, the financial consequences of the events covered by DA375 were significant both in absolute terms and in relation to the Party's trading base at the time. Ofgem was present to hear the dispute referral DA375 and can take this information into account when determining the merits of a retrospective change as regards the materiality of the loss incurred due to the prevailing rules.

We believe that there are also good arguments against the proposition that, in this instance, a retrospective implementation should not apply because it may undermine market confidence. The circumstances surrounding this case will not be repeated, and the risks of regulatory uncertainty through applying a retrospective change, identified by the working group, in this instance are misplaced. A small change to the position of BSC Parties through amending RCRC is part of the everyday BSC operations. Analysis shows the likelihood of only one such change, so this would not give rise to a disorderly market and, given the

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implementation date, parties will have had well over a year to be aware of a potential adjustment. In the view of the proposer, this impact is outweighed by the benefits under objective (c).

In fact we believe there is a persuasive argument that retrospective implementation would support market confidence. Given the circumstances, allowing retrospective implementation of a one-off change would provide confidence to those considering entering the market because a known anomaly that worked to the commercial disadvantage of a trading party has been corrected. It demonstrates that the governance process works to achieve fair outcomes and that inconsistencies that flow from the complexity of the code and a rigid interpretation of it can be dealt with through the application of common sense. It thus helps to demonstrate that the rules can be applied justly and not skewed in favour of incumbents. Creating a more equitable playing field in this way would demonstrably better facilitate applicable BSC objective (c).

I hope you will find these comments pertinent, and I should be grateful if you could highlight them in the DMR that goes to the Panel's August meeting.

Please do not hesitate to contact me if you wish to discuss this further.

A handwritten signature in blue ink that reads "Nigel Cornwall". Below the signature is a long, thin arrow pointing to the right.

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