



Direct Dial: 020-7901 7355

6 June 2002

The National Grid Company, BSC Signatories and
Other Interested Parties

Our Ref: MP No P55

Dear Colleague,

Modification to the Balancing and Settlement Code ("BSC") - Decision and Direction in relation to Modification Proposal P55: "BSC Conflicts with Consolidation of Embedded Generation in Central Volume Allocation"

The Gas and Electricity Markets Authority (the "Authority")¹ has carefully considered the issues raised in the Modification Report² in respect of Modification Proposal P55, "BSC Conflicts with Consolidation of Embedded Generation in Central Volume Allocation".

The Balancing and Settlement Code Panel (the "Panel") recommended to the Authority that:

- (i) the Proposed Modification should not be made; and
- (ii) the Alternative Modification should not be made.

The Authority has decided to direct a Modification to the BSC.

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 Balancing and Settlement Code ("BSC") in line with Modification Proposal P55, as set out in the Modification Report.

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

Background

Modification Proposal P55, "BSC Conflicts with Consolidation of Embedded Generation in Central Volume Allocation", was submitted on 30 November 2001 by SmartestEnergy Limited.

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

² ELEXON document reference 011MMU, Version No. 1, dated 25 February 2002

The justification for the Modification Proposal was based on the Applicable BSC Objective³ C3 (3) (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".

An Initial Written Assessment (Version 0.2) of the Modification Proposal P55 was produced on 10 December 2001. The Panel meeting on 13 December 2001 agreed that Modification Proposal P55 should be submitted to the Assessment Procedure, and that the Assessment Report should be presented to the Panel meeting on 14 February 2002. Subsequently, ELEXON received a notice from the Authority on 4 January 2002, pursuant to BSC Section F, paragraph 1.4.3 (d), instructing the Panel Chairman to present an Assessment Report to the Panel Meeting on 17 January 2002. The Modification Proposal was assessed by the Modification Group, which held two meetings on 4 January 2002 and 10 January 2002.

Following a review of the Assessment Report at the Panel meeting of 17 January 2002, the Panel agreed to forward the Proposal to the report stage.

The Modification Proposal

Generating Plant is "Exemptable" where the company generating electricity at the plant is, or would be if they had no other Generating Plant, exempt from the requirement to hold a generation Licence. There are specific criteria under which plant can be considered Exemptable, but frequently it relates to generation capacity, e.g., plants that provide not more than 100MW. The operators of Exemptable Plant are known as Licence Exempt Generators ("LEGs").

Many LEGs are not signatories to the BSC, but instead, chose to sign contracts for all of their output with local supplier(s) within the same Grid Supply Point ("GSP") Group. The LEGs Metering System will often be registered in the Supplier Metering Registration System ("SMRS"). This one physical metering unit will measure both Export and Import active energies separately.

Modification Proposal P55 seeks to modify the BSC Section K to address an incompatibility between:

1. the requirement that a Metering System may only be registered in the Central Meter Registration Service ("CMRS") provided that there is not an associated Metering System registered in the SMRS; and
2. the concept of a consolidator, i.e., someone who acquires export energy from a number of generators, and aggregates the energy in a single account for trading in the open market.

Consolidation allows LEGs to participate in the New Electricity Trading Arrangements ("NETA"), whilst reducing their risk of exposure to energy imbalance prices. However, a consolidator can be a pure trader with no physical generation or supply facilities. Since they do not generate or supply, they do not require a Supply licence, but they are then restricted to dealing on behalf of CMRS registered Metering Systems, because Section K 2.4.2 of the BSC requires that the

³ The Applicable BSC Objectives, as contained in Condition C3 (3) of National Grid Company'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.

responsible party for SMRS registered Metering Systems must hold a Supply Licence. This prohibits a consolidator from dealing with LEGs whose Metering Systems are registered in SMRS.

The Proposed Modification would confer the right to a LEG to register their Export energy meter in CMRS, independently of the associated SMRS registered Import meter. Furthermore, it provides for both Central Volume Allocation ("CVA") and Supplier Volume Allocation ("SVA") data collectors to access the same outstation, and for a single Meter Operator Agent ("MOA") to access the Metering Equipment on behalf of the CVA and SVA data collectors.

The proposer believes that the allowance for Metering Systems to be registered in CMRS, whilst there is an associated Metering System registered in SMRS, would remove an obstacle to such consolidator trading.

The Modification Group raised an Alternative Modification Proposal, based on amending the definition of Exempt Export BM Unit in the BSC such that it would allow for the LEG to form a Trading Unit (a group of Balancing Mechanism Units ["BM Units"] that are in close proximity on the transmission system) in conjunction with a Supplier. It could then avail of the "embedded benefits" (the netting off of local generation with local GSP Group demand, which reduces the associated transmission and other charges), without the requirement to be registered in the CMRS. The Modification Group considered that the Alternative Modification Proposal would be less disruptive to the current system than the original Modification Proposal. However, in the time since this was proposed, the Authority made a determination on Alternative Modification Proposal P7, "Allocation of Supplier Demand to the same BM Unit in a GSP Group for all Suppliers in the same Company". This permits any grouping of Supplier BM Units in the same GSP Group to be within the same Trading Unit together with any number of CMRS registered LEG BM Units in the GSP Group. Although the scope of Alternative Modification Proposal P7 is wider than that of Alternative Modification Proposal P55, it incorporates the envisaged outcome of Alternative Modification Proposal P55, thereby rendering Alternative Modification Proposal P55 redundant.

ELEXON published a Draft Modification Report on 28 January 2002, which invited respondents' views by 4 February 2002.

Respondents' views

In total, ELEXON received ten responses to the consultation on the draft Modification Report for Modification Proposal P55. Of the responses, three (representing 14 Parties) expressed support for the proposed Modification and six (representing 22 Parties) were against implementation of the Modification Proposal. Five of the respondents against implementation felt that the approval of Alternative Modification Proposal P7 negated the need for this Modification Proposal, with one additionally citing the lack of a clear cost impact assessment as a further case for its rejection.

One response (representing four Parties) supported implementation of the Alternative Modification. Nine responses (representing thirty-three Parties) supported rejection of the Alternative Modification. The responses rejecting the Alternative Modification did so on the basis that the Authority's approval of Alternative Modification Proposal P7 improved the ability of LEGs to realise their embedded benefits, which they felt made the Alternative Modification redundant.

The respondents' views are summarised in the Modification Report for Modification Proposal P55, which also includes the complete text of all respondents' replies.

Panel's recommendation

The Panel considered the Assessment Report for Modification Proposal P55 at the meeting of 17 January 2002. It believed that both the original and Alternative Modification Proposals better facilitated achievement of the Applicable BSC Objectives. However, the Panel were concerned with the costs and risks to the integrity of settlements posed by the large number of transfers of registration from SMRS to CMRS that may result from the original Modification Proposal. Since the Alternative Modification Proposal avoided the need for such transfers, the Panel felt that it would better facilitate achievement of the Applicable BSC Objectives, as compared with the original Modification Proposal.

The Panel met on 14 February 2002 and considered the Modification Proposal P55, the draft Modification Report, the views of the Modification Group and the consultation responses received. In view of the intervening approval of P7 by the Authority, the Panel felt that the Alternative Modification Proposal was now redundant, and so changed their opinion from the previous meeting. The majority of the Panel felt that the original Modification Proposal posed too many risks and was too costly, especially in light of the reduced assessment time allowed to it by the Authority.

The Panel recommended that the Authority should reject both the Proposed Modification P55 and the Alternative Modification Proposal P55.

Ofgem's view

Ofgem agrees with the Panel's recommendation that the Alternative Modification Proposal P55 should be rejected. The approval of the wider ranging Alternative Modification Proposal P7 achieves the aims of Alternative Modification Proposal P55, thereby rendering it redundant.

However, Ofgem considers, having had regard to its statutory duties, that Modification Proposal P55 will better facilitate achievement of the Applicable BSC Objectives. It will provide additional opportunities for smaller generators to participate in NETA, through the medium of a consolidator. This should help to promote competition in the sale and purchase of electricity, in line with Condition C3 (3) (c) of NGC's transmission licence.

At the Assessment stage of the Modification Proposal, respondents expressed concern as to the robustness of the meter registration transfer process, and the Panel echoed these concerns. Ofgem understands their concerns, but believes that the competitive benefits to market participants wishing to avail of this process outweigh any perceived procedural risks. Furthermore, we believe that the registration process is now sufficiently well understood to cope with an orderly migration of meter registrations from SMRS to CMRS. It is not anticipated that ELEXON will be overburdened with numbers of applicants for the meter registration transfer process. Also, Ofgem believes that the potential benefits available to smaller generators through consolidation outweigh the costs incurred through having to transfer the registration of meters from SMRS to CMRS.

Consequently, Ofgem disagrees with both the Panel's reasons for recommending rejection of the original Modification Proposal P55 and the majority view of respondents that the approval of Alternative Modification Proposal P7 has negated the need for Modification Proposal P55.

The Authority's decision

The Authority has therefore decided to direct that the original Proposed Modification P55, as set out in the Modification Report for Modification Proposal P55, 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 as amended (the "Transmission Licence"), hereby directs NGC to modify the BSC as set out in the Modification Report for Modification Proposal P55.

The Modification is to take effect from the date of this letter approving the Modification Report.

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 'A. N. Simpson', with a horizontal line underneath.

Nick Simpson

Director of Industry Code Development

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