

**Responses from P188 Assessment**

**Consultation Issued 08 June 2005**

**Representations were received from the following parties**

<b>No</b>	<b>Company</b>	<b>File number</b>	<b>No BSC Parties Represented</b>	<b>No Non-Parties Represented</b>
1.	EDF Energy	P188_AR_001	9	0
2.	EDF Trading Ltd	P188_AR_002	2	0
3.	Scottish and Southern Energy plc	P188_AR_003	6	0
4.	BizzEnergy Ltd	P188_AR_004	1	0
5.	Scottish Power	P188_AR_005	6	0
6.	Opus Energy Ltd	P188_AR_006	1	0
7.	Utility Link	P188_AR_007	1	0
8.	E.ON UK plc	P188_AR_008	15	0
9.	RWE Npower	P188_AR_009	10	0
10.	British Gas Trading	P188_AR_010	1	0
11.	Zest4	P188_AR_011	1	0

## P188 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties (“Parties”) and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

<b>Respondent:</b>	Stephen Moore (EDF Energy)
<b>No. of Parties Represented</b>	9
<b>Parties Represented</b>	EDF Energy Networks (EPN) plc; EDF Energy Networks (LPN) plc EDF Energy Networks (SPN) plc; EDF Energy (Sutton Bridge Power) EDF Energy (Cottam Power) Ltd; EDF Energy (West Burton Power) Ltd; EDF Energy plc; London Energy plc; Seeboard Energy Limited
<b>No. of Non Parties Represented</b>	0
<b>Non Parties represented</b>	N/A
<b>Role of Respondent</b>	Supplier/Generator/Trader

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	Yes	P188 should increase competition and efficiency by moderating the risk to the rest of the industry of a rogue party continuing to trade whilst in credit default.
2.	Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale	No	
3.	Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale	Yes	Although most breaches of 100% CCP have resulted in relatively low levels of exposure, Elexon have highlighted one case where the potential exposure was more than £500k.

Q	Question	Response	Rationale
4.	Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below: <ul style="list-style-type: none"> <li>- 75%;</li> <li>- 90%; or</li> <li>- Another level (please state)?</li> </ul> Please give rationale	75%	The rationale behind P188 is to incentivise parties not to be in credit cover default, thus it is desirable that parties who breach 100% CCP have to reduce their exposure significantly which reducing to 90% does not always achieve.
5.	Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover? Please give rationale	Yes	Apart from the lack of a two-hour cure period this is no stricter than the existing Level 2 provisions A party entering Level 1 default has a 24 hour query period which still applies under L2 and the proposes L3. The incentive should be to avoid default completely, not to move between different levels.
6.	Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)? Please give rationale	Yes	Frequent breaches of 100% CCP could be indicative of a trading strategy that is flawed or of dubious intent. It is imperative that any such party is placed in Section H and called before the BSC panel to account for this; this does give the party a chance to set out genuine reasons for such frequent breaches.
7.	Does P188 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **12:00 on Thursday 16 June 2005** to [modification.consultations@elexon.co.uk](mailto:modification.consultations@elexon.co.uk) and please entitle your email 'P188 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to David White on 020 7380 4374, email address [david.white@elexon.co.uk](mailto:david.white@elexon.co.uk).

## P188 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

<b>Respondent:</b>	<i>Steve Drummond</i>
<b>No. of Parties Represented</b>	<i>2</i>
<b>Parties Represented</b>	<i>EDF Trading Ltd and EDF (Generation)</i>
<b>No. of Non Parties Represented</b>	<i>None</i>
<b>Non Parties represented</b>	<i>N/A</i>
<b>Role of Respondent</b>	<i>Trader/Generator</i>

<b>Q</b>	<b>Question</b>	<b>Response</b>	<b>Rationale</b>
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	Yes	The current baseline fails to give a supplier the correct incentives to avoid breaching its 100% credit cover provision. This places other market participants at an unnecessary and unjustifiable risk in the event of default. P188 provides an incentive to lodge an appropriate amount of credit cover and therefore reduces the risk to other parties and is therefore conducive to promoting more effective and efficient competition.
2.	Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale	No	
3.	Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale	Yes	Potentially it could be, depending on the size of the defaulting party and whether they subsequently withdrew from the market. However, it is an unfair and unnecessary risk for other parties to bear, especially if those parties are deliberately breaching the 100% for commercial reasons.

Q	Question	Response	Rationale
4.	<p>Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below:</p> <ul style="list-style-type: none"> <li>- 75%;</li> <li>- 90%; or</li> <li>- Another level (please state)?</li> </ul> <p>Please give rationale</p>	75%	<p>If anyone is in credit default then they should get out of that position asap. Provisions are currently made for parties who stray into Level 1 or Level 2 credit default and to be out of the default zone completely a party must reduce the CCP to below 75%. It is therefore not unreasonable for parties who do more than stray into the default zone and actually breach the 100% level, thereby placing undue risks on other parties, to have to come completely out of the default area by reducing to below 75% directly. To allow them to only reduce to 90% would allow them to remain in Level 1 default, which if they are 'gaming' the system is where they would probably stay until the next breach. These parties should be encouraged to have credit cover that keeps them out of the default zones.</p>
5.	<p>Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover?</p> <p>Please give rationale</p>	Yes	
6.	<p>Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)?</p> <p>Please give rationale</p>	Yes	<p>Persistent breaches need closer investigation, especially if 'gaming' is suspected and placing them in Section H Default will achieve that end. The current proposal to define 'persistent' in this instance as 6 times in 6 months does however seem very lenient and may not be a sufficient enough deterrent. The original proposal was for 2 breaches with CCP restored to a sensible level straight away, however this apparently was felt to be too heavy handed by the modification group, so maybe something in between would be more acceptable.</p>
7.	<p>Does P188 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure?</p> <p>Please give rationale</p>	No	

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<b>Respondent:</b>	<i>Andrew Colley, Scottish and Southern Energy plc.</i>
<b>No. of Parties Represented</b>	<i>6</i>
<b>Parties Represented</b>	<i>SSE Energy Supply Ltd, SSE Generation Ltd, Keadby Power Generation Ltd, Medway Power Ltd, Southern Electric Power Distribution plc, Scottish Hydro-Electric Power Distribution Ltd</i>
<b>No. of Non Parties Represented</b>	
<b>Non Parties represented</b>	
<b>Role of Respondent</b>	<i>Supplier/Generator/ Trader/ Party Agent /LDSO</i>

<b>Q</b>	<b>Question</b>	<b>Response</b>	<b>Rationale</b>
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	Yes	SSE believe that the proposed modification seeks to mitigate risks within the current BSC baseline that could result in significant liabilities accruing to all parties were the risk scenarios described to be realised. On this basis we believe that this modification better facilitates applicable objective (c), by minimising Parties’ exposure to bad debt liabilities.  Additionally, SSE believe that the proposed modification would increase the incentive upon Parties to actively manage their credit cover position in order to avoid Section H default and the remedies that could be directed by the BSC Panel. This incentive should reduce the numbr of instances of credit default that are occurring on a day to day basis, and thus we believe that the proposal better facilitates applicable objective (d), by reducing the expense and overhead required to manage the process by BSCCo.
2.	Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale	No	Alternative solution were considered by the SSMG a part of the Issue 16 discussions and discounted due to ineffectiveness, complexity or degree of reform.

Q	Question	Response	Rationale
3.	Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale	Yes	<p>Yes. Particularly in the case of large Suppliers, significant indebtedness could be accrued within the rolling credit assessment window. Parties could face significant, potentially catastrophic smearing liabilities should that Supplier subsequently default on payments.</p> <p>Whilst typically the historical analysis suggests a relatively low materiality in the context of the total market cashflow,, the potential remains nevertheless for exposures to enormous in the worst case scenario. As this proposal is principally concerned with mitigating a perceived risk, the worst case ought to be the minimum scenario addressed by the modification, and therefore weights heavily in our consideration.</p>
4.	Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below: <ul style="list-style-type: none"> <li>- 75%;</li> <li>- 90%; or</li> <li>- Another level (please state)?</li> </ul> Please give rationale	90%	We believe that asking Parties to reduce their CCP to a level beyond that requested by the Level 2 default would create an unacceptable ambiguity and inconsistency of treatment within the Code that could be challenged at a later date. Whilst SSE have sympathy with the view that any Party breaching 100% of CCP should ensure a sizeable reduction in their CCP, we do not believe that 75% is appropriate given the context of existing thresholds for Levels 1 and 2. We believe that providing for a minimum number of breaches within a given timescale as described in Q6 below, would create an incentive upon Parties to reduce well beyond 90% in order to avoid breaching the "3 strikes and out" rule that would thus exist.
5.	Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover? Please give rationale	Yes	1 working day acts as sufficient notice to arrange for immediate collateral to be provided through banks. The timescale must remain tight to provide the necessary incentive for Parties to avoid breaching the threshold.
6.	Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)? Please give rationale	Yes	Persistent mismanagement and/or gaming of the rules must be controlled. The existing provisions within the BSC are not strong enough in this respect. It is not unreasonable to ask serious questions of Parties that breach credit provisions persistently. An average on once per month over a 6 month period seems a reasonable benchmark.



Q	Question	Response	Rationale
7.	Does P188 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	

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## P188 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties (“Parties”) and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

<b>Respondent:</b>	<i>Name Keith Munday</i>
<b>No. of Parties Represented</b>	<i>1</i>
<b>Parties Represented</b>	<i>Please list all Parties responding on behalf of (including the respondent company if relevant). BizzEnergy Ltd</i>
<b>No. of Non Parties Represented</b>	<i>0</i>
<b>Non Parties represented</b>	<i>Please list all non Parties responding on behalf of (including the respondent company if relevant).</i>
<b>Role of Respondent</b>	<i>(Supplier/Generator/ Trader / Consolidator / Exemptable Generator / BSC Agent / Party Agent / other – please state <sup>1</sup>) Supplier</i>

<b>Q</b>	<b>Question</b>	<b>Response <sup>1</sup></b>	<b>Rationale</b>
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	No	Under some circumstances the outcome would be disproportionate to the risk presented. Such a complex area cannot be solved by the impost of simple rule changes of this nature. Consideration needs to be given to the reasons for the breach and the likely materiality of impact on the market.
2.	Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale	Yes / No	Yes see below
3.	Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale	Yes / No	Potentially the risk could be significant. The materiality of the risk is important and the response and the cost and administration of the response needs to be proportionate to the risk presented. The use of a percentage value is not an accurate reflection of the materiality of risk that the market may be asked to face. A set of triggers for invoking section H should be a monetary value. This should be set at a level which if a failure were to occur would not move market imbalance energy prices over a month by more than say 0.5%.

<sup>1</sup> Delete as appropriate – please do not use knockout, this is to make it easier to analyse the responses

Q	Question	Response <sup>1</sup>	Rationale
4.	<p>Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below:</p> <ul style="list-style-type: none"> <li>- 75%;</li> <li>- 90%; or</li> <li>- Another level (please state)?</li> </ul> <p>Please give rationale</p>		<p>A party who has breached 100% has probably done so due to an unforeseen event such as a period of extreme cold weather and increased demand associated with high imbalance prices. The impost of a penal reduction will only serve to increase the strain on an already stretched cashflow. The Supplier under this scenario should only be obliged to reduce credit cover to below 100%.</p> <p>The posting of additional collateral is a double whammy to a supplier as they not only must find the funds to pay the imbalance costs but also the additional amount for security. The response of making a supplier pay twice (in cashflow terms) seems a disproportionate response which may under certain circumstances precipitate early and unnecessary failures.</p>
5.	<p>Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover?</p> <p>Please give rationale</p>	/ No	<p>No. Small players have limited finance and banking facilities. It is not always possible to raise significant sums of money at short notice due to operational constraints on banking and finance facilities. Also, internal staff availability and sickness may not allow a proper time to analyse whether there is material doubt and then raise monies especially if appropriate authorised parties are not available to transfer the money.</p>
6.	<p>Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)?</p> <p>Please give rationale</p>	Yes (depends)	<p>Persistent material offenders should be placed in breach. The measure of a material breach needs to be established. A large player being in breach by 5% presents a material risk to the market and warrants attention, however a 5% breach by a small party would have to persist for some time to have the same financial impact.</p>
7.	<p>Does P188 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure?</p> <p>Please give rationale</p>	Yes	<p>The materiality of the breach on the market prices must be quantified. Faster responses and reactions should be available to the Panel when large sums of money are involved. A single large failure has the potential to do far more damage than a few minor breaches and should be the main focus of attention.</p> <p>If it is seen fit to implement the modification then it would be appropriate to consider a faster timetable for the release collateral.</p>

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Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

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<b>Respondent:</b>	Man Kwong Liu (SAIC Ltd)
<b>No. of Parties Represented</b>	6
<b>Parties Represented</b>	<i>Please list all Parties responding on behalf of (including the respondent company if relevant).</i> Scottish Power UK plc; ScottishPower Energy Management Ltd.; ScottishPower Generation Ltd; ScottishPower Energy Retail Ltd.; SP Transmission Ltd; SP Manweb plc.
<b>No. of Non Parties Represented</b>	0
<b>Non Parties represented</b>	<i>Please list all non Parties responding on behalf of (including the respondent company if relevant).</i>
<b>Role of Respondent</b>	<i>(Supplier/Generator/ Trader / Consolidator / Exemptable Generator / BSC Agent / Party Agent / other – please state<sup>1</sup>)</i> Supplier / Generator / Trader / Consolidator / Exemptable Generator

Q	Question	Response <sup>1</sup>	Rationale
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	Yes	We agree with the view that by reducing the potential exposure of BSC Parties to debts that caused by defaulting parties via the introduction of more robust credit arrangements would improve market confidence and therefore better facilitate the BSC Objective (c) – promote competition.  P188 also improve the process of actions on Parties whose CCP is greater than 100%, as well as providing incentive for parties not to enter into defaults. It therefore also better facilitate the BSC Objective (d) – improve efficiency.
2.	Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale	No	We believe the Proposed Modification is suitable and not too onerous on parties.

<sup>1</sup> Delete as appropriate – please do not use knockout, this is to make it easier to analyse the responses

Q	Question	Response <sup>1</sup>	Rationale
3.	Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale	Yes	Whilst the analysis showed that currently materiality is relatively low, the risk and potential exposure could be significant and therefore would support this change.
4.	Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below: <ul style="list-style-type: none"> <li>- 75%;</li> <li>- 90%; or</li> <li>- Another level (please state)?</li> </ul> Please give rationale		We believe that to be consistent with the current process and arrangement, it should be 90% (the level currently required to be reduced for level 2 default). However, we would also accept 75% if the industry feel this level gives a better safety margin and protection.
5.	Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover? Please give rationale	Yes	There should be enough time for actions to be taken, particularly when there would be further delay for the Panel to convene and invoke Section H default.
6.	Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)? Please give rationale	Yes	This would give the necessary incentive for parties to remain in credit.
7.	Does P188 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	

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<b>Respondent:</b>	<i>Opus Energy Limited</i>
<b>No. of Parties Represented</b>	<i>1</i>
<b>Parties Represented</b>	
<b>No. of Non Parties Represented</b>	
<b>Non Parties represented</b>	
<b>Role of Respondent</b>	<i>Supplier</i>

<b>Q</b>	<b>Question</b>	<b>Response</b>	<b>Rationale</b>
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	No	It is considered by Opus that a move to Section H Breach within 1 working day after entering Level 2 Default is overly stringent and is likely to lead to unintentional breach by parties.  This could potentially cause damage to companies operating under the BSC, and increases the risk of operating in the market. Consequently it is considered that while the proposed change will reduce exposure of the industry to party failure, on balance it does not facilitate the achievement of Applicable BSC Objective (c), ie the promotion of competition.
2.	Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale	Yes	It is the view of Opus that a move to Section H breach should occur within 3 working days after entering Level 2 Default. This would match the default timetable for non payment of charges, and also coincides with standard practice for default under GTMA terms.
3.	Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale	Yes	

Q	Question	Response	Rationale
4.	Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below: <ul style="list-style-type: none"> <li>- 75%;</li> <li>- 90%; or</li> <li>- Another level (please state)?</li> </ul> Please give rationale	90%	There has been considerable work carried out within the industry over the last 2 years, aimed at reducing over-collateralisation in the transmission and distribution of electricity. Consequently it seems at odds with current views on collateralisation to enforce a reduction to 75%
5.	Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover? Please give rationale	No	No – Please see comments in 1 and 2
6.	Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)? Please give rationale	Yes	
7.	Does P188 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes / No	

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<b>Respondent:</b>	Alan Goodbrook
<b>No. of Parties Represented</b>	One
<b>Parties Represented</b>	Utility Link Limited
<b>No. of Non Parties Represented</b>	None
<b>Non Parties represented</b>	N/A
<b>Role of Respondent</b>	Supplier/ Party Agent

<b>Q</b>	<b>Question</b>	<b>Response</b> Error! Bookmark not defined.	<b>Rationale</b>
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	No	We consider the proposals to be unduly onerous on small suppliers and hence to conflict with Applicable BSC Objective ©: Promoting effective competition in the generation and supply of electricity. The proposals are likely to result in Trading Parties being required to face the panel for potential exposures which in the majority of cases would amount to less than £10k. This would appear to be inconsistent with Applicable BSC Objective (d): Promoting efficiency in the implementation and administration of the balancing and settlement arrangements.

Q	Question	Response Error! Bookmark not defined.	Rationale
2.	Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale	Yes	As explained in the response to Q5 below a small supplier such as ourselves may have practical difficulty in lodging additional credit cover. Credit cover is also more costly for most small suppliers to provide because they invariably have a higher cost of capital. Rather than lodging additional credit cover we would prefer to trade out of a credit default position by contracting for additional power. This is not viable under any of the options being put forward by the Modification Group.
3.	Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale	No	The materiality/risk assessment acknowledges that there were only 17 instances of a Trading Party having exceeded 100% CCP and in the majority of cases exposure is estimated at less than £10k. In no cases had a party defaulted when actual trading liabilities became due for payment.
4.	Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below: – 75%; – 90%; or – Another level (please state)? Please give rationale	90%	The proposed provisions are essentially an extension to the existing Level 2 Credit Default and hence if the modification is to be implemented it should have the same reduction threshold. Moreover, Trading Parties are already publicised for being over 100% and this – especially when combined with a potential appearance in front of the Panel – is damaging enough to their reputation without imposing more severe provisions.
5.	Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover? Please give rationale	No	Invariably the timescale for providing additional credit cover for smaller suppliers can extend to several weeks. Because of this potential difficulty in lodging additional credit cover and its associated high cost we would prefer to be able to trade out of a credit default position by contracting for additional power. For this to be a practicable solution we consider that Trading Parties should be allowed at least 10 working days to reduce their CCP from 100% to 90% because of the 29 day averaging in calculating indebtedness.

Q	Question	Response Error! Bookmark not defined.	Rationale
6.	Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)? Please give rationale	No	The materiality/risk assessment carried out shows that in the majority of cases of a Trading Party having exceeded 100% CCP over a year, exposure is estimated at less than £10k. For Trading Parties to be required to face the panel for potential exposures of this magnitude would appear to be inconsistent with Applicable BSC Objective (d): Promoting efficiency in the implementation and administration of the balancing and settlement arrangements.
7.	Does P188 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	The materiality/risk assessment undertaken shows there to have been 17 instances of a Trading Party having exceeded 100% CCP over a year. We consider the analysis of these instances should be shown categorized according to whether the party was a generator, large supplier or small supplier with a view to the Assessment Procedure identifying adverse competition issues associated with the proposals.

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Please send your responses by **12:00 on Thursday 16 June 2005** to [modification.consultations@elexon.co.uk](mailto:modification.consultations@elexon.co.uk) and please entitle your email 'P188 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

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## P188 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties (“Parties”) and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

<b>Respondent:</b>	<i>E.ON UK plc</i>
<b>No. of Parties Represented</b>	15
<b>Parties Represented</b>	E.ON UK plc, Powergen Retail Limited, Cottam Development Centre Limited, Enizade Ltd, E.ON UK Drakelow Limited, E.ON UK Ironbridge Limited, E.ON UK 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.
<b>No. of Non Parties Represented</b>	N/A
<b>Non Parties represented</b>	N/A
<b>Role of Respondent</b>	Supplier, Generator, Trader, Consolidator & Exemptable Generator

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	Yes	<p>We concur with the working group that the current credit cover provisions do not provide satisfactory incentive to ensure that Trading Parties post a sufficient level of Credit Cover in all instances. We therefore agree that enhanced provisions should be introduced to make sure that <u>all</u> Parties maintain a Credit Cover Percentage (CCP) of less than 100%.</p> <p>The proposed modification would better facilitate the achievement of Applicable BSC Objective (c) in that it would reduce the potential exposure faced by market participants as a result of the unpaid liabilities of a third party. P188 also provides a consistent and equitable approach to the credit cover arrangements.</p> <p>P188 would improve the efficiency of the credit cover provisions by reducing the number of parties who exceed 100% CCP and as such, would better facilitate the achievement of Applicable BSC Objective (d).</p>

Q	Question	Response	Rationale
2.	Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale	No	
3.	Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale	Yes	Whilst recognising that the worst case scenario considered within the assessment consultation represents a very low probability/high materiality event, the information provided by ELEXON reveals that there has been a significant breach of 100% CCP creating an estimated exposure of more than £500k. We therefore agree with the Group that there is a significant level of risk and materiality associated with the defect.
4.	Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below: – 75%; – 90%; or – Another level (please state)? Please give rationale		We believe that the suggested requirement to return below 75% CCP would in itself act as an additional incentive not to breach 100% CCP. We also agree with a number of the modification group who have suggested that parties should be dissuaded from remaining within Level 1 Default for a sustained period of time. However, we note the counter arguments and in particular agree that as this modification is seen as an extension to Level 2 Default, the reduction threshold should remain the same (e.g. 90%).  On balance we believe that the 75% threshold better facilitates the aims of this proposal.
5.	Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover? Please give rationale	Yes	
6.	Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)? Please give rationale	Yes	Provided that the six breaches are on separate Settlement days and not part of the same instance this aspect of the proposal appears reasonable.

Q	Question	Response	Rationale
7.	Does P188 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	

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<b>Respondent:</b>	<i>Carl Wilkes</i>
<b>No. of Parties Represented</b>	<i>10</i>
<b>Parties Represented</b>	RWE Trading GmbH, RWE Npower plc, Npower Co-gen Ltd, Npower Co-gen Trading Ltd, Npower Direct Ltd, Npower Ltd, Npower Northern Ltd, Npower Northern Supply Ltd, Npower Yorkshire Ltd, Npower Yorkshire Supply
<b>No. of Non Parties Represented</b>	
<b>Non Parties represented</b>	<i>Please list all non Parties responding on behalf of (including the respondent company if relevant).</i>
<b>Role of Respondent</b>	<i>Supplier/Generator/ Trader / Consolidator / Exemptable Generator / <del>BSC Agent</del> / Party Agent / other</i>

<b>Q</b>	<b>Question</b>	<b>Response</b>	<b>Rationale</b>
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	Yes	The present arrangements for credit cover are insufficient, in particular where parties consistently breach 100% CCP.
2.	Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale	No	
3.	Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale	Yes	The deficiencies in the present arrangements pose a significant risk to the market in certain circumstances.
4.	Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below: <ul style="list-style-type: none"> <li>– 75%;</li> <li>– 90%; or</li> <li>– Another level (please state)?</li> </ul> Please give rationale		In the first instance of a 100% breach Trading Parties should have to reduce their indebtedness below 90%. From the second incidence of a 100% breach onwards, they should be required to reduce it below 75%. This would give the market the re-assurance that the party concerned is able to manage its credit cover risk.

Q	Question	Response	Rationale
5.	Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover? Please give rationale	No	In our practical experience two working days is a more realistic time period for this type of activity.
6.	Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)? Please give rationale		This would depend on the circumstances. Every potential situation for Section H default should be considered on a case by case basis.
7.	Does P188 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	

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<b>Respondent:</b>	Mark Manley
<b>No. of Parties Represented</b>	
<b>Parties Represented</b>	British Gas Trading (BGT)
<b>No. of Non Parties Represented</b>	
<b>Non Parties represented</b>	
<b>Role of Respondent</b>	

<b>Q</b>	<b>Question</b>	<b>Response</b> Error! Bookmark not defined.	<b>Rationale</b>
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	Yes	<p>BGT believes this modification better facilitates competition in the generation and sale of electricity, Applicable BSC Objective (c). The current rules contain a defect, as the baseline does not provide sufficient protection to industry parties to prevent against exposure to a bad debt. BGT believe the credit cover arrangements need to strike a balance between providing a level of protection whilst ensuring parties lodge credit commensurate with their level of activity. BGT believes this balance is not being met by the current baseline as it favours individual parties at the expense of the market.</p> <p>BGT note the analysis contained within the assessment consultation, which illustrates the number of incidents when the 100% threshold has been breached. BGT acknowledge that two thirds of the breaches may relate to relatively minor amounts, however BGT is concerned by the number of breaches and the scale of the most significant incident, over £500k.</p>

Q	Question	Response Error! Bookmark not defined.	Rationale
			<p>BGT believe the materiality of the issue is important but BGT believe the principle and the potential materiality is of equal importance. The arrangements need to be robust and provide an appropriate level of protection against all instances of credit default. This is why it is essential that this issue be addressed.</p> <p>The current baseline allows parties Credit Cover Percentage (CCP) to exceed 100% and at this point there is insufficient credit cover lodged to cover any outstanding debts. BGT acknowledge that it is not possible to prevent a party's indebtedness exceeding 100%. However, this modification proposal provides an appropriate incentive for parties to ensure their CCP does not breach 100% and enables any bad debt to be crystallised much sooner. This modification helps to ensure that the credit arrangements in the BSC provide as secure and stable business environments as is reasonable. This is a desired objective stated by Ofgem in the recently published best practice guidelines for the 'Arrangements for gas and electricity network operator credit cover'.</p>
2.	<p>Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale</p>	No	
3.	<p>Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale</p>	Yes	<p>The materiality quoted in the consultation illustrates the significance of the risk. Within the sample year the materiality of the most significant issue was more than £500,000. If this incident had resulted in a bad debt individual BSC Parties would have been liable for substantial sums of money to cover the debt.</p> <p>The defect could also result in significantly larger debts being 'run-up' if a large supply business was to get into financial difficulty. BGT believe on the basis of actual materiality as presented in the consultation and the potential</p>

Q	Question	Response Error! Bookmark not defined.	Rationale
			for the defect to be exposed poses a significant risk to all BSC Parties with a physical position.
4.	<p>Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below:</p> <ul style="list-style-type: none"> <li>- 75%;</li> <li>- 90%; or</li> <li>- Another level (please state)?</li> </ul> <p>Please give rationale</p>	75%	<p>BGT believe that Trading Parties should reduce their CCP below 75%. BGT believes setting the threshold at 90% sends the wrong signal. It sends the message that being in credit default is acceptable, BGT do not believe it is acceptable to be in either of the levels of credit default. Therefore BGT believe that 75% is the appropriate threshold.</p> <p>BGT also believe that obligating Parties to lodge sufficient credit cover to reduce their CCP below 75% will active as an incentive for Parties to maintain head room and not allow their indebtedness to exceed 100%. This should also help to ensure that Parties post a level of credit cover that is commensurate with the level of activity the Party is undertaking.</p> <p>BGT acknowledge that this is essentially an extension to the level 2 provisions and understands the rationale for wanting to maintain the 90% threshold. However BGT continue to believe that 75% is the right level and do not believe the group should be tied to 90%.</p>
5.	<p>Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover?</p> <p>Please give rationale</p>	Yes	<p>BGT drafted the modification proposal with 1 working day in square brackets for the modification group to discuss the parameter. One of the aims of the modification is to crystallise any bad debt as quickly as possible and therefore limit the potential liability that parties could face. However, BGT understands that Ofgem have stated in its best practice guidelines for network operators that 2 working days is an appropriate time frame. Whilst BGT's preference is for 1 working day it would appear that there is a strong steer from Ofgem in respect of an appropriate window for lodging credit cover.</p>
6.	<p>Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)?</p>	Yes	<p>BGT support the implementation of a process to capture persistent breaches of the 100% threshold. BGT believe irrespective of whether additional credit is lodged within 1 working day that should be counted</p>

Q	Question	Response Error! Bookmark not defined.	Rationale
	Please give rationale		towards the target. If a party makes a mistake with the calculation on an occasion then that wouldn't necessarily result in the Party being placed in default. However 6 occurrences within a 6 month period is a result of mismanagement and having insufficient credit cover lodged. Therefore it would be appropriate to place the Party in default. Introducing a time band will also act as a disincentive for Parties continuously breaching the 100% threshold.

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<b>Respondent:</b>	<i>ZEST4</i>
<b>No. of Parties Represented</b>	
<b>Parties Represented</b>	<i>Please list all Parties responding on behalf of (including the respondent company if relevant).</i>
<b>No. of Non Parties Represented</b>	
<b>Non Parties represented</b>	<i>Please list all non Parties responding on behalf of (including the respondent company if relevant).</i>
<b>Role of Respondent</b>	<i>(Supplier/Generator/ Trader / Consolidator / Exemptable Generator / BSC Agent / Party Agent / other – please state<sup>1</sup>)</i>

<b>Q</b>	<b>Question</b>	<b>Response<sup>1</sup></b>	<b>Rationale</b>
1.	Do you believe Proposed Modification <b>P188</b> better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	No	Materiality is key. From the data provided it seems that there are very few incidences when the amount in excess of 100% has exceeded £10,000. There does not seem to be any point in having a solution that will cost many hundreds of thousands of pounds when the risk in the vast majority of cases is insignificant.
2.	Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered? Please give rationale	Yes	Am solution which measures the materiality of the risk to the market as a whole.
3.	Do you believe that the risk and materiality associated with the perceived defect is significant? Please give rationale	Yes	In some cases yes i.e. where the exposure is greater than (say) £100,000.

<sup>1</sup> Delete as appropriate – please do not use knockout, this is to make it easier to analyse the responses

Q	Question	Response <sup>1</sup>	Rationale
4.	Do you believe that after breaching 100% CCP, Trading Parties should reduce their CCP to below: <ul style="list-style-type: none"> <li>- 75%;</li> <li>- 90%; or</li> <li>- Another level (please state)?</li> </ul> Please give rationale		It seems logical that they should reduce to 90% i.e. the next level down.
5.	Do you believe that 1 Working Day (plus any Query Period from breaching 80%) is sufficient to lodge additional Credit Cover? Please give rationale	No	1 working will not allow small players to cover the risk i.e. to put new arrangements into place. There should be at least 3 working days.
6.	Do you agree that Trading Parties which persistently breach 100% CCP should be placed in Section H Default (even if additional Credit Cover is placed within 1 WD)? Please give rationale	No	Again it depends on materiality. Those breaching significantly (i.e. greater than £100k) should be placed in Section H. Otherwise no.
7.	Does P188 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	Again materiality needs to be assessed.

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