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MODIFICATION REPORT
MODIFICATION PROPOSAL P98 – Dual
Notification of Contract Positions

Prepared by ELEXON on behalf of the Balancing
and Settlement Code Panel

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1 SUMMARY AND RECOMMENDATIONS

1.1 Recommendation

On the basis of the analysis, consultation and assessment undertaken in respect of this Modification Proposal during the Modification Procedure, and the resultant findings of this report, the BSC Panel (the Panel) recommends that:

Proposed Modification P98 should not be made.

In the event that the Authority determine that Proposed Modification P98 should be made, the Implementation Date should be 5 July 2004, where an Authority determination is received prior to 8 April 2003. Should an Authority determination be received after this date, but prior to 19 August 2003 then the Implementation Date should be 8 November 2004.

1.2 Background

The Assessment Report for Modification Proposal P98 (Reference 1) contains the detailed background and history of Modification Proposal P98, and this report can be found on the BSC Website, as follows:

ftp://www.elexon.co.uk/ta/modifications/modspros/P098/P098_Assess_Report.pdf

Modification Proposal P98 'Dual Notification of Contract Positions' (P98) was raised by Dynegy UK Limited on 2 September 2002. P98 seeks to introduce a (voluntary) dual notification system within the BSC Systems. Dual notification is the process of notifying contract volumes, whereby both parties to the notification (via their nominated notification agent), submit their agreed contract volumes to the BSC Central Service Agent, where the volumes are matched. Matched contract volumes are then submitted to settlement, as an agreed position. This effectively ensures that both Parties have agreed the contract volumes that go forward into Settlement.

It should be noted that P98 seeks to address the issues that were identified under Modification Proposal P4 'Dual Energy Contract Notification' (P4) (raised in March 2001). P98 also seeks to utilise the definition and assessment work undertaken under P4, to provide a solution based on the P4 Requirements Specification (O14AAR V1.0).

The Panel considered the Initial Written Assessment for P98 at its meeting of 12 September 2002, and agreed to submit Modification Proposal P98 to the Assessment Procedure, with the Assessment Report to be submitted for consideration at the Panel meeting of 12 December 2002. The Panel also agreed that the Assessment Procedure should be undertaken by the Settlement Standing Modification Group (SSMG). The Panel further agreed that an initial consultation should be undertaken to determine the likely take up of the voluntary dual notification system, with an interim report to be submitted for consideration at the Panel meeting of 17 October 2002.

During the Assessment Procedure for P98, the SSMG met five times, on 23 September 2002, 10 and 16 October 2002, and 14 and 29 November 2002, to assess P98 against the assessment criteria identified, define the requirements for the dual notification service, consider the consultation responses and impact assessments and to agree the recommendations to be made to the Panel in respect of P98.

To assist in the assessment of P98:

- An Assessment Consultation mainly aimed at determining the likely take up of the voluntary dual notification service (indicated as just over a third of respondents), but also requesting information

for assisting the SSMG assessment of P98, was issued on 26 September 2002, with responses received by 8 October 2002. From the consultation, the Panel determined that there was sufficient interest in the Modification Proposal for the Assessment Procedure to continue;

- A request for an Impact Assessment, based on the Requirements Specification, was issued on 4 November 2002 for industry high level impact assessment (MC00022), with responses received by 12 November 2002, and to the BSC Central Service Agent for detailed level impact assessment, on 4 November 2002, with an interim response received on 14 November 2002 and a final response received on 27 November 2002; and
- A second Assessment Consultation aimed at obtaining information to assist the SSMG in making their recommendations in respect of P98, was issued on 18 November 2002, with responses received by 27 November 2002.

The SSMG met on 29 November 2002 to consider the responses made in respect of the second assessment consultation and to finalise the assessment of P98, agree the Assessment Report and the recommendations in respect of P98.

On balance the majority (two thirds) of the SSMG agreed that Proposed Modification P98 should not be made. The SSMG noted that approximately the same proportion of consultation responses (just under two thirds) were of the same opinion. Therefore the SSMG recommended to the Panel that Proposed Modification P98 should not be made.

The Panel considered the Assessment Report at its meeting of 12 December 2002, and unanimously agreed to provisionally endorse the recommendations of the SSMG, that the Proposed Modification should not be made. Therefore, the Panel agreed to submit P98 to the Report Phase.

The Panel further agreed that, if the Authority determined that the Proposed Modification should be made, that the Implementation Date should be 5 July 2004, if the Authority determination is received prior to 8 April 2003. Should an Authority determination be received after this date, but prior to 19 August 2003, the Implementation Date should be 8 November 2004.

The Panel noted the BSC Central Service Agent development and implementation costs associated with Proposed Modification P98 of £1,888,540, (excluding ELEXON effort of approximately 500 man days) and the ongoing BSC Central Service Agent operate and maintain costs of approximately £800,000 per annum.

The Panel noted that these costs were attributable to the significance of the software development required to support dual notification, and the consequential additional hardware required to support the web based reporting and web based submission of notifications, as well as the requirement to handle increased volume of reports resulting from the use of dual notification (potentially a ten fold increase in notifications and feedback reports (acceptance and rejection)).

The Panel noted that it believed these costs to be significant, and requested that work be undertaken by ELEXON to reduce these costs. The Panel further noted that the development and implementation timescales of 64 weeks could be split into a two phase release, whereby dual notification functionality could be made available earlier, with the web based reporting and web based notification submission implemented in the following release. Therefore the Panel also requested that this implementation approach be investigated, with a view to reducing the implementation timescales.

The draft Modification Report, containing the provisional recommendations of the Panel, was provided to Industry for consultation on 9 January 2003, allowing 15 working days for respondents (responses due 30 January 2003).

During the Report Phase, ELEXON reviewed the development and implementation costs associated with Proposed Modification P98, as requested by the Panel. It was determined, in informal discussion with the BSC Central Service Provider, that there may be the potential to reduce the development and implementation costs of the BSC Central Service Provider and of ELEXON. It was noted that these costs will be finalised at any initiation of the project to implement P98, should an Authority determination to this effect be received, when detailed requirement specifications and resultant impact assessments are produced. It is not proposed to investigate the development and implementation cost further with the BSC Central Service Agent at this time, as this would incur further, potentially not insignificant, impact assessment expenditure.

The implementation strategy was also reviewed to determine whether a two phased approach would be feasible. It was agreed that the existing implementation strategy, i.e. implementation of all the functionality associated with the Proposed Modification in one systems release, would be the most appropriate implementation mechanism. The rationale for this approach results from the potential for increased project overhead costs, resulting from the development and implementation of the functionality to support P98 in two BSC System releases, outweighing the benefit of implementing the dual notification functionality only three months earlier than the currently specified Implementation Date. Therefore the implementation strategy has not changed from that set out in the Assessment Report and in the draft Modification Report sent out for consultation. Thus Proposed Modification P98 will be implemented to the Implementation Date set out in this draft Modification Report.

The consultation responses made in respect of the Draft Modification Report were received on 30 January 2003. The majority of the respondents (seven of eight that commented on the draft Modification Report) indicated support for the provisional recommendations contained within the draft Modification Report, namely that the Proposed Modification should not be made. The one respondent that did not support the provisional recommendations of the draft Modification Report reiterated arguments made during the Assessment Procedure (response P98_DR_005). However no new, substantive arguments were raised.

The Panel considered the draft Modification Report and the associated consultation responses at its meeting of 13 February 2003 and unanimously agreed to confirm its provisional recommendation that the Proposed Modification P98 should not be made.

1.3 Rationale for Recommendations

The Panel supported the rationale for the recommendations made by the SSMG with regards to Proposed Modification P98 and on the basis of this rationale, the Panel recommended that Proposed Modification P98 should not be made, as it does not better facilitate achievement of the Applicable BSC Objectives.

1.3.1 Applicable BSC Objectives

The SSMG identified a set of issues that it considered to be the key issues to be considered in the Assessment of P98, and therefore to be considered when assessing whether Modification Proposal P98 better facilitates achievement of the Applicable BSC Objectives. The discussions and considerations of the SSMG with respect to these issues are set out in full in section 5 of the Assessment Report (Reference 1), and are summarised in section 1.3.2 of this Modification Report.

The SSMG noted that dual notification would provide enhanced contract notification facilities, in particular the web based reporting. However, the SSMG concluded that there was one key argument for or against dual notification and that is the individual Party assessment of the materiality of the issue

of unlimited settlement liability. Those Parties that believe the risk of exposure to unlimited settlement liability is unmanageable will support dual notification at any cost, as the cost of providing the dual notification service will be negligible compared to the costs of erroneous / malicious notifications to individual BSC Parties and potentially the industry as a whole.

However, those Parties that believe that the risk of the potential for exposure to unlimited settlement liability is manageable by other mechanisms (checking of notification reports, contractual and legal recourse) are not likely to support dual notification, as the cost of implementing dual notification, including the costs to industry from amending notification processes and renegotiating the Grid Trade Master Agreement (GTMA) will outweigh their perceived benefits.

Therefore the SSMG agreed that the decision to support the implementation of P98 would be down to whether the perceived risk of not implementing it is too great.

On balance the majority (two thirds) of the SSMG agreed that the potential risk of exposure to unlimited settlement liability was insufficient to warrant implementation of dual notification at this time. The SSMG noted that approximately the same proportion of consultation responses (just under two thirds) were of the same opinion. The minority view of the SSMG, in support of P98, strongly believed that dual notification was essential to safeguard existing Parties against this risk and encourage new entrants to the market.

The SSMG, having reached a conclusion on each of these assessment issues (set out in full in section 5 of the Assessment Report (Reference 1)), considered how the conclusions on the impacts and incentives of P98 would lead to the Proposed Modification better facilitating achievement of each of the Applicable BSC Objectives, and the extent to which this is the case.

The SSMG noted that the assessment as to whether Proposed Modification P98 better facilitates achievement of the Applicable BSC Objectives lies with the assessment as to whether the implementation of dual notification is cost beneficial, which in turn, results from the assessment as to whether the risk of exposure to unlimited settlement liability is manageable, or not.

However, on balance, the majority (two thirds) of the SSMG believed that, although Proposed Modification P98 may have the effect of reducing notification risk and thus may improve competition in the sale and purchase of electricity (Objective 3(c)), the costs associated with the implementation of dual notification and therefore the decrease in the efficiency of the implementation of the balancing and settlement arrangements (Objective 3(d)) outweigh these benefits to competition. Therefore, they believed that the Proposed Modification P98 does not better facilitate achievement of the Applicable BSC Objectives.

The SSMG noted that the consultation responses (made in respect of the second assessment consultation) were split to the same degree as the SSMG. The majority of consultation responses (two thirds) did not believe that Proposed Modification P98 better facilitated achievement of the Applicable BSC Objectives.

1.3.2 Assessment Issues for Modification Proposal P98

The SSMG identified a set of issues that it considered to be the key issues to be considered in the Assessment of P98. The discussions and considerations of the SSMG with respect to these issues are set out in full in section 5 of the Assessment Report (Reference 1), and can be summarised as follows:

– **Potential for Exposure to Unlimited Liability from Single Notification**

The Proposer of P98 asserts that the Modification Proposal was raised primarily to address the issue of the potential for exposure to unlimited (settlement) liability as a consequence of an erroneous or malicious notification under single notification. The Code contains no concept of limitation of exposure to Energy Imbalance charges, and therefore Settlement liability, in the event of an erroneous or malicious notification made against a Party by their counterparty. It was further noted that there is the potential for malicious or erroneous notifications to push a BSC Party into Credit Default under the Code.

The SSMG noted that there are commercial arrangements in place (outside of the Code) to deal with these circumstances, for example the Grid Trade Master Agreement (GTMA), however, it was noted that these commercial arrangements will not address the circumstance where the notifier can not meet their obligations under the commercial contract, for example, where either they are insolvent, potentially as a consequence of the settlement liability (perhaps resulting from the erroneous notification), or where they are in administration (and the administrators are enforcing a certain course of action).

The SSMG noted that although the probability of such extreme circumstances is relatively low, the materiality could be high and potentially catastrophic for the Party on the receiving end of the erroneous / malicious notification, and the implication is that this may have (detrimental) knock on effects for other Parties.

The SSMG agreed that the key consideration is the perception of risk. The risk of exposure to unlimited settlement liability is present, but some believe it to be an acceptable risk, or a risk that can be mitigated. However, others believe it to be an unmanageable risk that, whilst it has a low probability of occurring, has a high materiality with potentially catastrophic consequences.

– **Incentives to Maintain Robust Systems**

One of the concerns raised by the Authority in their determination on Modification Proposal P4 'Dual Energy Contract Notification' was the potential for the implementation of dual notification to incentivise a reduction in the robustness of BSC Party notification systems.

Under the current single notification system, there is the potential for the other counterparty to notify where there is a failure of a party notification system. However, under dual notification, there is no such back up, as both Parties have to notify, and notify correctly. Therefore the consequences of Party notification system failure are potentially higher under dual notification, incentivising notification systems that are equally, or potentially more robust than under the current single notification arrangements, as noted by the majority of consultation responses (made in respect of the second assessment consultation on P98).

– **Notification (Commercial) Disputes Resolution**

The SSMG noted that the use of a dual notification system could clarify the identification of the culpability of erroneous notifiers. It is proposed that adoption of a dual notification system would improve the ability of Parties to identify where the culpability, and therefore liability, for an erroneous notification lies, as it is clear which of the counterparties made the error. This may improve the efficiency of the (commercial) disputes resolution process where there have been erroneous notifications made.

However, there was no consensus amongst the SSMG as to whether this would be the case. A number of the SSMG believe that it will require as much effort to assign culpability for incorrect notifications under dual notification as it does under single.

– **Liability for Errors in the Dual Notification Process**

Another of the concerns raised by the Authority in their determination on P4, was the potential for the liability associated with erroneous contract notifications / matching to be carried by the BSC Central Service Agent and therefore recovered from all BSC Parties via BSCCo charging mechanism.

The SSMG noted that the liability of the provider of any dual notification commercial service arises as a consequence of the inability of the provider to correct the erroneous notification in the Energy Contract Volume Aggregation Agent (ECVAA) systems. Thus the counterparties that are the subject of the erroneous notification / match are exposed to Energy Imbalance charges to the extent of the erroneous notification / match and are entitled to recover some portion of this from the service provider in accordance with the commercial contract in place.

If the dual notification service were to be part of the BSC Central Services and a BSC System, then the liability for an erroneous match would fall on the BSC Central Services (and therefore on ELEXON). However, under these circumstances, and under strict Code obligations and constraints, the error can be corrected in the ECVAA data, meaning that there is effectively no material liability, as Settlement has been corrected to reflect the correct notification / match. Thus the exposure to Energy Imbalance charges to the extent of the erroneous notification / match is removed, and this could be considered, by some, to be more efficient.

The SSMG considered that this approach would mean that there is no increase in the liability of ELEXON, and therefore BSC Parties, as a consequence of erroneous notifications / matches falling within the scope of the dual notification service.

– **Existing Commercial Provision of Dual Notification Services**

A further point raised by the Authority in their determination on P4 is the existing provision of commercial dual notification services.

In the first Assessment Consultation on P98, the SSMG specifically asked Parties whether they used the commercially provided dual notification services. Of the twenty-two responses made in respect of the consultation, only one respondent indicated that they utilised such services. Rationale was requested as to the reasons for utilisation, or not, and the majority of respondents indicated that the reasons for not using commercially provided dual notification services are the perceived expense of such services, the limitation of liability by the provider, and additionally the perceived complexity of such services.

Therefore a number of the SSMG believe that the commercially provided services do not address the issues that P98 is seeking to address.

– **Changes to Pattern of Trading and Market Liquidity**

The SSMG considered the impact that implementation of a dual notification service might have on the way in which Parties trade. A number of the SSMG proposed that implementation of dual notification may lead to a move away from the notification of trades at peak times, under the current GTMA arrangements to a more flexible, trade by trade notification system. This, in turn, may have the effect of reducing the peak load of notifications on the ECVAA system.

However, the SSMG could make no definitive comment on how the implementation of dual notification may change notification habits, as the consultation responses (made in respect of the second assessment consultation) indicated that the manner in which notification habits would change is dependent on many other factors.

The SSMG also considered the impact that implementation of dual notification may have on the liquidity of the market. Some members of the SSMG believe that any reduction in notification risk may have the effect of increasing liquidity in the trading markets. However, others believe that the implementation of the enhanced ECVAAs reporting would have a more material effect on liquidity, and that dual notification may have very little effect on liquidity in the traded markets.

The SSMG considered the issue to assess whether notification risk is the reason why there is little within day trading and therefore relatively low liquidity. The SSMG concluded that if the sole reason for not trading within day is the notification risk, then dual notification has the potential to improve the liquidity within day. However, if this is not the case, then the implementation of dual notification is likely to have more limited impact on liquidity.

– **Cost Benefits from Implementation of Dual Notification**

The SSMG noted that P98 is a cost-benefit driven Modification Proposal. A number of the SSMG believe that the costs of implementation of dual notification are far outweighed by the benefits that the dual notification process offers, namely the reduction in notification risk from erroneous or malicious notifications, the mitigation of the potential for unlimited (settlement) liability resulting from such erroneous or malicious notifications, and in the increased ability to identify culpability for errors in notifications, and the associated reduction in the cost of recovering commercial compensation for such errors.

In the first of the assessment consultations, a number of questions were aimed at determining the cost to the industry resulting from erroneous / malicious notifications in the six months prior to the issue of the consultation. The costs provided in the responses ranged from zero to sums in the region of £250,000, with the number of erroneous notifications quoted ranging from none to forty-five.

Some of the SSMG noted that it is almost impossible to quantify the cost benefit of dual notification. In the worst case scenario where there is a catastrophic Party failure, then the cost of implementing dual notification could be considered to be negligible in comparison to the benefit. However, others of the SSMG noted that it is tempting to remain with the status quo, on the basis that the risk can be managed / mitigated.

Therefore the SSMG concluded that the assessment as to whether the implementation of dual notification is cost beneficial comes down to whether it is believed that the risk of exposure to unlimited settlement liability is manageable or not.

– **Cost Recovery of Dual Notification Development and Implementation Costs**

The SSMG noted that one of the concerns regarding the implementation of dual notification raised by consultation responses, was the issue of cost recovery of the development and implementation (and potentially operational) costs from those Parties choosing to utilise dual notification. The concerns raised by a number of consultation responses indicate that those Parties choosing not to use dual notification should not be required to incur the costs of its development, implementation and operation.

The SSMG considered this aspect of P98 and noted that:

- The implementation of the dual notification service would also improve, by association, the robustness and other aspects of the single notification process (see section 4). Thus all Parties would benefit from the implementation of P98, making a case for all Parties incurring the relevant costs;
- Defining a cost recovery mechanism that would recover the costs of development, implementation and operation of dual notification from users of the service equitably would be difficult to impossible, given that different Parties would use the process different amounts, and there would also be the issue of Parties moving to dual notification at different points, according to their counterparties level of usage; and
- The intent and implementation of the BSCCo charging structure means that costs are recovered from all Parties on a proportional basis (as set out in Section D of the Code) and this effectively means that all Parties may be paying for functionality that they do not use.

Therefore, the SSMG concluded that, on balance, the current BSCCo cost recovery mechanism would be appropriate for recovering the costs associated with P98.

– **Complexities from Operation of Two Notification Systems**

A number of consultation responses, made in respect of the first assessment consultation on P98, as well as a number of responses made in respect of the industry Impact Assessment request (MC00022), indicated that a number of Parties believe that there is increased complexity for them, as they will be required to operate two notification systems / processes, and apply them according to any agreement with the specific counterparty, and even specific trade.

The SSMG concluded that dual notification may increase or decrease the complexity of notifying for different Parties, dependent upon current practice, systems and processing.

In the second assessment consultation, the SSMG requested opinions from Parties as to whether, in principle (i.e. disregarding incumbent systems), new entrants would prefer to use dual or single notification. A number of respondents indicated that new entrants would choose the system that was preferred by the majority of incumbents in order to maximise their trading opportunities.

The SSMG noted that one response made in respect of the second assessment consultation was received from a new entrant (Conoco Phillips) indicated that dual notification would be their preferred system, because new entrants are likely to make more notification errors, and dual notification protects new entrants to some degree from the consequences of these errors.

– **Enhanced ECVAA Reporting**

The SSMG noted that Alternative Modification P4 and CP755 implementing enhanced ECVAA reporting by introducing Acceptance Feedback Reports from ECVAA (ECVAA – I028 and ECVAA – I029) for notification submissions, was implemented on 8 October 2002.

A number of the SSMG believe that, although the additional reporting implemented is extremely useful, it still does not address the main issue that P98 is seeking to address, namely the potential exposure to unlimited (settlement) liability where an erroneous or malicious notification has been made against a Party by their counterparty.

The SSMG noted that some Parties believe that the implementation of enhanced ECVAA reporting does not address the key issue that P98 is seeking to address, namely the mitigation of the risk of

exposure to unlimited settlement liability. Whereas other Parties believe that the implementation of the enhanced ECVAA reporting assists in mitigating this risk, and therefore negates the requirement for dual notification.

Therefore the SSMG noted that again, the requirement for dual notification comes down to an assessment of the risks associated with unlimited settlement liability by individual Parties.

– **Provision of Dual Notification by a non BSC Agent**

The SSMG considered the possibility of ELEXON procurement of dual notification from an existing commercial provider, rather than from the current BSC Agent, noting that provisions would be required to be put in place to make the dual notification service effectively a BSC System.

The SSMG noted that any decision regarding procurement of a dual notification service would be entirely the responsibility of ELEXON, and that any 'instruction' from the SSMG in this matter, would be beyond the vires of the SSMG. Thus the SSMG would be limited to consideration of the potential for the dual notification service to be provided by a provider other than the BSC Central Service Agent.

The SSMG noted that there were a number of issues associated with the (external) procurement of a dual notification service. These can be summarised as follows:

- The requirement for ELEXON to establish and maintain a new contract for an additional BSC Agent. It is expected that establishing and maintaining such a contract would require significant ELEXON resource.
- The implementation of an external dual notification service as a BSC System will materially increase the complexity of the ECVAA System Failure process. Very clear and unambiguous definitions of failure would be required in order to ensure that the ECVAA System Failure process is identified correctly and then recovered from appropriately.
- To ensure that there are no rejections on the grounds of business validation by the ECVAA following successful matching in the dual notification provider, it is expected that the dual notification provider may be required to emulate the ECVAA validation rules.
- A more complex issue surrounding validation is the validation required to be undertaken to refuse notifications as a consequence of credit default and to reject Metered Volume Reallocation Notifications (MVRNs) where either one of the counterparties is in credit default (refusal) or the MVRN requires an allocation in excess of 100%. These validations require information at a detailed level from the ECVAA, on a real time basis, in order that a notification is not matched and then rejected on these grounds.
- Potentially new interfaces from the (external) dual notification service provider into the ECVAA will be required to ensure that the notifications received by the external provider by Gate Closure can get into the ECVAA and be processed as if they were received by the ECVAA in time for Gate Closure.

The SSMG raised these points, which would need to be addressed should ELEXON procure the dual notification service from a provider other than the existing BSC Central Service Agent.

However it should be noted that the solution preferred by the SSMG, as set out in this Modification Report, precludes provision of the solution by any provider other than the BSC Central Service Agent, on the basis that it provides a solution that provides additional functionality in the solution, such as

enhancements to the single notification process and consistency between single and dual processing, that could not be provided by an 'external' provider.

2 INTRODUCTION

This Report has been prepared by ELEXON Ltd., on behalf of the Balancing and Settlement Code Panel ('the Panel'), in accordance with the terms of the Balancing and Settlement Code ('BSC'). The BSC is the legal document containing the rules of the balancing mechanism and imbalance settlement process and related governance provisions. ELEXON is the company that performs the role and functions of the BSCCo, as defined in the BSC.

This Modification Report is addressed and furnished to the Gas and Electricity Markets Authority ('the Authority') and none of the facts, opinions or statements contained herein may be relied upon by any other person. An electronic copy of this document can be found on the BSC website, at www.elexon.co.uk

3 HISTORY OF THE MODIFICATION

Modification Proposal P98 has been assessed by the SSMG, and the detail of the assessment is provided in the Assessment Report for Modification Proposal P98 (Reference 1).

4 DESCRIPTION OF PROPOSED MODIFICATION

4.1.1 Single Notification

Under the current single notification process, the Authorisation is set up for the nominated ECVNA to notify on behalf of a specified pair of counterparties, and their nominated Energy Accounts. Any notification received from the Authorised ECVNA is validated by the ECVAA to ensure that the counterparties and nominated Energy Accounts are those that the ECVNA is authorised for.

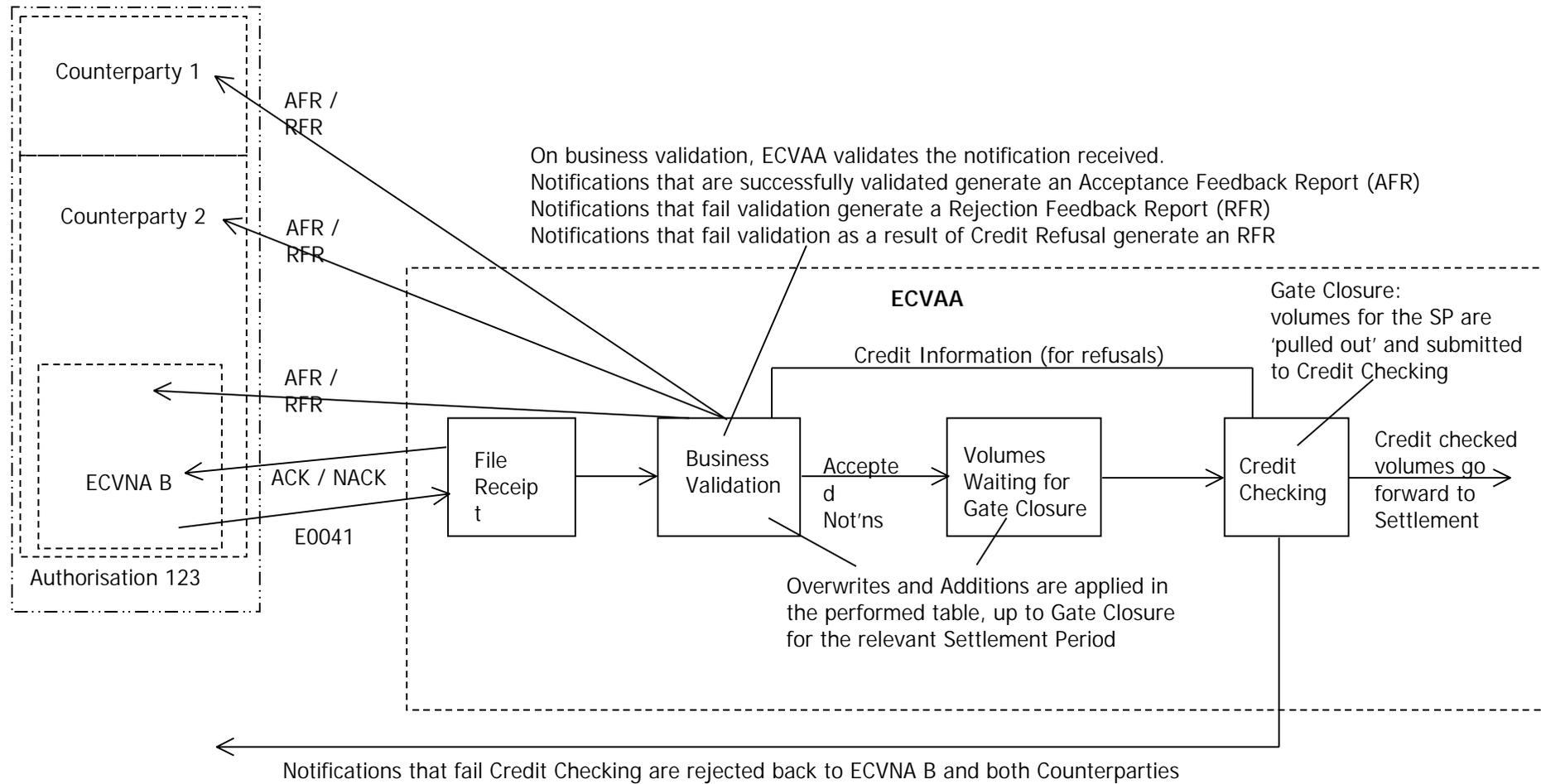
Where the submission is valid, an Acceptance Feedback Report (AFR) is generated, containing the detail of what has been accepted by the ECVAA. The contract volumes are placed in a table waiting for Gate Closure for the Settlement Period. At this point, they can be overwritten and / or added to, up to Gate Closure for the relevant Settlement Period.

At Gate Closure for each Settlement Period, the contract volumes for that Settlement Period are 'pulled out' and the Credit check performed. Where there is to be a rejection on the grounds of credit default rules, then the relevant contract volumes are rejected, using the Rejection Feedback Report (RFR). The same process is used for MVRNs, noting that there is additional validation to ensure that the MVRN has not exceeded 100% reallocation.

At the end of each Settlement Day, the ECVAA provides a report containing a summary of all the notifications processed by ECVAA for that Settlement Day to the relevant notification agents and counterparties. At specified periods during each Settlement Day, the ECVAA also generates a Forward Contract Report (often referred to as the 7 day report), to all counterparties (not notification agents) which provides a view (for each counterparty) of their contract positions for the current day and next seven calendar days.

These reports, plus any Rejection Feedback Reports and Acceptance Feedback Reports for individual submissions, provide the information required by BSC Parties to determine their contract position at any time. This process is represented by the following diagram entitled 'Current Notification Process'.

Current Notification Process



4.1.2 Dual Notification

Dual notification is the process of notifying whereby both parties to the notification (via their nominated notification agent) submit their agreed contract volumes to the BSC Central Service Agent, where the volumes are matched, and submitted to settlement, as an agreed position. This ensures that both Parties have effectively agreed the contract volumes that go forward into Settlement.

Under dual notification, the Authorisation is set up such that each counterparty nominates an ECVNA, to notify on behalf of that counterparty under dual notification (the expectation is that in the majority of cases, the notification agent will be the same organisation as the counterparty). The Authorisation will specify the pair of counterparties, their nominated Energy Accounts and their nominated ECVNA.

It is expected that both ECVNAs will use a common, agreed identifier, in order that the notifications submitted against that Authorisation can be recognised by the ECVAA and the associated contract volumes applied to the correct counterparty and Energy Account combination.

Any notifications received from the Authorised ECVNAs are validated by the ECVAA to ensure that the counterparties and nominated Energy Accounts are those that the ECVNA is authorised for.

Under dual notification, if a pair of counterparties wishes to use single notification, then the Authorisation is set up such that each Counterparty nominates the same ECVNA, to notify on their behalf. The Authorisation will specify the pair of counterparties, their nominated Energy Accounts and the nominated ECVNA.

As the Authorisation process is a paper based manual process, it is not envisaged that this will require material changes to the Authorisation process for Parties.

Each ECVNA indicates whether the contract volume notification(s) submitted are additional to those already in the database, or overwrites for existing volumes. It should be noted that in order to obtain a match, each ECVNA must specify additive or overwrite, using the agreed identifier.

Under dual notification, Parties and notification agents, will be able to submit contract volumes via a web based interface, allowing them secure access to their contract positions. The submission of contract volumes via the web based interface will also apply to single notification.

On receipt of the notification, ECVAA validates the submission. If any part of the submission fails validation, or is to be refused under Credit Default rules, then the contract volumes for the affected Settlement Periods are rejected individually, notified in the Rejection Feedback Report.

Where the submission is accepted, the contract volumes are submitted for matching, (noting that where the notification is the first of the two to be submitted, then it is expected that a 'no match' report will be generated for the entire notification).

Where there are matches for individual Settlement Periods, then an Acceptance Feedback Report (AFR) is generated, containing the detail of what has been accepted and matched by the ECVAA. A 'no match' report can be generated for the Settlement Periods that are not matched.

The transaction references in the reports will provide the sequence of acceptances and no matches, and these can be seen on the web view.

The matched contract volumes are placed in a table waiting for Gate Closure for the Settlement Period. At this point, they can be overwritten and / or added to, up to Gate Closure for the relevant Settlement Period.

P98 also seeks to implement a web based view of the matching of notifications, this could look as follows:

For each Authorisation Reference (ECVNAA Id)

Counterparty 1:	Counterparty 2:	Matched Volumes:
Volumes Submitted against each Settlement Period	Volumes Submitted against each Settlement Period	Latest matched volume against all SPs
Transaction of last submitted notification	Transaction of last submitted notification	N/A

i.e. each BSC Party can see their position for each Authorisation they have, and each counterparty.

This web based view could be applied to single notification as well, such that Parties can determine their position at all times from the viewer.

At Gate Closure for each Settlement Period, the contract volumes for that Settlement Period are 'pulled out' and the Credit check performed. Where there is to be a rejection on the grounds of credit default rules, then the relevant contract volumes are rejected, using the Rejection Feedback Report.

The same process is used for MVRNs, noting that there is additional validation to ensure that the MVRN has not exceeded 100% reallocation.

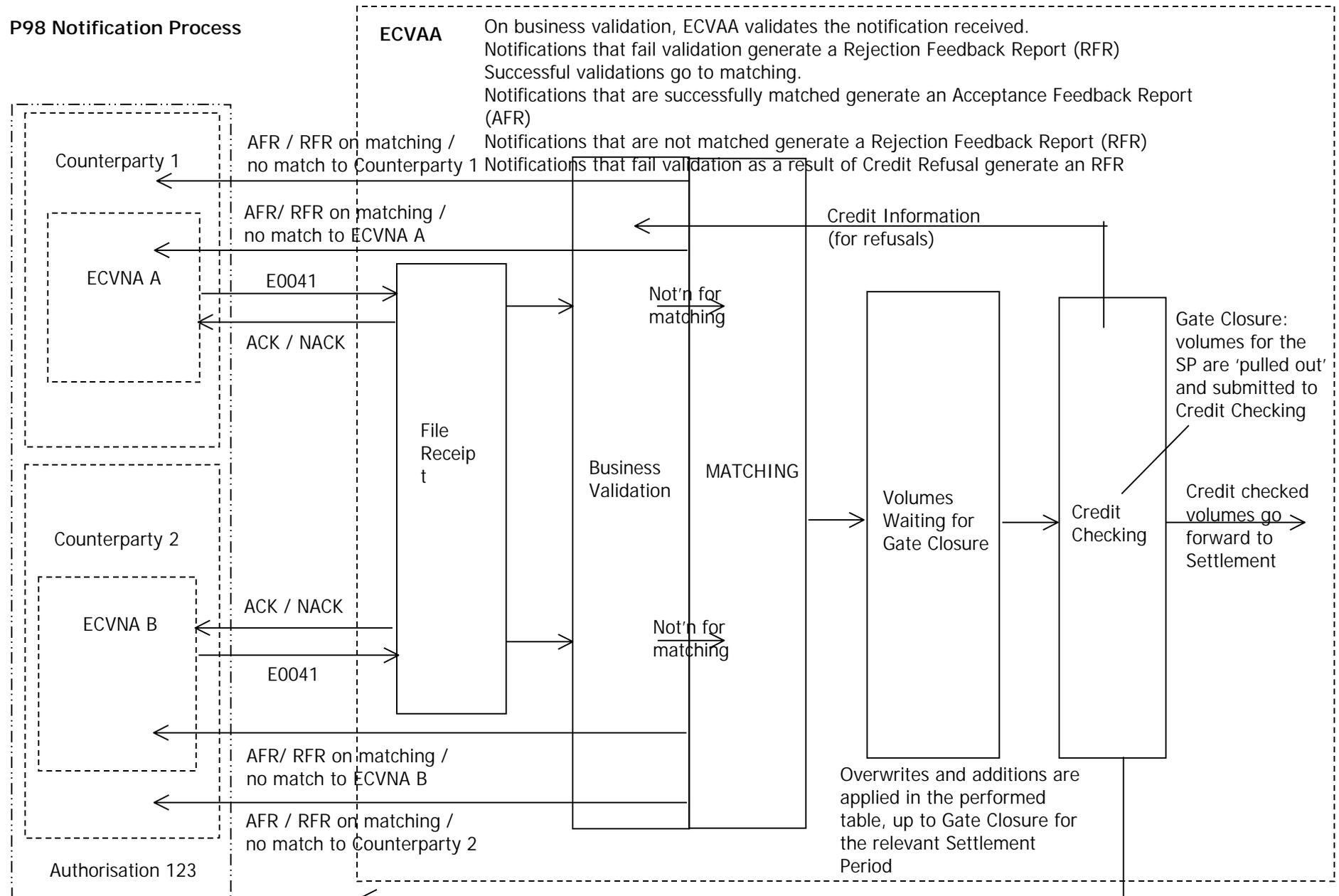
At the end of each Settlement Day, the ECVAA provides a report containing a summary of all the notifications processed by ECVAA for that Settlement Day to the relevant notification agents and counterparties.

At specified periods during each Settlement Day, the ECVAA also generates a Forward Contract Report (often referred to as the 7 day report), to all counterparties (not notification agents) which provides a view (for each counterparty) of their contract positions for the current day and next seven calendar days.

These reports, plus any Rejection Feedback Reports and Acceptance Feedback Reports for individual submissions, provide the information required by BSC Parties to determine their contract position at any time. However, it should be noted that the web based reporting will also provide a real time (secure) view of the contract position for each counterparty and authorisation.

This process is represented by the following diagram entitled 'P98 Notification Process'.

P98 Notification Process



4.1.3 Dual Notification Process: No Change to ECVAAs Functionality

As noted above, the intent is to implement dual notification alongside the current single notification process, attempting to minimise the impact on the single notification processing, whilst keeping the two processes as similar as possible, in order to minimise impact on those Parties choosing to use dual notification.

On this basis, it should be noted that there is no change to the following ECVAAs functionality required to support dual notification:

- **Credit Procedures** – Credit default, credit checking and other related procedures. Since the dual notification submissions will not be treated any differently to currently, other than the requirement to match contract volumes prior to submission onwards within ECVAAs, the process will be the same as that currently defined, undertaken to the same timescales.
- **Authorisation Terminations and Other Authorisation Activities** – All other Authorisation activities, such as requesting the termination of an Authorisation, requesting Key changes etc. will remain as currently defined.
- **Use and Handling of File Sequence Numbers (FSNs)** – Since the dual notification submissions will not be treated any differently to currently, the process will be the same as that currently defined, noting the requirement to receive and process reports in the order of submission, and return feedback reports (AFRs and RFRs) in the correct sequential order. Handling of out of sequence files will not require amendment specific to dual notification. Therefore it should be noted that the same issues with out of sequence files will exist with dual notification as with the current single, but that the issues are unlikely to be exacerbated by use of dual notification.
- **Clock Change Rules** - Since the dual notification submissions will not be treated any differently to currently, other than the requirement to match contract volumes prior to submission onwards within ECVAAs, the processing of clock change notifications will be the same as that currently defined.
- **Forward Contract Report** – The Forward Contract Report (ECVAAs – I022, E0222) will continue to provide a forward looking view of the contract volumes held by the ECVAAs for each BSC Party, against Authorisation and counterparty. Under dual notification, the forward contract report will contain this information for the contract volumes that have been matched, and therefore no amendment to usage or format is envisaged. It is not intended to amend the Forward Contract to report unmatched volumes.
- **End of Day Report** – The End of Day Report (ECVAAs – I014, E0141) provides a view of the notifications processed by ECVAAs during the preceding Settlement Day, and this supports the dual notification functionality. Therefore, it is not intended that the format or usage of this report be amended.

4.1.4 Amendments to the Single Notification Process

There are potential enhancements to the current single notification process that are to be implemented to bring it in line with the dual notification process. These can be summarised as follows:

- Functionality to specify who wishes to receive Acceptance Feedback Reports and Rejection Feedback Reports for each Authorisation.

For a single notification, each Authorisation specifies the counterparties and the submitting notification agent. Currently, all of these three will each receive RFRs and AFRs, as generated. However, where the notification agent is the same as one of the counterparties, this duplicates the reports received, and the implementation of dual notification has the potential to increase this duplication further by introducing another notification agent.

Therefore, as specified in section 4.2.2, the parties / notification agents to receive the AFRs and RFRs can be specified. For example, where counterparty 1 is the same party as the notification agent, then the counterparty can choose not to receive the RFRs and AFRs, instead these can be received and acted upon by the notification agent.

- ECVAA business validation at Settlement Period level.

Currently if any part of a notification submitted fails business validation, the notification is rejected in entirety. However, as specified in section 4.2.3, dual notification proposes to validate at Settlement Period level, such that Settlement Periods that pass validation are accepted, and only those Settlement Periods that fail validation are rejected. This does not require amendment to the format of the RFRs and AFRs, only to the interpretation.

- Web Based View of Contract Positions.

Dual notification proposes to implement a facility to view contract positions on the internet, as a web based viewing facility. As specified in section 4.2.7, contract positions will be available to view for each counterparty against each Authorisation.

- Web Based Entry of Contract Positions.

Dual notification proposes to implement a facility to submit contract positions via the web front end of the web based view of contract positions, i.e. on the internet. As specified in section 4.2.8, contract positions will be available for amendment for each counterparty against each Authorisation.

- Low Grade Back up where the High Grade Service fails.

The BSC Central Service Agent noted that one way of dealing with the increased volumetrics, without degrading the service is to restructure such that all 'IO' reports (i.e. automated reports in and out of the BSC Central Service Agent) are moved to the low grade server, such that there is a high grade and low grade link. This has the added advantage that where the high grade service fails currently, a cut over process is required to the low grade. However, with the proposed configuration, this would not be the case, as the reports would be there, and there would be no requirement to cut over.

4.2 Dual Notification Process

See attached document 'MR098 Section 4_2'.

5 LEGAL TEXT TO GIVE EFFECT TO THE PROPOSED MODIFICATION

For the legal drafting to support Proposed Modification P98 see attached document 'P098RR_Proposed Legal Text'.

6 SUMMARY OF REPRESENTATIONS

Nine responses (on behalf of 37 Parties) were received in respect of the draft Modification Report for Modification Proposal P98. In summary:

- Seven responses (35 Parties) supported the provisional recommendations contained within the draft Modification Report, namely that the Proposed Modification should not be made;
- One responses (1 Party) did not support the provisional recommendations contained within the draft Modification Report; and
- One response (1 Party) made no comment in respect of the draft Modification Report.

The consultation responses contained no new, substantive arguments.

A number of respondents referenced the arguments raised during the Assessment Procedure in support of their responses, specifically response P98_DR_005 (Barclays Capital) which indicates support of Proposed Modification P98 and therefore does not support the provisional recommendations set out in the draft Modification Report, and response P98_DR_004 (Powergen) which supports the provisional recommendation in the draft Modification Report that the Proposed Modification should not be made.

ANNEX 1 – REPRESENTATIONS

Representations were received from the following parties:

No	Company	File Number	No. BSC Parties Represented	Support Recommendations
1.	British Gas Trading	P98_DR_001	1	YES
2.	SEEBOARD	P98_DR_002	1	YES
3.	Aquila Networks	P98_DR_003	1	NO COMMENT
4.	Powergen	P98_DR_004	15	YES
5.	Barclays Capital	P98_DR_005	1	NO
6.	Scottish Power	P98_DR_006	4	YES
7.	LE Group	P98_DR_007	7	YES
8.	British Energy	P98_DR_008	3	YES
9.	Scottish and Southern	P98_DR_009	4	YES

P98_DR_001 – British Gas Trading

Re: Modification Proposal P98 – Dual Notification of Contract Positions

Thank you for the opportunity of responding to this draft modification report considering Modification Proposal P98. British Gas Trading (BGT) does not support the Modification Proposal and does not believe this would better facilitate Applicable BSC Objectives (c) or (d). BGT were supportive of the principle of dual notification at Go-Live and still are. However, BGT believe that the implementation costs of Modification Proposal P98 are cost prohibitive and the perceived benefits do not justify the additional costs.

The existing market provisions for contract notification is understood by the industry and is working reasonably well. In addition the implementation of Change Proposal (CP) 755 has resulted in enhanced

ECVAA reporting. This enhancement has provided a facility that allows for discrepancies with contract notifications to be identified in a timely manner. Thereby allowing BSC Parties time to undertake corrective action to amend their position.

Furthermore the nature of the proposal, which is proposing implementation on a voluntary basis, will lead to the running of parallel contract notification schemes. As well as the cost of implementing and maintaining a single and dual notification process this will also introduce added complexity to the market place and increase the risks associated with notifying contract positions.

Yours sincerely

Mark Manley, Contract Manager

P98_DR_002 – SEEBOARD

With respect to draft modification report for P98 (Dual Notification of Contract Positions) dated 9th January. We agree with recommendations in section 1.1 of that report that this modification should not be made to BSC.

Dave Morton

SEEBOARD Energy Limited

P98_DR_003 – Aquila Networks

Please find that Aquila Networks Plc response to P98 Consultation on draft Modification Report is 'No Comment'.

regards

Rachael Gardener

Deregulation Control Group & Distribution Support Office

AQUILA NETWORKS

P98_DR_004 – Powergen

P098 Report Comments

On behalf of Powergen UK plc*, we thank you for the opportunity to comment on the Draft Report for Modification Proposal P098 – Dual Notification

Powergen supports the Panel's decision to reject this modification. This support is based on:-

- Cost - the solution proposed is probably the cheapest that could be arrived at, but is still a very expensive way of solving the problem that the proposer perceives – a risk most parties view as having a very low likelihood of occurring.
- Missing the main problem - Operational experience has shown that the main problems with Energy Contract Volume Notifications (ECVNs) occur on intra-company balancing trades, and this modification offers no assistance in this area.

- Better Alternatives - The majority of disputed inter-party notifications identified prior to gate closure are the result of either:-
 - one of the two parties having recorded trade details incorrectly. This issue would be better addressed by parties investing in bi-lateral trade confirmation systems (outside any BSC related systems)
 - the notifying party having problems with their notification submission system, in which case the current single notification approach provides a backup that would not be available under dual notification.
- Operational Complexity – providing alternatives will increase the chances of mistakes being made, especially at times of stress.

Tim Johnson

Powergen Energy Trading

*Powergen UK plc, Powergen Retail Limited, Diamond Power Generation Limited, Cottam Development Centre Limited, TXU Europe Drakelow Limited, TXU Europe Ironbridge Limited, TXU Europe High Marnham Limited, Midlands Gas Limited, Western Gas Limited, TXU Europe (AHG) Limited, TXU Europe (AH Online) Limited, Citigen (London) Limited, Severn Trent Energy Limited (known as TXU Europe (AHST) Limited), TXU Europe (AHGD) Limited and Ownlabel Energy Limited.

P98_DR_005 – Barclays Capital

P98 Report Comments from Barclays Capital - 30 January 2002

Barclays Capital supports the proposed modification P98 and therefore disagrees with the Panel's recommendation that P98 should not be made.

Notification errors are the single largest risk associated with trading UK power. While market participants invest significant time and resources in attempting to avoid notification errors, the risk cannot be completely eradicated or shared effectively under bilateral contracts between market counterparties. In particular, there are possible – albeit unlikely – scenarios associated with deliberate mis-notification and a market participant's entry into administration, which could result in massive, unlimited liability of market participants to imbalance charges. This constitutes a major systemic risk to the UK power system, which could result in the cascading failure of several market participants. Dual notification of contracts offers the scope for removing this risk and we therefore believe that the benefits clearly outweigh the development costs. Dual notification would also promote competition in the market by reducing the cost of entry and operation imposed by single notification and by removing the unlimited liability for notification errors (which in itself could deter a potential entrant). Below we set out some brief comments on the rationale for recommendations in Section 1 of the Draft Modification Report.

Potential for Exposure to Unlimited Liability from Single Notification/Cost-Benefits from Implementation of Dual Notification

Section 1.3.2 (Cost Benefits from Implementation of Dual Notification) notes that “the assessment as to whether the implementation of dual notification is cost beneficial comes down to whether it is believed that the risk of exposure to unlimited settlement liability is manageable or not”. While we accept that the decision swings on the perception of the systemic risk involved, we would stress that the risks that dual notification seeks to avoid are in fact - and not merely in opinion - unmanageable and unlimited. Even the best managed market participant will make notification errors, will be vulnerable to sabotage

and will not be able to recover money under a contract which has been terminated. The decision should therefore not swing on the weight of perception on whether these risks can or cannot be managed, but on an objective assessment of the probability of a major systemic notification error and the attendant costs. In our view, the likelihood of a major problem, while small, is sufficiently large to justify the implementation of P98.

Incentives to Maintain Robust Systems

Since dual notification as proposed to P98, adds to – and does not subtract from - the current notification procedures, we cannot accept that “the consequences of Party notification system failure are potentially higher under dual notification”. In particular, having dual notification as an option would not prevent counterparties resorting to single notification were they to experience system problems with dual notification. Moreover, the possibility of web-based confirmations would provide an additional alternative in the event that a participant’s main systems failed. It is therefore difficult to conceive of an instance under which participants face higher risks for system failure than under the current system. At the same time, since dual notification leads to a clearer attribution of responsibility for notification errors, participants will retain strong incentives to have robust notification systems.

Notification (Commercial) Disputes Resolution

One of the main benefits of dual notification is that it clearly delineates which counterparty is at fault for a notification error, ie, the counterparty notifying volumes that differ from the agreed commercial volumes is at fault. Under single notification, however, participants bear a dual responsibility to notify correctly and to check that notifications made on their behalf are correct. This dual responsibility often makes it difficult to assign responsibility for erroneous notifications, which can lead to drawn out disputes as to which counterparty should bear the costs of the error. This uncertainty is absent under dual notification and we therefore disagree with the contention of some members of the SSMG that “it will require as much effort to assign culpability for incorrect notifications under dual notification as it does under single.”

Enhanced ECVAA Reporting

While enhanced ECVAA reporting may reduce the incidence of ongoing operational notification errors, it does not address the systemic risks posed by malicious notification and/or the events surrounding the insolvency or entry into administration of a market participant. In our view, while enhanced reporting is useful, it does not address the fundamental risk that P98 seeks to avoid.

P98_DR_006 – Scottish Power

P98 Draft Modification Report Comments

For and on behalf of: - *Scottish Power UK plc; ScottishPower Energy Trading Ltd.; Scottish Power Generation plc; ScottishPower Energy Retail Ltd.; SP Transmission plc; SP Manweb plc*

With reference to the above, we wish to reiterate the view which we have previously expressed in rejection of P98, that the costs of the Mod are substantial, both to Central Systems and to Parties and do not represent an efficient use of funds given the potential benefits. We have also identified that there may be drawbacks in adopting the dual notification method both in terms of technical compatibility and operational flexibility.

We therefore maintain the view that P98 does not satisfy the Applicable BSC Objectives and agree with the Panel's recommendation that it should not be made.

I trust that you will find these comments helpful. Nonetheless, should you require further clarification of any of the above, please do not hesitate to contact me.

Yours sincerely,

Man Kwong Liu

Calanais Ltd.

P98_DR_007 – LE Group

Thank you for the opportunity to comment. We supported the Panel's unanimous recommendation to reject P98 at BSC Panel Meeting No.54, on 12th December 2002, and our views have not changed on consideration of the Draft Modification Report.

We believe that the risks of exposure to unlimited settlement liability are very low and can be considerably mitigated by the use of various mechanisms, including the enhanced reporting provided by alternative P4/CP755. Thus when the Modification is considered against the costs of nearly two million pounds for BSC Central Service Agent development and implementation costs, plus the estimated Elexon effort of approximately 500 man days and the significant costs of implementation for individual market participants – we strongly believe that the Modification goes against the applicable BSC Objective 3(d), "Promoting efficiency in the implementation and administration of the balancing and settlement arrangements."

Regards

Rob Hetherington

Wholesale Market Analyst, Energy Strategy and Regulation, LE Group

This response represents the following BSC Parties;

EPN Distribution Ltd, London Electricity plc, London Electricity Group plc, Jade Power Generation Ltd, London Power Networks plc, Sutton Bridge Power, West Burton Ltd

P98_DR_008 – British Energy

To: Modifications Secretary

From: Rachel Lockley

Date: 30 Jan 2003

British Energy supports the recommendation of the Panel that the Proposed Modification P98 should not be made.

The potential for exposure to unlimited settlement liability under the present arrangements, which is at the heart of this modification proposal, is we believe, manageable by other mechanisms (checking of notification reports, contractual and legal recourse). The cost of implementing dual notification is a very significant factor. The costs to industry from amending notification processes and renegotiating the Grid Trade Master Agreement (GTMA), £1,888,540, (excluding ELEXON effort of approximately 500 man days) outweighs any perceived benefits.

While some have argued that reducing notification risk may improve competition in the sale and purchase of electricity (Objective 3(c)). British Energy considers that the costs associated with the implementation of dual notification results in a decrease in the efficiency of the implementation of the balancing and settlement arrangements (Objective 3(d)) which far outweigh any benefits to competition. The Proposed Modification P98 does not therefore better facilitate achievement of the Applicable BSC Objectives.

Regards

Rachel Lockley

on behalf of British Energy Power and Energy Trading, Eggborough Power, British Energy Generation

P98_DR_009 – Scottish and Southern

This response is sent on behalf of Scottish and Southern Energy, Southern Electric, Keadby Generation Ltd. and SSE Energy Supply Ltd.

Further to your note of 9th January 2003, and the associated Modification Report for P98, we agree with the proposed BSC Panel recommendation to the Authority that this Modification Proposal P98 should not be made.

For the avoidance of doubt, we have come to this view based on a number of factors, including:-

- that a majority of parties do not support this Modification;
- there is insufficient justification for this proposed Modification;
- facilities are already available to mitigate the risk / exposure associated with single notification, such as check reports etc.;
- it should be up to parties to ensure their own processes / systems are robust;
- the cost and effort involved in implementing this Modification are significant, i.e. £1.8m central system costs, 500 man days of Elexon time, 64 weeks to implement, this being in addition to market participants own costs;
- the introduction of a dual notification processes will introduce complexity and runs the risk of being more confusing for market participants hence more, not less mistakes are likely to be made; and
- parties who don't use the dual notification facility should not be required to pay for it, rather the cost should be focused on those supporting this Modification / indicating they will use dual notification.

If the Modification Proposal P98 is approved, we agree with the proposed BSC Panel recommendation on the timing for the Implementation Date, as outlined in Section 1.1 of the Modification Report.

Regards

Garth Graham, Scottish & Southern Energy plc