
Paper	Modification Consultation
Date	11 th December 2001
Paper Title	MODIFICATION PROPOSAL P044 'CORRECTION OF NOTIFICATION ERRORS WHERE PARTIES ARE ABLE TO SATISFY A REASONABLE AND PRUDENT OPERATOR TEST'
Purpose of Paper	For Second Consultation
Synopsis	This paper presents the progress made since the first consultation and High Level Impact Assessment on P044. In addition it requests that Parties consider the questions raised in this second consultation relating to the Error Correction Payment. Responses to this second consultation are required by 18 th December 2001.

1. INTRODUCTION

- 1.1 Modification Proposal P044 (P044) 'Correction of Notification Errors where Parties are able to satisfy a Reasonable and Prudent Operator test' was submitted on 8th October 2001 by Powergen. P044 seeks to modify the BSC so that Parties will be able to apply to the Panel requesting the ex post creation of new Energy Contract Volume Notifications (ECVNs) / Metered Volume Reallocation Notifications (MVRNs) or amendment of a previously submitted ECVN / MVRN. P044 seeks to address the increased risks faced by Parties that have no alternative but to notify their Volume Notifications close to Gate Closure.
- 1.2 The first Error Processing Modification Group (the Group) meeting was held on 12th November 2001 to progress P044 through the Assessment Procedure, as required by the Panel. The Assessment Report for P044 is to be presented to the Panel in January 2002.
- 1.3 Following the meeting a consultation and HLIA request was issued to Parties, Party Agents and the BSC Central Service Agent on 14th November 2001.
- 1.4 The results of this first consultation and HLIA were discussed by the Group at their second meeting on 5th December 2001 and as a result a number of refinements to P044 were agreed. Furthermore, one particular feature was considered by the Group to be of merit, but was felt to be of sufficient difference to constitute a potential alternative to P044. Also, some detailed aspects of this feature need to be considered further. Therefore, a further consultation was felt to be required.
- 1.5 This document constitutes that second consultation; responses should be provided to Modifications@elexon.co.uk by **5pm on 18th December 2001**. Any queries relating to this second consultation should be referred to the ELEXON help desk on 0207 380 4222.

2. DESCRIPTION OF PROPOSAL

- 2.1 P044 assumes that, in the main, Parties are able through robust checking processes and systems to minimise the probability of Volume Notification errors. Nevertheless, there are specific circumstances in which Parties and their Volume Notification Agents are unable to check submitted data where reports are not received from the ECVAA showing within day Volume Notifications and contracted positions. P044 allows a Party to apply to the Panel, requesting the ex-post creation or amendment of an ECVN/MVRN, if the above circumstances arise and subject to the Party demonstrating that they have operated in a reasonable and prudent fashion and that the support of both Party and counterparty to the notification is forthcoming.
- 2.2 The Proposer believes that P044 better facilitates the Applicable BSC Objectives, as defined in Transmission Licence Condition C3 Paragraph 3; namely objective (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'.
- 2.3 P044 is attached to this paper.

3. MODIFICATION GROUP DELIBERATIONS

- 3.1 The Group at their first meeting on 12th November 2001 considered P044 and formulated the first consultation and HLIA approach. The Group also agreed the detailed approach for the overall Assessment Procedure. The P044 Consultation and High Level Impact Assessment which included a questionnaire was produced by the Group and this was issued for consultation and HLIA on 14th November 2001. This document is available on the BSC Website.
- 3.2 A second Group meeting was held on 5th December 2001 and its purpose was to review the results of the first consultation and HLIA. The following key issues were raised:
- i) Definition; the Group agreed that the definition of an error should be that which was described in Modification Proposal P037 'To Provide for the remedy of past errors in Energy Contract Volume Notifications and Metered Volume Reallocations' (P037).
 - ii) Tests; the Group agreed that P004 'Dual Contract Notification' would not remove the need for P044, but the tests relating to the availability of ECVAA reporting would be made more generic, in recognition not just of the potential for P004 to introduce new reports, but for other reporting enhancements that may occur (and indeed have occurred). The Group also agreed that the BSC should contain a generic description of a 'Reasonable and Prudent Operator' (being an operator whose risk management is commensurate with the level of risk associated with their trading strategy) and that Panel guidelines would be drawn up to enable the Panel to determine whether this (and other tests) had been demonstrated to their satisfaction, rather than the tests being demonstrated beyond reasonable doubt.
 - iii) Decision making body; the Group confirmed its view that the responsibility for decision making should lie with the Panel. It was also concluded that there should be an appeals process, as with P037.
 - iv) Cash flows; there was no change to the fees to be levied for the raising of claims. However, it was considered that an Error Correction Payment should be included in P044. The significance of this was such that the Group considered that this distinct element of the proposal should constitute an Alternative Modification Proposal. This is considered further, below.

- v) Administrative process; the Group decided that the process was acceptable, including the timescales for the raising of claims. It was also accepted that the treatment of credit cover would be the same as that for P037.
- vi) Implementation; the potential interactions between P035, P044 and other Modification Proposals is still being considered by the Group. However, the Group concluded that no alternative was required to cover for the eventuality that a gap would exist if both P037 and P044 were approved.

Attached to this paper is the P044 Requirements Specification that has been updated in view of the agreements reached by the Group on 5th December 2001.

4. ALTERNATIVE MODIFICATION PROPOSAL

4.1 As described above, an Alternative Modification Proposal has emerged from the previous consultation exercise. This alternative is identical to the original Modification Proposal, along with the refinements described above, except that the alternative includes an Error Correction Payment (ECP).

4.2 Rationale for ECP

4.2.1 The consultation responses were split; those in favour thought that incentives to make correct Volume Notifications would be strengthened, those against considered that the non-retrospective nature of P044 and the stringency of the tests was such that incentives to make correct Volume Notifications were adequate without an ECP.

4.2.2 The Group noted that P044 would be simpler and cheaper to implement without an ECP, with one Group member stating that the cost of implementing an ECP might therefore be disproportionate. It was also suggested that the 'Reasonable and Prudent Operator' test implied a sufficient incentive and that, to impose further costs would lead to inefficient investment. However, the Group acknowledged that both sides of the argument had merit.

4.2.3 The Group considered that one scenario that might arise where a claim would be made was that of an organisation who was vertically integrated and an error had been detected in its demand forecast after it was able to make a Volume Notification. It was considered that this scenario could involve significant volumes, at significant imbalance price differentials, therefore the potential gains were high if the claim was determined to be valid. It was further suggested that, in applying the tests, in light of such a scenario, reasonable industry practice for different sizes and types of Party might be difficult.

4.2.4 The Group also considered the Authority views, as expressed in Modification Proposal P019 'To provide for the remedy of errors in Energy Contract Volume Notifications and in Metered Volume Reallocation Notifications' (P019) determination that:

- *"a fixed percentage limit on recovery of a claim, in addition to the fee. Ofgem agrees with one of the respondents that a fixed percentage limit on recovery of a claim, in addition to a fee, may better achieve the relevant objectives by providing an incentive to accurate notification. The effectiveness of such provisions in providing appropriate incentives would need to be kept under review;"* (paragraph 25 (ii)).
- *"...The Authority, however, recognises that a notification error correction mechanism may not necessarily be incompatible with the BSC Objectives if it were to include the elements*

outlined in paragraph 25 above, including a fixed percentage limit on recovery of the claim.” (paragraph 28).

- *“If a future modification proposal were submitted which sought to address the question of a correction mechanism for erroneous notifications retrospectively, Ofgem would want to consider such a proposed modification in the light of its comments above. However, Ofgem considers it appropriate, in the light of the view expressed in paragraph 19 above, that there should be a more stringent cap on the retrospective recovery of monies lost through errors in notification. Ofgem would expect that those concerned would address these points in the consideration of any future modification proposal.” (paragraph 37).*

4.2.5 The Group concluded that the RPO test may not be a sufficient incentive to deter spurious claims and that an ECP was required.

4.3 Level of ECP

4.3.1 Although the previous consultation had asked for participant views as to whether an ECP should be introduced and if so should it be uncapped, no response provided had suggested an appropriate level. Of those respondents who thought that ECP was a necessary element of P044, the following comments were received relating to the level of ECP:

- one response indicated that the value should be less than that for P037 on the basis that the tests for P044 were much tighter than those for P037;
- another response indicated that significant financial penalties should apply on the basis that this would maintain high incentives to operate robust systems and would assist in limiting any pressure on the process to implement a successful claim.

Again the Group considered the views of the Authority as described in the determination on P019 (refer to 4.2.2). The Group considered that an ECP of 10% would provide a strong incentive to make correct Volume Notifications, and noted that this was consistent with the Authority's determination on P019. The Group concluded that a 10% ECP would be appropriate, taking account of the above and given that a 20% ECP has been proposed as part of Modification Proposal P037.

4.4 Cap on ECP

4.4.1 One response to the consultation suggested that there should not be a cap on any ECP.

4.4.2 One Group member expressed the view that higher values of Volume Notifications required higher incentives to ensure correctness and hence, there should be no cap on the ECP, but that the form of the ECP (being a percentage of the value of the claim) was appropriate. The Group supported this approach. This would be consistent with the P019 determination.

5. CONSULTATION APPROACH

5.1 In order to complete the Assessment Procedure for P044, views are required on the detail of the Alternative Modification Proposal. Hence, given that views have already been sought on whether there should be an ECP, it only remains for views to be given in respect of the value of the ECP and whether this value should be capped.

- 5.2 It is assumed that the detailed application of the ECP would be as for P037, the value being set as a percentage of the energy imbalance benefit for the claimant (and counterparty, if appropriate) and the resultant cash flow being redistributed to those whose energy accounts do not benefit, pro-rata on credited energy.
- 5.3 On the basis of the above, answers to the following questions are requested to assist in finalising the proposals:
- i) **Level of ECP;** Do you agree that the level of ECP should be set at 10%? If not what level do you believe the ECP should be set at? Please give reasons, including specifying what BSC Objectives would be better facilitated as a result of this proposal.
 - ii) **Cap on ECP;** Do you agree that there should be no cap on ECP? If you disagree, at what value should a cap be set? Please give reasons, including specifying what BSC Objectives would be better facilitated as a result of this proposal.