

4.5. MP Form

Modification Proposal – BSCP40/03	MP No: P274 <i>(mandatory by BSCCo)</i>
Title of Modification Proposal : Cessation of Compensatory Adjustments	
Submission Date <i>(mandatory by originator):</i> 29 September 2011	
Description of Proposed Modification <i>(mandatory by originator)</i> This Modification seeks to amend the Balancing and Settlement Code (BSC) so that it specifies that ‘crystallised’ errors cannot be compensated for in subsequent Settlement calculations. A direct consequence of this would be to remove the process of Gross Volume Correction (GVC). The BSC does not allow data that has already been finalised in Settlement to be changed except via the Trading Dispute process, but is otherwise silent on how crystallised errors can be treated. The options available where a crystallised error is identified are: <ul style="list-style-type: none"> • Perform a compensatory adjustment in subsequent Settlement via the GVC process so that the volumes in Settlement are accurate overall; or • Write off the crystallised error but adjust data so Settlement is accurate going forward, typically done at present by carrying out a dummy meter exchange. The Modification proposes that the BSC specifies that compensatory adjustment in subsequent Settlement cannot be employed for crystallised errors. This would be achieved by amending the relevant parts of the BSC, probably in Section S, ‘Supplier Volume Allocation’, and Section U, ‘Provisions Relating to Settlement’ (though this should be considered and confirmed as part of progression of this Modification). Consequent changes would be made to Code Subsidiary Documents, primarily BSCP504, ‘Non Half Hourly Data Collection for SVA ¹ Metering Systems Registered in SMRS ² ’, which sets out the provisions for compensating crystallised errors and the GVC process.	
Description of Issue or Defect that Modification Proposal Seeks to Address <i>(mandatory by originator)</i> This Modification contends that compensatory adjustment of volumes via the GVC process, as currently permitted by the BSC, materially compromises the extent to which Settlements accurately reflect the energy volumes supplied by Suppliers at particular periods, leading to the issues set out below. <u>Background:</u> Licensed Distribution System Operators (LDSOs) are required, through Standard Licence Condition 44B (Distribution Losses Reporting Regime), to use Settlement data to determine and report energy entering and energy exiting their networks in accordance with Regulatory Instruction and Guidance	

¹ Supplier Volume Allocation

² Supplier Meter Registration Service

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<p>(RIGs). This information is the primary input into the Distribution Loss Incentive Mechanism (DLIM), which is effected through Special Condition CRC³ 7 (Adjustment of licensee’s revenues to reflect distribution losses performance).</p> <p>LDSOs are required to report this information for the Distribution Price Control Review 5⁴ (DPCR5) so that the DLIM for this period can operate, and for the DPCR4⁵ period so that the DLIM for this period can be closed down and so that the DLIM targets for the DPCR5 period can be set.</p> <p>The incentive / penalty was £48/MWh for the DPCR4 period and is £60/MWh for the DPCR5 period. As a consequence, the financial implications of the DLIM for each LDSO can run into many £100s millions for each 5 year price control period.</p> <p>Determination of the inputs to the DLIM – both in terms of target setting and of performance measurement – is based on Settlement data. As a consequence, the DLIM is reliant on the quality of this data. More specifically, effective operation of the mechanism is reliant on the Settlement data used to set the targets being consistent with the Settlement data used to measure performance.</p> <p>However, the scale of Supplier adjustments to Settlement data in the 14 months reconciliation window increased significantly in the five year DPCR4 period. The principal reason for this was an increased focus by Suppliers in addressing Settlement data quality issues using a variety of techniques currently permitted under the BSC. This has created an inconsistency between the basis of the target setting and performance measurement components of the DLIM. For DPCR4, this is having a very material impact on LDSOs – running into £10s millions for most and greater than £100 million for some. Ofgem is soon to consult on the most appropriate means of addressing this for DPCR4.</p> <p>LDSOs are very concerned that such issues could impact the operation of the DLIM in DPCR5 in a similar manner, with comparable financial implications. This creates uncertainty for LDSOs in their regulated allowable revenue and uncertainty for Suppliers in the Distribution Use of System (DUoS) costs they will incur. Impacts such as more volatile energy prices and / or increased energy prices could also affect consumers, though this is outside the scope of the BSC.</p> <p>LDSOs and Suppliers set up an industry working group under the Distribution Charging Methodology Forum (DCMF) to consider these issues. These ran over an 11 week period from June to August. This group concluded that the primary issue lies with the design of the DLIM. However, Ofgem has indicated that there is no scope for making any fundamental changes to the DLIM effective in DPCR5. Consequently, LDSOs want to ensure, to the extent that it is possible, that Settlement data better supports operation of the DLIM.</p> <p><u>Issue:</u> The increased level of adjustments to Settlement data described above have been effected by Suppliers using a range of techniques currently permitted under the BSC. One such technique, purportedly used</p>	

³ Charge Restriction Condition.

⁴ Running for the 5 year period starting on 1st April 2010.

⁵ Running for the 5 year period ending on 31st March 2010.

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<p>extensively by some Suppliers, is “Gross Volume Correction” (GVC).</p> <p>GVC compensates for volume errors that have crystallised in the Final Reconciliation (RF) run by introducing an equal and opposite error in periods that have not yet been subject to the RF run. This is on the basis that where an error has occurred it is better to have the correct volume settled, regardless of whether the error volume is associated with the actual period (days, months and, sometimes, years) in which it accrued. As a consequence the extent to which Settlement reflects the energy flows on the days being settled is compromised materially.</p> <p>GVC was legitimised by Modification P176 in 2005, largely on the grounds of efficiency, in that it would reduce the need for Trading Disputes to deal with errors post RF. This Modification contends that the broader implications of compromising the extent to which Settlement reflects actual energy flows of particular periods may not have been fully appreciated under P176 and should be considered further.</p> <p>Use of GVC is a major issue for the DLIM as it precludes adequate determination of when energy flows took place. This creates uncertainty for LDSOs in their regulated allowable revenue and uncertainty for Suppliers in the DUoS costs they will incur. This uncertainty could ultimately impact consumers, though this is outside the scope of the BSC.</p> <p>In addition, GVC has a number of adverse implications under the BSC, including:</p> <ul style="list-style-type: none"> • New entrants having volumes attributed to them that relate to periods before they started trading (through the effect of GSP Group Correction Factor on the compensatory error volume) – which acts a deterrent for new entrants and so inhibits effective competition; • Suppliers (big and small alike) having volumes attributed to them that relate to periods of cheaper wholesale energy prices (through the effect of GSP Group Correction Factor on the compensatory error volume) – which inhibits effective competition; and • LDSOs being unable to produce suitable forward looking Line Loss Factors for use in Settlement (as these are based on historical Settlement data) – which impacts the accuracy of Settlements and so inhibits effective competition. <p>The likely impact of the rollout of Smart Metering should also be considered. Smart Meters should ultimately provide for more accurate Settlement and fewer errors, experiences from rollouts elsewhere in the world suggest that introduction of Smart Meters can identify errors that had gone undetected. The rollout of Smart Meters in Great Britain could result in many errors being detected and if such errors were addressed using GVC the issues described above – for the DLIM and the BSC – would be exacerbated.</p>	
<p>Impact on Code <i>(optional by originator)</i> BSC Sections S and U.</p>	

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Impact on Core Industry Documents or System Operator-Transmission Owner Code <i>(optional by originator)</i> None.	
Impact on BSC Systems and Other Relevant Systems and Processes Used by Parties <i>(optional by originator)</i> To be confirmed during assessment of proposal.	
Impact on other Configurable Items <i>(optional by originator)</i> BSCP504 NHH Data Collection for SVA Metering Systems in SMRS.	
Justification for Proposed Modification with Reference to Applicable BSC Objectives <i>(mandatory by originator)</i> The modification would remove the practice of compensatory adjustments for data that has already been finalised in Settlement. This would address the issues set out above in relation to new entrants, Suppliers and LDSOs. The proposed modification therefore better facilitates Applicable BSC Objective (c) (the promotion of 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).	
Is there a likely material environmental impact? <i>(mandatory by originator)</i> No.	
Urgency Recommended: Yes / No <i>(delete as appropriate) (optional by originator)</i> No.	
Justification for Urgency Recommendation <i>(mandatory by originator if recommending progression as an Urgent Modification Proposal)</i>	
Self-Governance Recommended: Yes / No <i>(delete as appropriate) (mandatory by originator)</i> No.	
Justification for Self-Governance Recommendation <i>(mandatory by originator if recommending progression as Self-Governance Modification Proposal)</i>	
Should this Modification Proposal be considered exempt from any ongoing Significant Code Reviews? <i>(mandatory by originator in order to assist the Panel decide whether a Modification Proposal should undergo a SCR Suitability Assessment)</i> Yes; there is no ongoing SCR relevant to this Modification Proposal.	

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<p>Attachments: Yes / No <i>(delete as appropriate) (mandatory by originator)</i></p> <p>No.</p> <p>If Yes, Title and No. of Pages of Each Attachment:</p>	