



Direct Dial: 020-7901 7052

26 February 2003

The National Grid Company, BSC Signatories and
Other Interested Parties

Our Ref: MP No P99

Dear Colleague,

Modification to the Balancing and Settlement Code (“BSC”) - Decision and Direction in relation to Modification Proposal P99: “Changes to Accreditation and the PARMS Serials and Standards, resulting from the Performance Assurance Framework (PAF) Review (Phase 1)”

The Gas and Electricity Markets Authority (the “Authority”)¹ has carefully considered the issues raised in the Modification Report² in respect of Modification Proposal P99, “Changes to Accreditation and the PARMS Serials and Standards, resulting from the Performance Assurance Framework (PAF) Review (Phase 1)”.

The Balancing and Settlement Code Panel (the “Panel”) recommended to the Authority that Modification Proposal P99 should be made with an Implementation Date of 20 January 2004, if an Authority determination is received prior to 1 March 2003; or 1 April 2004 if an Authority determination is received on or after 1 March 2003 but prior to 1 July 2003.

Having considered the Modification Report and the Panel’s recommendation and having regard to the Applicable BSC Objectives and the Authority’s wider statutory duties, the Authority has decided to direct a Modification to the BSC in line with the Modification Proposal P99.

This letter explains the background and sets out the Authority’s reasons for its decision. In addition, the letter contains a direction to The National Grid Company plc (“NGC”) to modify the BSC in line with Modification Proposal P99, as set out in the Modification Report.

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

² ELEXON document reference P099MR10, Version No. 1, dated 24 January 2003.

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

Background

In September 2001 the Panel requested a review of the Performance Assurance Framework (“PAF”) within the Trading Arrangements, with a view to reducing the costs incurred by BSC Parties while maintaining or improving the level of assurance provided. Phase 1 of the PAF Review focused on the techniques of Accreditation, Audit, Entry Processes and the Performance Assurance and Reporting and Monitoring System (“PARMS”). Each technique was analysed by an expert group comprised of industry participants representing a range of market roles.

The findings of the PAF Review were presented to and approved by the Panel in April 2002. An industry consultation was held to seek the views of participants to the changes. The results of the consultation were in general favourable to the recommendations of the PAF Review. Therefore on 2 September 2002, British Gas Trading raised Modification Proposal P99 in order to implement the PAF Review findings.

The Modification Proposal

Modification Proposal P99 seeks to progress the changes proposed by the PAF Review in relation to three of the Performance Assurance techniques used within the Trading Arrangements, namely Accreditation, Entry Processes and PARMS Serials and Standards. The justification for the Modification Proposal was that it would better facilitate achievement of the Applicable BSC Objectives³ C3 (3) (c) and (d).

Of the four techniques considered in Phase 1, only the Accreditation and PARMS improvements were recognised as requiring a Modification to the BSC. The Entry Process improvements, while only requiring changes to Code Subsidiary Documents rather than the BSC itself, were included within the scope of Modification Proposal P99 so as to ensure that where possible the majority of the Phase 1 improvements were approved and progressed as a whole. The Requirements Specification for Modification Proposal P99⁴ explains in detail the proposed changes to Accreditation, Entry Processes and PARMS Serials and Standards. The Audit improvements were not included within the scope of Modification Proposal P99 as they were recognised as being solely the responsibility of the Panel, which agreed to progress this change separately.

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

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

⁴ Document P99RS10, Version 1.0, dated 17 October 2002

The Proposer considered that the proposed changes to Accreditation would serve to reduce barriers to entry by making the process more straightforward both for new and existing participants, thereby promoting competition and so better facilitating Applicable BSC Objective (c). The Proposer also believed that improved monitoring and reporting would encourage increases in performance standards of all participants, helping to improve the overall efficiency of the Trading Arrangements and so better facilitate Applicable BSC Objective (d).

The Panel considered the Initial Written Assessment at its meeting of 12 September 2002 and agreed to submit Modification Proposal P99 to the Assessment Procedure. The Volume Allocation Standing Modification Group (the "Group") considered the Modification Proposal at two meetings, which were held on 27 September 2002 and 1 November 2002. After reviewing the consultation responses received, the Group agreed that it was prepared to support the Modification Proposal in principle, but that it needed to confirm the likely extent of the participant costs before making a recommendation to the Panel.

The Group presented an Assessment Report on 14 November 2002 with a recommendation to the Panel that the Assessment Procedure be extended by one month so as to allow the Group to request an additional industry impact assessment and determine the level of participant support for Modification Proposal P99. The Panel agreed with the Group's recommendation.

The Group met on 2 December 2002 to consider the responses to the industry consultation and the impact assessment. The Group agreed that the revised system, being more flexible to change than the current system, should continue to provide a useful monitoring and reporting service for years to come and so would be a worthwhile development to the Trading Arrangements. The Group estimated that while the industry costs for Modification Proposal P99 would be large (estimated at £1m - £3m in total), when considered on a per Metering System basis it agreed that the costs would be reasonable. The Group considered that over the long term the potential benefit to industry could amount to a saving of between £2m - £5m per year.

Having taken these issues into account, the Group agreed that Modification Proposal P99 would better facilitate Applicable BSC Objectives (c) and (d). A revised Assessment Report was then presented to the Panel on 12 December 2002, with the recommendation that Modification Proposal P99 should be made.

ELEXON published a draft Modification Report on 20 December 2002, which invited respondents' views by 3 January 2003.

Respondents' views

ELEXON received eight responses to the consultation on Modification Proposal P99. Four responses (representing 9 Parties and 1 Party Agent) expressed support for the Proposed Modification. Two respondents (representing 10 Parties) were not in favour of the Proposed Modification. The remaining two respondents (representing 2 Parties) provided no comment.

Those respondents who did not support the recommendations argued mainly on the grounds of costs. One Party argued that it would like to see proper justification of the costs of the PARMS work, particularly on the costs of the PARMS Serials. Another Party argued that whilst it supported the review of PARMS Serials in principal, it did not believe that the suggested benefits outweighed the costs of implementation.

The respondents' views are summarised in the Modification Report for Modification Proposal P99, which also includes the complete text of all respondents' replies.

Panel's recommendation

The Panel met on 16 January 2003 and considered Modification Proposal P99, the draft Modification Report, the views of the Modification Group and the consultation responses received. The Panel agreed with the recommendations and rationale put forward by the Group in support of its recommendation.

The Panel recommended that the Authority should approve the Proposed Modification and that, if approved, the Proposed Modification should be implemented with an Implementation Date of 20 January 2004, if an Authority determination is received prior to 1 March 2003; or 1 April 2004 if an Authority determination is received on or after 1 March 2003 but prior to 1 July 2003.

Ofgem's view

Having carefully considered the Modification Report and the Panel's recommendation, Ofgem considers, having regard to the Applicable BSC Objectives and its statutory duties, that Modification Proposal P99 will better facilitate achievement of Applicable BSC Objectives (c) and (d) as the changes to the Accreditation and Entry Processes will promote efficient competition and the changes to the PARMS will promote efficiency of Settlement.

Phase 1 of the PAF Review undertook a full assessment on the techniques of Accreditation, Audit, Entry Processes and the PARMS Serials and Standards. The objective of the review was to reduce the costs incurred by a range of BSC Parties whilst maintaining or improving the level of assurance provided. Modification Proposal P99 seeks to make changes to Sections J and S of the BSC, Code Subsidiary Documents, and the systems of BSCCo and participants.

Ofgem considers the changes to the techniques of Entry Processes and Accreditation should lessen the burden placed upon applicants (new and existing market participants). The Certification Agent's reduced role with low risk applicants and the Entry Process Agent's increased assistance to Suppliers should prove of benefit to all Parties. Ofgem accepts the Group's view that Accreditation and Entry Process scripts should ensure that the market is adequately protected against risk and provide simplified tests for the smaller Parties. This therefore facilitates the achievement of Applicable BSC Objective (c).

Of the current set of sixty-three serials, Modification Proposal P99 recommends the removal of fifty on the grounds that they are not currently used because, for example, it is not possible to collect accurate data or because other assurance techniques are more appropriate for the processes that require monitoring. Twenty-one new serials have been recommended for

inclusion to address the areas of assurance not currently covered by an existing serial. Implementation of Modification Proposal P99 results in the production of a new set of thirty-four serials.

Ofgem supports the Group's view that improvements in data quality aligned with the revised Supplier Charges will provide an increased assurance that the data entering Settlement is accurate. Furthermore, the submission by the Supplier Meter Registration Service of registration information direct to the BSCCo will reduce an unnecessary workload for each Supplier. Ofgem accepts the Group's assertion that the removal of certain data acquisition obligations will be of benefit, in particular to smaller Suppliers and new entrants. These improvements will help to improve the overall efficiency of the Trading Arrangements and so better facilitate the achievement of Applicable BSC Objective (d).

The two respondents who were opposed to the Modification Proposal P99 argued that the costs of implementation would outweigh the benefits to industry. The Group estimated a cost to industry of £1m – 3m in total and that the potential benefit to industry could amount to savings of between £2m - 5m per year. Whilst Ofgem acknowledges the concerns of the respondents, the identified benefits to the operational efficiency and data quality of settlement are significant. Ofgem notes that the cost-benefit analysis of Modification Proposal P99 was undertaken by the Group and based on Party responses to consultation. Ofgem accepts the Group's opinion that the overall cost of performance assurance will decrease, even if this is not the case for each performance assurance technique.

It should be noted that on the 16 October 2001 the Authority decided not to direct Modification Proposal P29 "Improve Efficiency of PARMS Reporting". It was the Authority's view that the implementation of Modification Proposal P29 prior to the completion of the PAF Review would pose an unquantifiable risk to the integrity of settlement. The Authority is satisfied that the PAF Review has given due consideration to the risks involved in alterations to the PARMS Serials so that it is now able to approve Modification Proposal P99.

The Authority's decision

The Authority has therefore decided to direct that the Proposed Modification P99, as set out in the Modification Report, should be made and implemented.

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

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

The Implementation Date for Modification Proposal P99 is 20 January 2004.

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 'Iain Osborne', written on a light-colored background.

Iain Osborne

Director of Supply

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