

**ASSESSMENT REPORT for Modification Proposal P178  
'Reduction in the BSC withdrawal timescale for Parties who have  
settled the vast majority of their trading debts'**

**Prepared by: Settlement Standing Modification Group (SSMG)**

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This document has been distributed in accordance with Section F2.1.10<sup>1</sup> of the Balancing and Settlement Code.

## **RECOMMENDATIONS**

The SSMG invites the Panel to;

- **AGREE that the Proposed Modification P178 should not be made;**
- **AGREE that the Alternative Modification P178 should not be made;**
- **AGREE a provisional Implementation Date for the Proposed Modification P178 of 29 June 2005 if an Authority decision is received on or before 9 March 2005, or 2 November 2005 if the Authority decision is received after 9 March 2005 but on or before 6 July 2005;**
- **AGREE a provisional Implementation Date for the Alternative Modification P178 of 29 June 2005 if an Authority decision is received on or before 9 March 2005, or 2 November 2005 if the Authority decision is received after 9 March 2005 but on or before 6 July 2005;**
- **AGREE that Modification Proposal P178 be submitted to the Report Phase; and**
- **AGREE that the draft Modification Report be issued for consultation and submitted to the Panel Meeting of 13 January 2005.**

<sup>1</sup> The current version of the Balancing and Settlement Code (the 'Code') can be found at <http://www.elexon.co.uk/bscrelateddocs/BSC/default.aspx>

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## SUMMARY OF IMPACTED PARTIES AND DOCUMENTS

As far as the SSMG has been able to assess, the following parties/documents would be impacted by the implementation of Modification Proposal P178.

Parties	Sections of the BSC	Code Subsidiary Documents
Suppliers <input type="checkbox"/>	A <input checked="" type="checkbox"/>	BSC Procedures <input checked="" type="checkbox"/>
Generators <input checked="" type="checkbox"/>	B <input type="checkbox"/>	Codes of Practice <input type="checkbox"/>
Licence Exemptable Generators <input checked="" type="checkbox"/>	C <input type="checkbox"/>	BSC Service Descriptions <input checked="" type="checkbox"/>
Transmission Company <input type="checkbox"/>	D <input checked="" type="checkbox"/>	Service Lines <input type="checkbox"/>
Interconnector <input checked="" type="checkbox"/>	E <input type="checkbox"/>	Data Catalogues <input type="checkbox"/>
Distribution System Operators <input type="checkbox"/>	F <input type="checkbox"/>	Communication Requirements Documents <input type="checkbox"/>
Non-Physical Traders <input checked="" type="checkbox"/>	G <input type="checkbox"/>	Reporting Catalogue <input type="checkbox"/>
<b>Party Agents</b>		
	H <input type="checkbox"/>	MIDS <input type="checkbox"/>
Data Aggregators <input type="checkbox"/>	I <input type="checkbox"/>	<b>Core Industry Documents</b>
Data Collectors <input type="checkbox"/>	J <input type="checkbox"/>	Grid Code <input type="checkbox"/>
Meter Operator Agents <input type="checkbox"/>	K <input type="checkbox"/>	Supplemental Agreements <input type="checkbox"/>
ECVNA <input type="checkbox"/>	L <input type="checkbox"/>	Ancillary Services Agreements <input type="checkbox"/>
MVRNA <input type="checkbox"/>	M <input type="checkbox"/>	Master Registration Agreement <input type="checkbox"/>
<b>BSC Agents</b>		
SAA <input type="checkbox"/>	N <input checked="" type="checkbox"/>	Data Transfer Services Agreement <input type="checkbox"/>
FAA <input checked="" type="checkbox"/>	O <input type="checkbox"/>	British Grid Systems Agreement <input type="checkbox"/>
BMRA <input type="checkbox"/>	P <input type="checkbox"/>	Use of Interconnector Agreement <input type="checkbox"/>
ECVAA <input type="checkbox"/>	Q <input type="checkbox"/>	Settlement Agreement for Scotland <input type="checkbox"/>
CDCA <input type="checkbox"/>	R <input type="checkbox"/>	Distribution Codes <input type="checkbox"/>
TAA <input type="checkbox"/>	S <input type="checkbox"/>	Distribution Use of System Agreements <input type="checkbox"/>
CRA <input checked="" type="checkbox"/>	T <input type="checkbox"/>	Distribution Connection Agreements <input type="checkbox"/>
Teleswitch Agent <input type="checkbox"/>	U <input type="checkbox"/>	<b>BSCCo</b>
SVAA <input type="checkbox"/>	V <input type="checkbox"/>	Internal Working Procedures <input checked="" type="checkbox"/>
BSC Auditor <input type="checkbox"/>	W <input type="checkbox"/>	<b>Other Documents</b>
Profile Administrator <input type="checkbox"/>	X <input checked="" type="checkbox"/>	Transmission Licence <input type="checkbox"/>
Certification Agent <input type="checkbox"/>		System Operator-Transmission Owner Code <input type="checkbox"/>
MIDP <input type="checkbox"/>		
<b>Other Agents</b>		
SMRA <input type="checkbox"/>		
Data Transmission Provider <input type="checkbox"/>		

\*P178 has no direct impact upon Parties' systems, processes or documentation. However, under P178 a Non-Supplier Trading Party would be able to achieve an earlier withdrawal from the Code following the 2nd Reconciliation Settlement Run – providing that the Party left a cash deposit to cover its estimated future liabilities up to the Final Reconciliation Settlement Run. Where this deposit was not sufficient, this could result in the shortfall amount being recovered from all remaining Parties.

# **1 DESCRIPTION OF MODIFICATION PROPOSAL AND ASSESSMENT AGAINST THE APPLICABLE BSC OBJECTIVES**

## **1.1 Modification Proposal**

Modification Proposal P178 'Reduction in the BSC withdrawal timescales for Parties who have settled the vast majority of their trading debts' ('P178') was raised by Uskmouth Power Company Limited ('the Proposer') on 4 October 2004. The defect identified by, and the solution proposed within, the Modification Proposal were previously considered by the Settlement Standing Modification Group ('SSMG') as Issue 12 at a meeting held on 27 September 2004 (Reference 1).

### **1.1.1 Background: current withdrawal criteria**

The current criteria for withdrawal from the Balancing and Settlement Code ('the Code') are contained in paragraph A5.1.3. One of these criteria is that a BSC Party ('Party') may not withdraw if (as at 1700 hours on the day which is 2 Business Days prior to the Withdrawal Date) the Final Reconciliation Settlement Run ('RF') has not been carried out in relation to the Party's last Settlement Day, or if the corresponding Payment Date has not yet passed.

Since Parties may not withdraw before the RF Payment Date, they must therefore wait approximately 14 months<sup>2</sup> to withdraw, even if all the other criteria in A5.1.3 have been met at an earlier date (e.g. the Party has no outstanding sums payable, no Default capable of remedy and no registered Meters or BM Units).

### **1.1.2 Defect identified by Modification Proposal**

The Modification Proposal identifies three perceived defects in the current requirement to remain a Party to the Code until RF:

#### **a) Inappropriate requirement for Non-Supplier Trading Parties**

The Proposer suggests that the current 14-month timescale seems to have been designed around the Supplier Volume Allocation (SVA) reconciliation process. The Proposer argues that there appears to be no compelling reason to treat Non-Supplier Trading Parties<sup>3</sup> in the same way as Suppliers, since such Parties will have settled the vast majority of their Reconciliation Charges by the 2nd Reconciliation Settlement Run ('R2') and their remaining future charges will therefore be small.

#### **b) Legal risk of ongoing Code obligations**

Parties to the Code who are seeking to withdraw and are no longer operational in the market (e.g. have ceased trading, terminated other contracts and transferred all assets), continue to be bound by any new obligations introduced via a Code modification prior to RF. The Proposer argues that this creates unwarranted ongoing legal liabilities for Non-Supplier Trading Parties. In addition, the Proposer argues that Parties who are no longer trading or are in administration will not necessarily have the staff or expertise to manage such liabilities.

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<sup>2</sup> 291 Business Days after the Party's last trades.

<sup>3</sup> Defined in Section M2.3A.7 of the Code as a Trading Party which (at the time of its last Settlement Day) is not a Supplier, or a Subsidiary Party in a Metered Volume Reallocation Notification where the Lead Party is a Supplier. Annex X-1 defines a Supplier as a Trading Party which has one or more SVA Metering Systems.

### c) **Administrative inefficiencies for Parties, FAA and BSCCo**

The Proposer argues that the current withdrawal timescale results in administrative inefficiencies for the following market participants:

- **Withdrawing Non-Supplier Trading Parties**, through the need to manage invoices for small amounts of Reconciliation Charges between R2 and RF. The Proposer argues that the current timescale prevents a non-operational Party from paying its bills and exiting the market in a timely manner. The Proposer also suggests that the current arrangements may result in unintentional payment Defaults by non-operational Parties due to a lack of resources to monitor invoices (for example, where the Party is in administration) rather than an actual lack of capital.
- **Other Parties**, where any Reconciliation Charges which are not recovered from Parties in Default are recouped from all other Parties.
- **Funds Administration Agent (FAA)**, through the need to invoice a Non-Supplier Trading Party for small amounts of Reconciliation Charges between R2 and RF.
- **BSCCo**, through time spent in pursuing the unpaid amounts of Parties in Default and in providing advice to non-operational Parties regarding their obligations between R2 and RF.

#### 1.1.3 **Solution proposed by Modification Proposal**

To address these perceived defects, P178 proposes to allow Non-Supplier Trading Parties to withdraw from the Code following R2 on a voluntary basis, providing that:

- The Withdrawing Party meets all other withdrawal criteria (however, see SSMG's agreed solution outlined in Section 1.2); and
- The Withdrawing Party lodges a refundable cash 'withdrawal deposit' with the FAA as security against its estimated Reconciliation Charges between R2 and RF.

P178 proposes that the cash 'withdrawal deposit' be debited and credited by the FAA as required for each subsequent 3rd Reconciliation ('R3') and/or RF Settlement Run for each of the Party's remaining Settlement Days. The Modification Proposal suggests that no further invoices would be issued to the Party following its withdrawal and that, instead, a final statement and any remaining money would be returned to the Party after RF (however, see SSMG's agreed solution outlined in Section 1.2).

#### 1.1.4 **Proposer's view of Modification Proposal against Applicable BSC Objectives**

The Proposer believes that P178 would better facilitate the achievement of Applicable BSC Objectives (c) and (d).<sup>4</sup>

The Proposer argues that ease of exit is as important as ease of entry if the market is to encourage competition and keep the Code as a contract between Parties who are actually operational. The Proposer believes that P178 would:

- Provide a simpler and more timely withdrawal route for those Parties who have paid the vast majority of their bills by R2;
- Reduce administrative costs to Withdrawing Parties, other Parties, the FAA and BSCCo – allowing resources to be more appropriately targeted on those Parties who are active in the market.

<sup>4</sup> Applicable BSC Objectives (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' and (d) 'Promoting efficiency in the implementation and administration of the balancing and settlement arrangements'.

### **1.1.5 Process followed to date**

The P178 Initial Written Assessment (IWA, Reference 2) was presented to the BSC Panel ('the Panel') Meeting held on 14 October 2004, where the Panel determined that P178 should be submitted to a two-month Assessment Procedure by the SSMG. The issues raised by BSCCo and the Panel during the IWA formed the basis of the SSMG's Terms of Reference for P178, and can be found in Annex 2 along with details of the Group's membership.

During the two-month Assessment timetable the SSMG held two meetings (on 26 October and 24 November 2004), issued an industry consultation (on 15 November 2004, Reference 2) and commissioned impact assessments from BSC Agents (Reference 3), BSCCo and the Transmission Company. Summaries of the responses received can be found in Sections 4, 5 and 6, whilst full copies of the responses are included as Annexes 3, 4 and 5.

Draft legal text for the Proposed and Alternative Modifications has been issued to the SSMG for review, and will be provided to the Panel prior to its meeting on 9 December 2004.

## **1.2 Proposed Modification**

This section outlines the solution developed by the SSMG to support the Proposed Modification. More detail regarding the Group's rationale in developing these requirements can be found in Section 1.3.

### **1.2.1 Solution overview – the 'Reconciliation Charges deposit'**

The solution developed by the SSMG for the Proposed Modification is to amend the Code's current requirement to remain a Party until RF, in order to allow any Non-Supplier Trading Party (including those in insolvency or administration) to withdraw from the Code at any time following the Payment Date for the R2 run relating to the Party's last Settlement Day. The Party would be entitled to exercise this right to early withdrawal providing it met all other withdrawal criteria (see below) and left a refundable cash 'withdrawal deposit' with the FAA to cover its estimated Reconciliation Charges up to RF (hereafter referred to as the 'Reconciliation Charges deposit').

The Proposed Modification would also amend the current Code requirement for a Withdrawing Party to remain a Party until the final determination of BSCCo Charges for the BSC Year in which its last Settlement Day fell, such that a Non-Supplier Trading Party could withdraw after R2 having paid only those BSCCo Charges accrued by its Withdrawal Date. BSCCo would invoice the withdrawn Party for its remaining share of Annual Net Main Costs and Annual Default Costs following the final determination of BSCCo Charges at the end of the BSC Year.

### **1.2.2 Detailed solution**

#### **a) Withdrawal criteria**

The shortened withdrawal process would be available to any Party, on a voluntary basis, where (at 1700 hours on the day which is 2 Business Days prior to its Withdrawal Date) it met the following withdrawal criteria:

- The Party was a Non-Supplier Trading Party as defined in paragraph M2.3A.7 of the Code (new P178 requirement);
- The Payment Date for the R2 Reconciliation Settlement Run relating to the Party's last Settlement Day had passed (P178 amendment of existing requirement in A5.1.3 to wait until the RF Payment Date);
- The Party had lodged a refundable cash deposit with the FAA to cover its estimated future payable Reconciliation Charges up to RF (new P178 requirement);

- The Party had paid all BSCCo Charges accrued by its Withdrawal Date (P178 amendment of existing requirement in A5.1.3 to wait until the end of the BSC Year);
- The Party had paid all other outstanding sums accrued and payable by that Party, whether or not due for payment or the subject of a dispute, but which may exclude the Base Monthly Charge if so determined by the Panel (existing A5.1.3 requirement);
- The Party had no registered Metering Systems or BM Units, except for Base BM Units (existing A5.1.3 requirement);
- The Party had no outstanding Default capable of remedy, excluding where the Party was in Default solely by virtue of its insolvency or being in administration (existing A5.1.3 requirement);
- The Party was not subject to any Licence condition and/or Exemption condition requiring it to remain a Party (existing A5.1.3 requirement); and
- If the Party was an Interconnector Administrator or Interconnector Error Administrator, a replacement Interconnector Administrator or Interconnector Error Administrator had been appointed (existing A5.1.3 requirement).

No further Code criteria would be applied, although the Withdrawing Party would also be required to comply with the existing withdrawal steps set out in BSCP65 'Registration of Parties and Exit Procedures' – such as ensuring that it has no Energy Contract Volume Notifications or Metered Volume Reallocation Notifications in place beyond its point of deregistration, and cancelling any Settlement Reports via BSCP41 'Report Requests and Authorisation'.

Please note that the Reconciliation Charges deposit would be entirely separate to any Credit Cover which the Non-Supplier Trading Party might have lodged prior to its withdrawal. Under the Proposed Modification, a withdrawing Non-Supplier Trading Party would therefore be able to reclaim all of its previous Credit Cover as under the current process for withdrawal at RF – but would be required separately to lodge the Reconciliation Charges deposit.

#### **b) Timing of withdrawal**

The earliest eligible Withdrawal Date of a Non-Supplier Trading Party under the Proposed Modification would therefore be 3 Business Days after the R2 Payment Date for its last Settlement Day.<sup>5</sup> Such Parties could choose to use the P178 process to withdraw at this point or on any other subsequent calendar day prior to the RF Payment Date. Alternatively, a Non-Supplier Trading Party could choose to remain a Party until RF, and then withdraw using the Code's existing withdrawal process without the requirement to lodge a cash deposit.

#### **c) Calculation of Reconciliation Charges deposit**

Following receipt of a Non-Supplier Trading Party's Withdrawal Notice, and providing that the Party met all other withdrawal criteria, BSCCo would calculate the Party's Reconciliation Charges deposit amount based on an estimate of the Party's future payable Reconciliation Charges up to RF. This would be a variation of the Code's existing P152 Credit Cover calculation in M2.3A, adapted to take into account only the R3 and/or RF Settlement runs as applicable.<sup>6</sup>

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<sup>5</sup> Approximately 3 months or 85 Working Days after the Party's last trades.

<sup>6</sup> Modification Proposal P152 'Reduction of Credit Cover for a Trading Party in Default which has ceased trading and which has paid all accrued Trading Charges'. Following implementation of P152 Alternative, a Non-Supplier Trading Party which is no longer trading and which is in Default solely under H3.1.1(g) may choose to reduce its Credit Cover to an amount estimated to cover its future payable Reconciliation Charges.



The Reconciliation Charges deposit amount left by a Withdrawing Party under P178 would be calculated by BSCCo as follows:

$$\sum_{x \in (3, F)} NR_{xSP} * \frac{\sum_{Rx(j)} \max(RxC_j, 0)}{RxSP}$$

**RxSP** is the count of all Settlement Periods falling any time up to a year before the date on which the Non-Supplier Trading Party in question ceased trading for which the Rx Reconciliation Run has been performed or if this number is less than 1440 (30 days) then 1440.

**ΣRx(j)** represents summation over all Settlement Periods falling within a year before the date on which the Non-Supplier Trading Party in question ceased trading for which the Rx Reconciliation Run has been performed or if the number of Settlement Periods in this sum is less than 1440, then the summation over the last 1440 Settlement Periods for which the Rx Reconciliation Run has been performed.

**RxCj** represents the Reconciliation Charges (as defined in N6.4.3) payable by the Non-Supplier Trading Party (summed across its accounts) due to the Rx Reconciliation Run in the relevant Settlement Period.

**NRxSP** represents the count of all Settlement Periods up to and including the date on which the Non-Supplier Trading Party ceased trading for which the Rx Reconciliation Run has not been performed.

Essentially, the purpose of the above calculation is to derive the Party's average historical positive Reconciliation Charge at R3 and/or RF, and then apply this value to all of the Party's Settlement Periods for which that run has not occurred.

#### **d) Administration of Reconciliation Charges deposit**

The FAA would hold the deposit as 'pre-payment' towards the Reconciliation Charges payable by the withdrawn Party as a result of any future R3 and RF Reconciliation Settlement Runs in respect of each of the Party's Settlement Days.

At the Payment Date for each R3 and/or RF run, in relation to each Settlement Day, the FAA would therefore debit the Party's Reconciliation Charges deposit with the following:

- Amount payable by the Party in respect of Reconciliation Charges (as calculated in accordance with existing paragraph N6.4 of the Code, including any interest relating to those charges) for the Settlement Day as a result of that R3 or RF run; and
- The Value Added Tax (VAT) applicable to the payable Reconciliation Charges amount.

Where a R3 or RF run resulted in Reconciliation Charges being payable to the Party, these would be credited to the deposit at the relevant Payment Date along with any VAT applicable to the amount.

No Advice Notes would be issued to the Party following its Withdrawal Date, although the FAA would still be required to issue Confirmation Notices (see Section 1.3.6). A final statement detailing the FAA's debits from/credits to the Reconciliation Charges deposit would be provided to the Party following the RF Payment Date for its last Settlement Day, along with any surplus deposit money and the interest accrued by the deposit during the period in which it was held by the FAA.<sup>7</sup>

If any surplus deposit money could not be returned to the Party (due to it having wound up its operations as a company), this money would be redistributed to all remaining Parties via their Default Funding Shares.

<sup>7</sup> Interest in relation to the Reconciliation Charges deposit would be calculated on a daily basis by the FAA, but would be paid to the Party following RF as a one-off sum.

### e) 'Ratchet' mechanism for Reconciliation Charges deposit

If the Reconciliation Charges deposit proved to be insufficient to cover the actual Reconciliation Charges payable by the Party, an additional pre-payment deposit amount would be requested by the FAA (the 'ratchet request') at the point the deficit occurred.

The requested ratchet amount would be as follows:

*Deficit amount \* 11 (set multiple based on maximum possible number of months remaining until RF)*

Payment of the ratchet request would be mandatory for the withdrawn Party. In the event of a non-payment, the FAA would resume issuing Advice Notes to the Party for any Reconciliation Charges not covered by the original deposit amount. Under existing paragraph A5.3.3(b) of the Code the withdrawn Party would remain liable for these charges and could be pursued for non-payment by BSCCo.<sup>8</sup> However, if the money could not be recovered it would be recouped from all remaining Parties via their Default Funding Shares.

Please note that payment of the Party's actual Reconciliation Charges, rather than the ratchet estimation of these charges, would be pursued.

### f) Remaining BSCCo Charges

The withdrawing Non-Supplier Trading Party would cease to pay all Specified BSC Charges (including the Base Monthly Charge) from its Withdrawal Date. Where the Party's Withdrawal Date occurred part-way through the BSC (financial) Year in which its last Settlement Day fell, BSCCo would invoice the Party for its remaining share of Annual Net Main Costs and Annual Default Costs following the final determination of BSCCo Charges for that BSC Year. Please note that the withdrawn Party's remaining share of Annual Net Main Costs and Annual Default Costs for that year would relate to any adjustment of the BSCCo Charges paid by the Party up to its Withdrawal Date (see Section 1.3.10 for more detail).

Under A5.3.3(b) the withdrawn Party would remain liable for payment of these charges, and BSCCo would seek to pursue any non-payment. However, any costs unpaid by the Party would be recovered via all remaining Parties' General Funding Shares on a default basis.<sup>9</sup>

Where the final annual determination of BSCCo Charges resulted in amounts payable to the withdrawn Party in respect of that BSC Year, BSCCo would seek to issue a rebate to the Party. If this repayment could not be made (due to the Party having wound up its operations as a company), the money would be redistributed to all remaining Parties via their General Funding Shares on a default basis.

Please note that a Party's BSCCo Charges could not be paid using the Reconciliation Charges deposit held by the FAA, which is unable to hold money for purposes other than Credit Cover or Trading Charges. The SSMG therefore developed an Alternative Modification under which a withdrawing Non-Supplier Trading Party would be required to lodge an additional deposit with BSCCo to cover such costs (see Sections 1.3.10 and 1.6.1).

## 1.3 Issues raised by the Proposed Modification

This section outlines the discussions of the SSMG regarding the following issues raised by the Proposed Modification:

- The eligibility for, and timing of, early withdrawal;

<sup>8</sup> A5.3.3(b) states that withdrawal from the Code does not release a Party from 'any rights and liabilities (whether actual, contingent, accrued or otherwise) of a Party which may accrue pursuant to any Reconciliation Settlement Run or Extra Settlement Determination relating to any Settlement Day up to and including the last Settlement Day'.

<sup>9</sup> Definitions of BSCCo Charges, Specified BSC Charges, Base Monthly Charge, Annual Net Main Costs, Annual Default Costs and General Funding Shares can be found in Section D of the Code.

- The administration of the Reconciliation Charges deposit by the FAA;
- Potential Reconciliation Charges deposit calculation options;
- VAT issues relating to the Reconciliation Charges deposit;
- The withdrawn Party's exit from future legal obligations under the Code;
- The risk of underestimation of the withdrawn Party's actual Reconciliation Charges;
- The risk of Trading Disputes entering Settlement after R2; and
- The outstanding BSCCo Charges of the withdrawn Party.

A summary of the Group's view regarding the merits of the Proposed Modification against the Applicable BSC Objectives can be found in Section 1.4.

### **1.3.1 Eligibility for, and timing of, early withdrawal**

#### **a) Existing definition of Non-Supplier Trading Party**

The SSMG noted that the intention of the Proposer was to exclude owners of Non Half Hourly (NHH) Meters from withdrawing prior to RF, since the Reconciliation Charges for such Parties would be the most susceptible to change between R2 and RF due to their initial estimated Settlement data becoming replaced with actual Meter readings. The Group considered that in principle there was no reason why owners of purely Half Hourly (HH) Meters should be excluded from the P178 process since their initial Settlement data would have been based on actual Meter readings and therefore any changes in Reconciliation Charges for such Parties after R2 were likely to be minimal.

However, the SSMG noted that the Modification Proposal sought to make the P178 shortened withdrawal process available to all Non-Supplier Trading Parties as defined in paragraph M2.3A.7 of the Code. The Group noted that the effect of using this existing definition would be that all Suppliers would be excluded from using the P178 process regardless of whether their SVA Metering Systems were HH or NHH. The SSMG noted that this reflected the earlier agreement of the Issue 12 group that attempting to make such a distinction in order to allow HH Meter Registrants to withdraw after R2 would be overly complex, and that Suppliers with purely HH Meters would in any case be rare since most would tend to have a mixture of HH and NHH Meters.

The SSMG therefore agreed that using the definition of Non-Supplier Trading Party would sufficiently capture those Parties who were not subject to SVA activity and thus the intended beneficiaries of P178 – i.e. non-physical traders, and Parties with CVA Metering Systems such as generators and Interconnectors. The Group also noted the benefits of using an existing Code definition for P178 rather than attempting to newly-define other types of Trading Party, such as 'non-physical trader'.

#### **b) Eligibility of Non-Supplier Trading Parties in insolvency/administration**

The SSMG noted that, following implementation of P127 Alternative,<sup>10</sup> where a Party is in Default under H3.1.1(g) as a result of its insolvency or being in administration this does not in itself prevent that Party from withdrawing from the Code. Such a Default is not counted as a Default capable of remedy, and the Panel may determine that the Base Monthly Charge incurred after the date of the Party's Withdrawal Notice shall not prevent its withdrawal.

The SSMG noted that a Non-Supplier Trading Party which was in insolvency or administration, but which met all other relevant withdrawal criteria, would therefore be able to use the P178 shortened

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<sup>10</sup> Modification Proposal P127 'Option de-registration by insolvent Party'.

process to withdraw after R2. The Group noted that the Modification Proposal made explicit reference to the inclusion of such Parties.

### **c) Point of withdrawal under P178**

The SSMG considered whether the point of early withdrawal under P178 should be following the completion of the R2 run, or the corresponding Payment Date for any resulting Reconciliation Charges. The Group agreed that Non-Supplier Trading Parties should only be able to withdraw once they had paid all Reconciliation Charges up to and including R2, and that the point of withdrawal under P178 should therefore be the R2 Payment Date.

The SSMG noted the intention of the Proposer that a Non-Supplier Trading Party should be able to withdraw at any time after R2. The Group agreed that any Parties who might not wish to withdraw at R2, or who might not be in a position to do so due to other withdrawal criteria, should not be prevented from realising the benefits of P178 at another point prior to RF. The Group therefore agreed that such Parties could choose to withdraw under P178 on any calendar day between the R2 and RF Payment Dates. The Group noted that this would require the Central Registration Agent (CRA) to record the dates of the R3 and RF runs for the Withdrawing Party's last Settlement Day on the withdrawal checklist provided to BSCCo (see Section 4).

#### **1.3.2 Administration of Reconciliation Charges deposit by the FAA**

The SSMG noted that some Parties already choose to lodge cash with the FAA as pre-payment of their Trading Charges, and agreed with the Proposer's suggestion that the P178 process should be an extension of this existing ability. The Group noted that this is currently an informal process, and agreed that it would be desirable for the processes for administering the P178 Reconciliation Charges deposit to be formalised in Code and BSC Agent documentation. The Group noted that no changes to FAA systems would be required, since its administration of the deposit would use existing functionality and new manual processes (see Section 4).

The SSMG noted that the Reconciliation Charges deposit would be entirely separate to any Credit Cover which a Party might have lodged prior to its withdrawal.

The SSMG noted the Proposer's intention that no Advice Notes or Confirmation Notices would be issued to the Party following its withdrawal, in order to reduce administrative costs. However, the Group noted BSCCo's advice that the FAA would still be required to issue Confirmation Notices in order to comply with its legal obligation to issue VAT invoices (see Section 1.3.6). The Group therefore agreed that only Advice Notes should be suppressed for a Party which withdrew after R2.

An attendee suggested that formalising the FAA's ability to accept 'pre-payments' would also benefit those Parties who already choose to lodge cash towards their future Trading Charges under the existing informal process. However, the Group noted that this lay outside the scope of P178, which would only formalise pre-payment for Withdrawing Non-Supplier Trading Parties and not for Parties which remained in the Code.

#### **1.3.3 Potential Reconciliation Charges deposit calculation options**

The SSMG considered four potential options, as outlined on the following page, for calculating the cash withdrawal deposit amount which should be lodged by a Non-Supplier Trading Party withdrawing after R2.

#### **Note on Reconciliation Charges Deposit Options**

Deposit Options 1 and 2 represent developments of the first two options originally suggested in the Modification Proposal, and are based on a positive correlation between a Party's Generation Capacity

(GC) value and its £ withdrawal deposit. Option 1 also uses the Credit Assessment Price (CAP), the value of which may be revised from time to time under Section M1.4 of the Code and is currently set at £21.15/MWh (inclusive of VAT).

Deposit Option 3 was developed as an additional option during the Group's discussions of P178, and is based on the Code's existing P152 Credit Cover calculation for Non-Supplier Trading Parties. This option was eventually chosen by the SSMG as the final calculation for the P178 Reconciliation Charges deposit.

The Modification Proposal's remaining two suggestions (a fixed amount stipulated in the Code and an amount set by the Panel) were combined by the Group as Deposit Option 4.

All calculations for Deposit Options 1-3 would be carried out by BSCCo using 12 months of historic data extracted from its Trading Operations Market Analysis Systems (TOMAS). Where these options refer to a Non-Supplier Trading Party's last day of trading, this is defined in paragraph M2.3A.6 of the Code as being 'the earliest date on which there are no Energy Contract Volume Notifications or Metered Volume Reallocation Notifications in force in respect of which the Non-Supplier Trading Party is a Contract Trading Party and there is no credited Energy in either the Production or Consumption Account of such Non-Supplier Trading Party'.

**Reconciliation Charges Deposit Option 1**

BSCCo would carry out an annual calculation of each Non-Supplier Trading Party’s average R2-RF gross decrease in Credited Energy Volumes (i.e. increase in Imports/decrease in Exports) over the previous 12 months, as a percentage of each Party’s RF volumes. An absolute average X% decrease across all Non-Suppliers would be calculated.

At the time of a Non-Supplier’s withdrawal, BSCCo would then scale the average X% to the individual Party using the number of Settlement Days remaining until RF, the Party’s GC at its last day of trading (incorporating associated Credit Assessment Load Factors (CALF) and multiplied by 24 hours to give a day figure), and the current value of CAP.

The deposit amount left by the Withdrawing Party can therefore be expressed as follows:

$$X\% * remaining Settlement Days * (GC at Party's last day of trading * CALF) * 24h * CAP$$

Or as: % multiplied by MW, converted to MWh, multiplied by £/MWh

The absolute value of the calculated deposit figure would be used.

**Reconciliation Charges Deposit Option 2**

BSCCo would carry out an annual calculation of the average £ per day gross increase in R2-RF Reconciliation Charges payable by each current Non-Supplier Trading Party over the previous 12 months. This would then be converted into a £X/MWh/day figure for each Party using its current registered GC value (incorporating associated CALF and multiplied by 24 hours). An average across all Parties would then be calculated.

At the time of a Non-Supplier’s withdrawal, BSCCo would scale the average £X/MWh/day to the individual Party using the number of Settlement Days remaining until RF, and the Party’s GC at its last day of trading (incorporating CALF and multiplied by 24 hours).

The deposit amount left by the Withdrawing Party can therefore be expressed as follows:

$$£X/MWh/day * remaining Settlement Days * GC(at Party's last day of trading, with associated CALF) * 24h$$

The absolute value of the calculated deposit figure would be used.

**Reconciliation Charges Deposit Option 3**

This option would only be based on the historic behaviour of the individual Withdrawing Party, and would therefore require no annual calculation to be undertaken by BSCCo.

At the time of a Non-Supplier’s withdrawal, BSCCo would calculate the Party’s estimated gross increase in payable Reconciliation Charges up to RF, using that Party’s historic charges over the 12 months prior to its last day of trading. This would be a variation of the Code’s existing calculation in M2.3A for P152. Under P178, this calculation would be adapted to take into account only the Settlement runs remaining until RF (so if a Party withdrew following the R3 Payment Date, the calculation would be performed for the RF run only).

The deposit amount left by the Withdrawing Party would therefore be as follows:

$$\sum_{x \in (3, F)} NR_{xSP} * \frac{\sum_{Rx(j)} \max(Rx C_j, 0)}{RxSP}$$

RxSP is the count of all Settlement Periods falling any time up to a year before the date on which the Non-Supplier Trading Party in question ceased trading for which the Rx Reconciliation Run has been performed or if this number is less than 1440 (30 days) then 1440.

ΣRx(j) represents summation over all Settlement Periods falling within a year before the date on which the Non-Supplier Trading Party in question ceased trading for which the Rx Reconciliation Run has been performed or if the number of Settlement Periods in this sum is less than 1440, then the summation over the last 1440 Settlement Periods for which the Rx Reconciliation Run has been performed.

RxCj represents the Reconciliation Charges (as defined in N6.4.3) payable by the Non-Supplier Trading Party (summed across its accounts) due to the Rx Reconciliation Run in the relevant Settlement Period.

NRxSP represents the count of all Settlement Periods up to and including the date on which the Non-Supplier Trading Party ceased trading for which the Rx Reconciliation Run has not been performed.

**Reconciliation Charges Deposit Option 4**

The Panel would set a withdrawal deposit amount, which it could review from time to time as required. Potentially, this could be a variation of Deposit Options 1, 2 or 3 where the Panel has the ability to review and amend the calculation.

### 1.3.4 SSMG discussion of Reconciliation Charges deposit calculation options

This section summarises the SSMG's discussions of the potential advantages and disadvantages associated with each calculation option. For more background regarding the Group's development of these options, please refer to the P178 Assessment Procedure consultation document.

The calculations for Deposit Options 1-3 all attempt to predict a withdrawing Non-Supplier Trading Party's future Reconciliation Charges up to RF, using different methodologies to arrive at this estimate. The SSMG noted that Reconciliation Charges could be payable both from and to a Party, and therefore considered whether the calculations should seek to estimate gross payable or net changes in these charges between R2 and RF. As an example, the Group noted that if a Party was required to pay £1,000 in Reconciliation Charges in respect of the R3 run for a Settlement Day, but its RF run for that Settlement Day resulted in a payment to the Party of £250, its gross R2-RF charges for the Settlement Day would be £1,000 whilst its net charges would be £750. The SSMG noted that the FAA's debits from the P178 Reconciliation Charges deposit would take place at each Settlement Run for each of the Party's Settlement Days, and therefore that the cash amount left by a Withdrawing Party would need to cover its estimated gross payable charges in order to avoid a shortfall on any given day (i.e. in the example given above the deposit would need to cover the £1,000 payable at the R3 run for that Settlement Day).

The SSMG therefore agreed that Deposit Options 1-3 should all attempt to predict a Withdrawing Party's future gross payable Reconciliation Charges. The Group noted that any amounts payable to the Party between R2 and RF would be credited to its deposit amount by the FAA – with any surplus deposit returned to it after RF, along with a statement of its final net position.

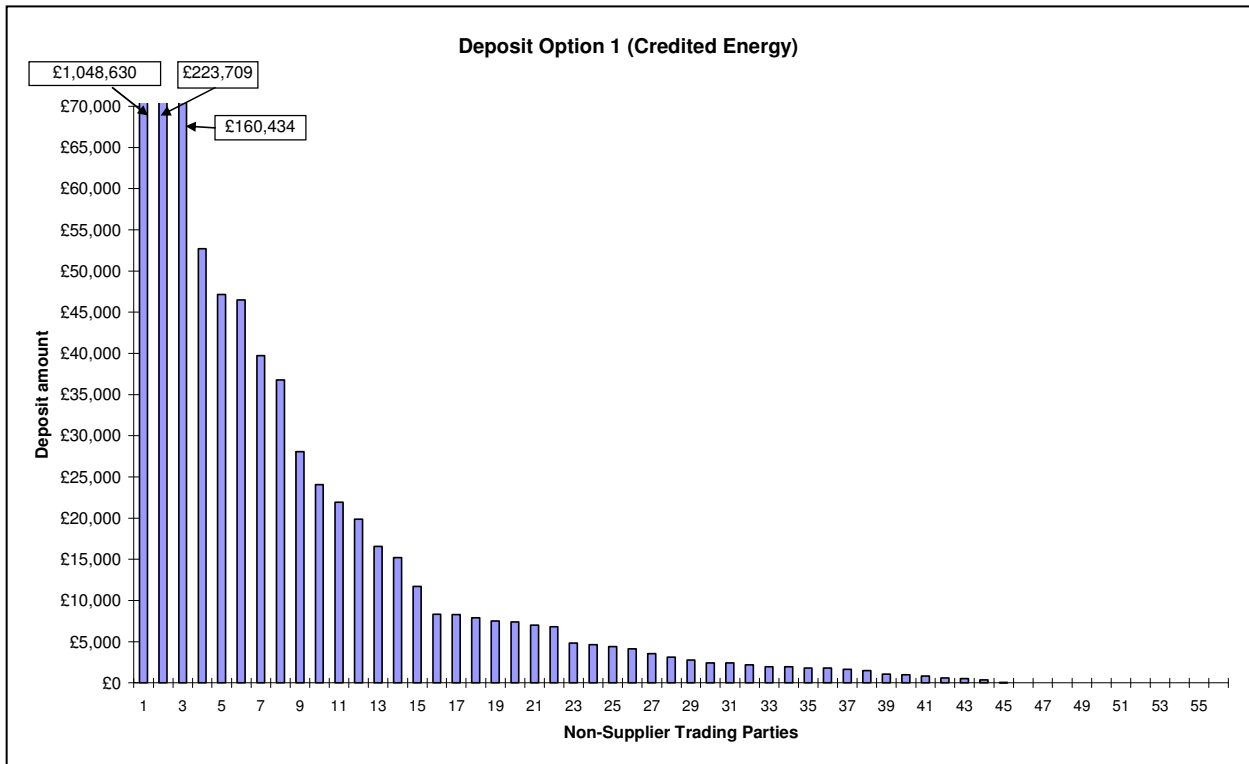
#### Reconciliation Charges Deposit Option 1

The SSMG noted that the intention of Deposit Option 1 was to predict a withdrawing Non-Supplier Trading Party's future gross payable Reconciliation Charges using the average historical gross decrease in energy volumes across all Non-Supplier Trading Parties between R2 and RF, scaled to the size of the Withdrawing Party.

The SSMG noted the following sample analysis provided by BSCCo of the £ deposit figures which would be generated for current Non-Supplier Trading Parties under the Deposit Option 1 calculation. The graph below is based on Credited Energy Volumes for the R2 and RF Reconciliation Settlement Runs in respect of Settlement Days between 10/04/03 and 15/09/03.<sup>11</sup> Where appropriate, Parties' latest GC values were used in place of GC at the last day of trading (since the data is based on current Parties).

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<sup>11</sup> Please note that the Settlement Day ranges of the sample data for Deposit Options 1, 2 and 3 are different and reflect the TOMAS data available at the time the calculations were run.



Having considered this sample analysis, the SSMG agreed that Deposit Option 1 would have the following potential disadvantages:

- Basing the calculation on a fixed value calculated using an average would mean that Parties' future liabilities would always be either overestimated or underestimated (see below);
- Since Credited Energy Volumes represent only one element of Reconciliation Charges, the resulting deposit amount might not take account of other reasons for increased charges such as Residual Cashflow Reallocation Cashflow (RCRC) payments as a result of upheld Trading Disputes; and
- Since CAP may not be reflective of imbalance prices, the calculation might not fully estimate a Parties' future Reconciliation Charges.

The SSMG noted that those Parties for whom Deposit Option 1 resulted in an overestimate would be required to lodge a deposit amount which exceeded their actual liabilities, even if their GC value was low. One member argued that this overestimate might act as a disincentive if the requested deposit materially exceeded a Party's actual Reconciliation Charges. It was queried whether this would effectively penalise smaller Parties by allowing those with larger liabilities to achieve the benefits of withdrawing after R2, whilst those with small future charges (the intended beneficiaries of the Modification Proposal) were disincentivised from using the P178 process. It was suggested that the cost of capital would be higher for smaller Parties, who might not be able to afford to lodge the requested amount up front – and that Parties in administration might also find it difficult to raise such amounts. The Group noted that the sample analysis for Option 3 showed that the actual gross payable Reconciliation Charges of many smaller Non-Supplier Trading Parties might only be in the area of £200 (see below).

A majority of SSMG members did not consider an overestimation to necessarily be a disincentive to using the P178 process, since any excess deposit would be returned to the Party following RF. Some members of the Group noted that the P178 withdrawal process would be voluntary, and that a Party could choose to remain until RF under the existing process if it did not wish to lodge the requested



deposit amount. These members noted that basing the Deposit Option 1 calculation on an average would also mean that many Withdrawing Parties' future charges could be underestimated, and therefore create the risk that their deposit amounts might prove insufficient. These members noted that this could potentially create 'bad debts' which would be recovered from remaining Parties (see Section 1.3.8). A majority of members therefore agreed that if Option 1 was adopted, the X% in the calculation should be based on a higher than average (rather than an average) amount – potentially the average amongst those Non-Supplier Trading Parties which had the highest 25% of changes.

The Proposer's Representative disagreed with this approach, arguing that this increased overestimation of the majority of Parties' charges would discriminate against smaller players and therefore be contrary to the intention of the Modification Proposal which intended the deposit to be proportionate to the likely charges of the individual Withdrawing Party. The Proposer's Representative argued that the reasons a Non-Supplier Trading Party would be withdrawing in the first place would be because it was a smaller player, whose operations in the market had not proved profitable and who therefore would have reduced liquidity. The Proposer's Representative stated their belief that the intention of such Parties was not to avoid their future liabilities, and that they would be willing to pay a deposit in order to achieve the benefits of P178 – but that if the requested amount was not a reasonable estimate of the risk posed by the Party, this would unfairly penalise it for its early withdrawal. The Proposer's Representative reiterated their view that the actual amount of post-R2 Reconciliation Charges for such Parties would be small and that the risk posed to the rest of the market by their early withdrawal would be minimal.

The other members of the Group noted these views, but argued that the deposit also needed to be proportionate to the risks to remaining Parties of allowing a Party to withdraw early, and therefore that a deposit which overestimated the majority of Parties' future charges (based on a higher-than-average amount) would offer greater protection than one which would underestimate those for up to half of Non-Supplier Trading Parties (based on an average amount).

The SSMG noted that the calculation for Deposit Option 1 would still return a deposit amount for a Party which had not traded during the last 12 months, since the GC for its last day of trading would be used. However, the Group noted that the calculation would return a deposit amount of zero for non-physical traders, since these Parties would not have GC values (due to not owning BM Units). The Group therefore unanimously agreed that if Option 1 was adopted, a minimum deposit amount would need to be set to cover the future Reconciliation Charges of such non-physical traders.

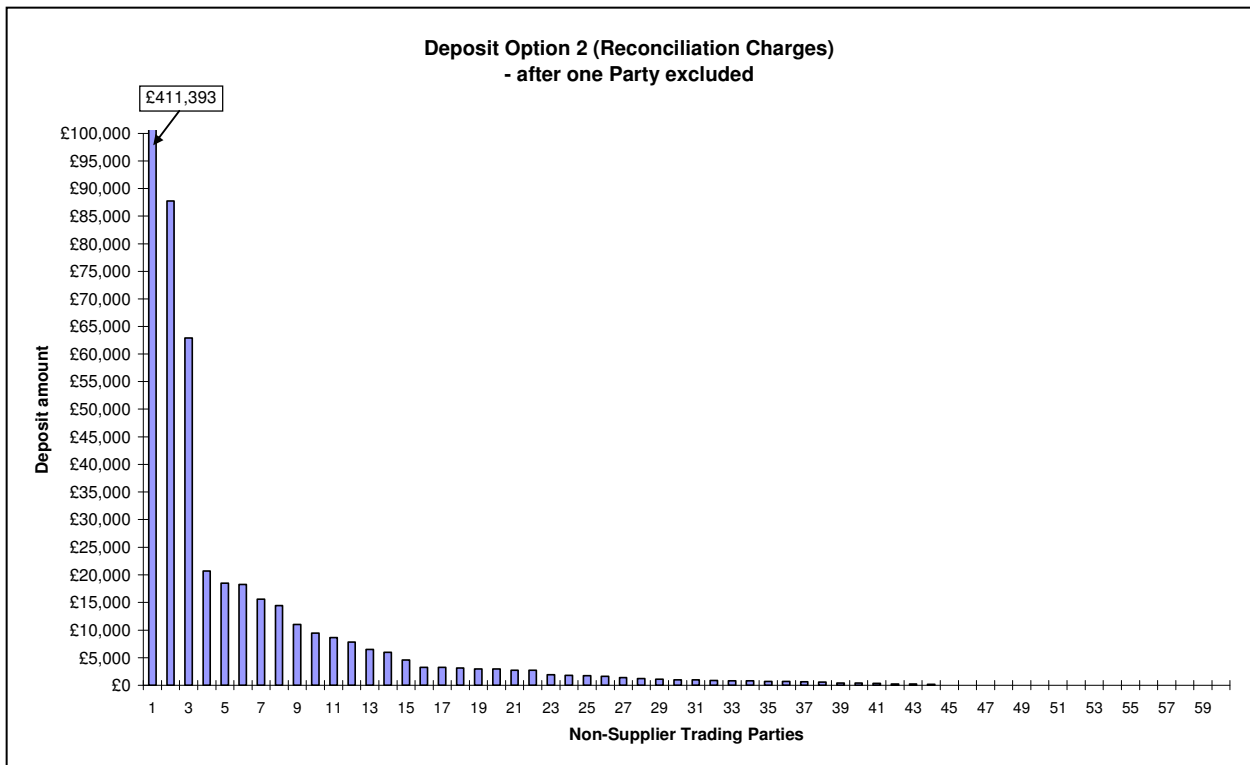
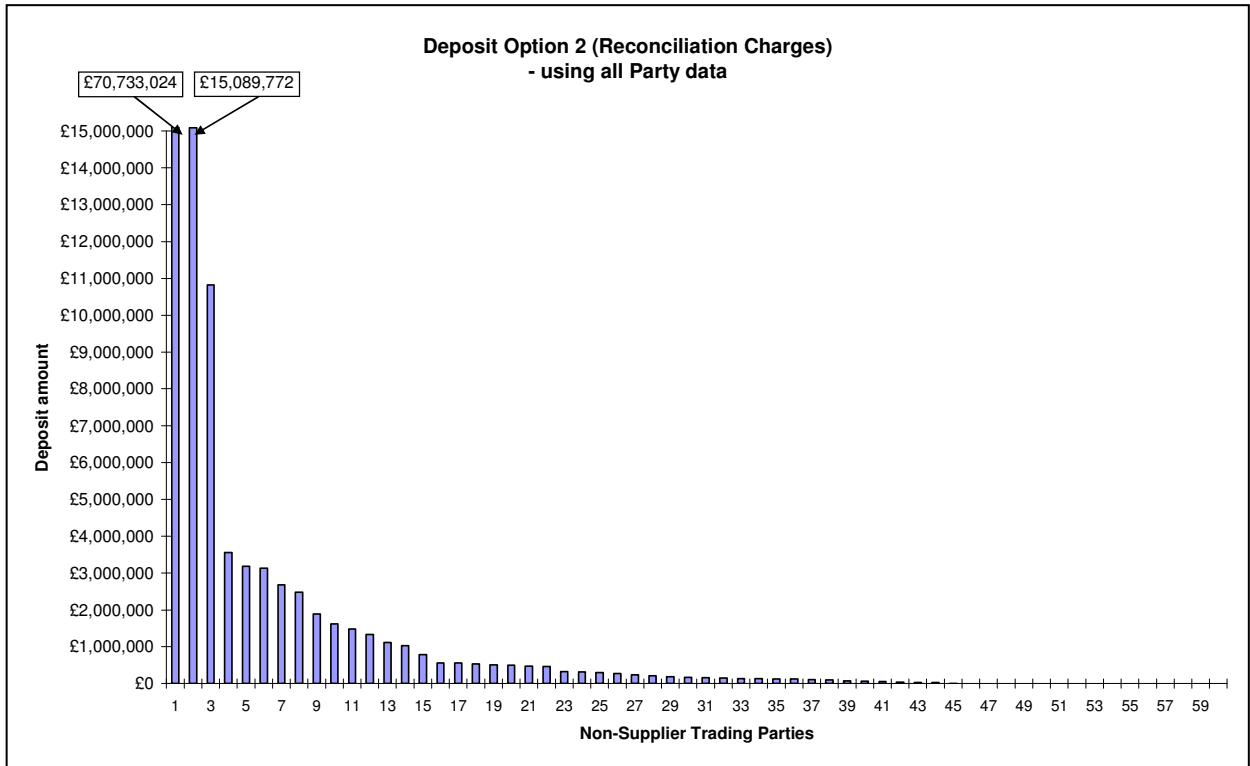
## **Reconciliation Charges Deposit Option 2**

The SSMG noted that the intention of Deposit Option 2 was to predict a withdrawing Non-Supplier Trading Party's future gross payable Reconciliation Charges using the average historical gross increase in such charges across all Non-Suppliers between R2 and RF, scaled to the size of the Withdrawing Party.

The SSMG noted the following sample analysis provided by BSCCo of the £ deposit figures which would be generated for current Non-Supplier Trading Parties under the Deposit Option 2 calculation.

The first graph below is based on the gross increase in payable Reconciliation Charges (extracted from TOMAS) for all current Non-Supplier Trading Parties between the R2 and RF Reconciliation Settlement Runs for Settlement Days between 23/12/02 and 31/07/03. Where appropriate, Parties' latest GC values were used in place of GC at the last day of trading (since the data uses current Parties).

The sample calculations were also rerun after removing one Party from the average due to its extremely high charges. The second graph shows the £ deposit amounts resulting from the calculation after this Party had been excluded from the sample.



Having considered the sample analysis and the responses received to the P178 Assessment Procedure consultation, the SSMG agreed that the potential advantage of Deposit Option 2 over Deposit Option 1 would be that its calculation of a Party’s estimated future Reconciliation Charges would be based on actual historic charges across Non-Supplier Trading Parties, rather than attempting to derive these using changes in Credited Energy Volumes. The Group considered that Option 2 would therefore take account of those additional elements of Reconciliation Charges which were not covered by Option 1.

However, the SSMG considered that this potential advantage of Option 2 would be outweighed by the disadvantages of basing the calculation on a fixed value calculated using an average, as outlined above under Option 1 and as shown in the difference between the two sample analysis graphs. The Group noted that a Party's deposit amount would be skewed upwards by the highest historical charges of a Non-Supplier Trading Party (thus overestimating many Parties' future charges) but would not cover the 'worst case' scenario since it would still be an average (thus underestimating future charges for other Parties). As for Option 1, a majority of members therefore agreed that the X% in the Option 2 calculation should be based on a higher-than-average amount – although the Proposer's Representative disagreed and argued that this would discriminate against smaller players.

One member of the SSMG expressed concern that the Option 2 calculation might be open to abuse, with Parties reducing their GC prior to their last day of trading in order that their deposit amount would be less when they withdrew from the Code. The other members of the Group noted that this was a possibility, and that this risk would also apply to Deposit Option 1.

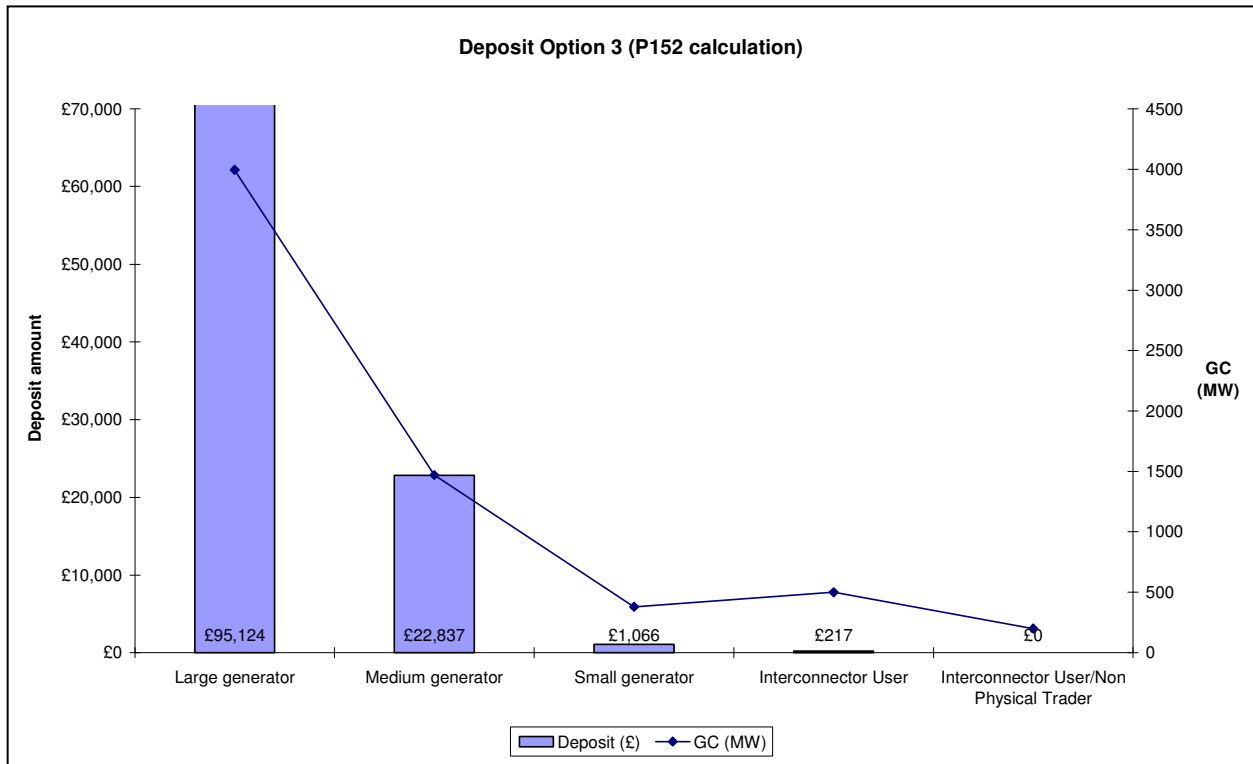
As for Option 1, the Group agreed that a minimum deposit amount would need to be set for non-physical traders if Option 2 were progressed.

### **Reconciliation Charges Deposit Option 3**

During discussion of Deposit Options 1 and 2, the SSMG noted that Section M2.3A of the Code already contains a calculation to estimate a Non-Supplier Trading Party's future gross payable Reconciliation Charges for the purposes of reducing Credit Cover under P152. The Group noted that the existing P152 calculation is very similar to the intention of the P178 Reconciliation Charges deposit options, in that it estimates the future gross payable Reconciliation Charges of an individual Non-Supplier based on that Party's historic charges over the previous 12 months.

The SSMG noted the following sample analysis provided by BSCCo of the £ deposit figures which would be generated for five current Non-Supplier Trading Parties under the Deposit Option 3 calculation, based on the Parties' historic Reconciliation Charges (extracted from TOMAS) for Settlement Days between 10/04/03 and 15/09/03. The Group agreed that the sample analysis did not need to include all current Non-Suppliers, since the calculation was specific to the Withdrawing Party concerned.

The five sample Parties were selected to represent different types and sizes of Non-Supplier Trading Party as shown on the graph. Although GC is not used in the calculation for Deposit Option 3, the Parties' latest GC values are shown on the graph to illustrate the positive correlation between the size of the Party and its deposit amount.



Having considered the sample analysis and the responses received to the P178 Assessment Procedure consultation, the SSMG agreed that Deposit Option 3 would offer the following potential benefits over Deposit Options 1 and 2:

- The calculation would only take place when a Party wanted to withdraw, rather than being carried out annually regardless of usage.
- The calculation would be based on an individual Party's historic data rather than using an average of other Parties' historic data, and would therefore:
  - reduce the risk of underestimation present in the calculations for Options 1 and 2 – providing greater protection to remaining Parties; and
  - reduce the risk of overestimation present in the calculations for Options 1 and 2 – generating a deposit amount which would be more proportionate to the Party's likely future charges and therefore potentially less discriminatory for smaller Parties.
- Both Deposit Options 1 and 2 assume that all of the Withdrawing Party's Settlement Days will not yet have been the subject of a R3 or RF run, and therefore use a fixed value based on average R2-RF changes (although this is then multiplied by only those Settlement Days remaining). However, each of the Party's Settlement Days would be going through these runs at different times in a proportion which would be determined by the timing of the Party's withdrawal. This is taken account of in Deposit Option 3, since if a Party withdrew after the R3 Payment Date the calculation could be adjusted to estimate R3-RF charges only.
- The Authority approved the P152 calculation, and may therefore consider an adapted version under Deposit Option 3 to be robust for P178.
- Using the P152-based calculation could avoid any perceived inconsistency in having two different methodologies in the Code for calculating a Party's future Reconciliation Charges – one for the purposes of Credit Cover (P152) and one for withdrawal (P178). The Group noted that using two different methodologies to calculate the same liabilities might potentially raise concerns regarding the legitimacy of the calculations.

- The ELEXON implementation effort to adapt an existing calculation under Deposit Option 3 would be of a smaller magnitude than the effort which would be required to build a new TOMAS calculation for Deposit Options 1 or 2. The ELEXON operational effort would also be less, as the calculation for Deposit Option 3 would be carried out on an ad hoc basis rather than annually.

The Group noted that if the calculation was performed using data over the 12 months prior to a Party's Withdrawal Date, it would return a zero amount for a Party which had not traded over that period. The SSMG therefore agreed with the suggestion of one consultation respondent that the calculation should use data from the 12 months prior to the Party's last day of trading, so that a minimum deposit amount would not need to be set (see Section 6).

The SSMG noted that under P152 the Panel reviews, and may refuse, a Non-Supplier Trading Party's request to reduce its Credit Cover. The Group therefore considered whether a similar process would be desirable for the Non-Supplier's application for early withdrawal under P178 – noting the suggestion of consultation respondents that the Reconciliation Charges deposit amount could be appealed to the Panel, or that the Panel should add an additional 'X%' to each Party's deposit amount under Option 3 (see Section 6). However, some members considered that the resulting administrative effort would outweigh any potential benefits of including this element of Panel discretion, whilst others argued that it would not be desirable to introduce an element of subjectivity into the calculation. One member of the Group also argued that since the Panel does not normally have the opportunity to comment on a Party's withdrawal, it would not be appropriate for it to do so under P178.

#### **Reconciliation Charges Deposit Option 4**

The SSMG considered that any amount set by the Panel would be arbitrary, unless based on criteria that could be set out in the Code. The Proposer's Representative suggested that this option could simply be a variation of Options 1, 2 or 3, with the ability for the Panel to review the calculation from time to time if required. The Group noted that this could be similar to the Code's existing provisions in M1.4 for the Panel to review the value of CAP.

The SSMG considered that, compared with Deposit Options 1, 2 and 3, Deposit Option 4 could offer the potential advantage of additional flexibility – in that the calculation could be adjusted post-implementation if necessary to reflect actual operational experience of the P178 process. However, the Group expressed their preference for a mechanistic calculation for the Reconciliation Charges deposit and agreed that it would not be desirable to introduce an element of subjectivity under Option 4. As for Deposit Option 3, one member also considered that it would not be appropriate for the Panel to comment on a Party's withdrawal. The SSMG therefore unanimously agreed that the Reconciliation Charges deposit calculation should be 'hard-wired' into the Code without a built-in process for its review.

#### **Summary of SSMG view of Reconciliation Charges Deposit Options**

The SSMG noted the majority support for Deposit Option 3 amongst respondents to the P178 Assessment Procedure consultation, and that no respondents had expressed support for Options 1 or 2 (see Section 6). The Group unanimously agreed that Option 3 should be progressed as the final calculation for the P178 Reconciliation Charges deposit, since it believed that this option contained the least risk of underestimation of a Party's future charges.

However, a majority of members remained concerned that no calculation for estimating a Party's future Reconciliation Charges would satisfactorily reduce the risk of underestimation, due to the unpredictable nature of such charges. These members therefore did not support P178 since they believed it would not protect remaining Parties against the 'worst-case scenario' (see Sections 1.3.8 and 1.4). One

member noted that the P152 Modification Group and the Panel had recommended rejection of P152 for this very reason.

### 1.3.5 Calculation of Reconciliation Charges deposit ratchet request

The SSMG considered three potential options for the 'ratchet request' calculation as outlined below. Please note that Options A and B represent developments of the two options originally suggested in the Modification Proposal, whilst Option C was subsequently developed by the Group during its discussions.

#### **Ratchet Option A:**

Party's original deposit amount \*  $\frac{\text{no. of months remaining until RF}}{\text{no. of months between Party's Withdrawal Date \& RF}}$

#### **Ratchet Option B:**

Deficit amount \* number of months remaining until RF

#### **Ratchet Option C:**

A set multiple of the deficit amount (e.g. 5, 10).

The Group noted that Ratchet Options A and B would be based on the assumption that the Party would continue to incur Reconciliation Charges at the same rate as previously, and therefore agreed that the amount calculated by these options would be equally as arbitrary as that generated under Option C.

Some members of the SSMG argued that the need for a ratchet mechanism at all demonstrated the impossibility of accurately predicting a Party's future Reconciliation Charges, and therefore of having an original deposit calculation which protected against the 'worst-case scenario'. These members argued that the ratchet, regardless of which calculation was chosen, would simply be replacing one arbitrary deposit amount with another. It was also queried whether a ratchet mechanism was required, since any actual Reconciliation Charges which were not covered by a Party's deposit would be invoiced and pursued under A5.3.3. However, the Proposer's Representative stated their view that the benefits of P178 for a Withdrawing Party would be reduced without the ratchet, since it was necessary to allow the Party the opportunity for an additional 'pre-payment' and thereby avoiding the inefficiencies of receiving further Advice Notes.

The SSMG therefore unanimously agreed that the ratchet mechanism should be included, and that Option C should be progressed on grounds of simplicity. A set multiple of 11 was chosen by the Group since this represents the number of months between the R2 and RF runs for any given Settlement Day, and would therefore be the maximum number of months that a ratchet request would have to cover. The Group argued that this would therefore offer greater protection to remaining Parties than Option B.

It was suggested that a potentially more accurate ratchet calculation might be one which was proportionate to the number of the Party's Settlement Days which had not yet been the subject of R3 or RF runs – and therefore that the most accurate re-estimate of a Party's future charges might be to run the original deposit calculation again using more recent available data. However, the SSMG rejected this approach due to the additional effort it would require and since it considered that the need to deploy the ratchet would have demonstrated the inaccuracy of the original calculation.

The SSMG agreed that it would not be desirable to revise the deposit calculation for future Withdrawing Parties as a result of the ratchet mechanism being deployed, since this would be counter to the

principle of basing the deposit calculation on an individual Party's historic behaviour – particularly since the ratchet itself would be an arbitrary amount.

### **1.3.6 VAT issues relating to Reconciliation Charges deposit**

The SSMG considered that the main potential benefits of P178 would be if it enabled a Party to fully 'wind up' its operations as a company at R2 rather than after RF as currently, and if it reduced administrative overheads for the withdrawn Party and the FAA by removing the need to manage Advice Notes and Confirmation Notices following the Party's early withdrawal. The Group asked BSCCo to provide advice as to whether any VAT issues would arise from the suppression of Advice Notes and Confirmation Notices.

BSCCo advised that the Reconciliation Charges deposit would have VAT implications for the FAA, and potentially also for the withdrawn Party, as outlined below.

#### **FAA**

BSCCo clarified that every debit from or credit to the withdrawn Party's Reconciliation Charges deposit by the FAA would be required by law to include the VAT applicable to the debited or credited amount. With every debit or credit arising from trading cashflows taken from or added to the deposit, a VAT transaction would therefore legally occur. BSCCo advised that, as a result, the FAA would have to continue to issue Confirmation Notices to the withdrawn Party in order to comply with its own legal obligations to issue VAT invoices within 30 days of a transaction. BSCCo confirmed that, following the changed application of VAT to Trading Charges from 1 January 2005,<sup>12</sup> this would apply regardless of whether the Party concerned was registered for VAT at the UK-prevalent rate (17.5%) or was zero-rated.

#### **Withdrawn Party**

BSCCo clarified that any Party which, following 1 January 2005, was zero-rated for VAT in the UK would not have to account for the VAT and thus the Confirmation Notices should not stop a Party being able to fully 'wind up' its company following its early withdrawal at R2.

However, BSCCo advised that its understanding, based on informal discussions with ELEXON's tax advisor, is that the following could apply for any Party which was registered for VAT at the UK-prevalent rate (currently all VAT-registered Parties):

- For situations where ELEXON Clear issues Confirmation Notices stating that amounts have been paid to a Party (i.e. ELEXON Clear raising a 'self billing' VAT invoice), the withdrawn Party would be required by law to repay the VAT included in the amount paid (added to the deposit) to Customs and Excise. Note that this is the case even if the Party is not registered for VAT as it has effectively raised an invoice to ELEXON Clear and received VAT amounts that belong to Customs. Whilst not the concern of the Code this would therefore appear to prevent the Party from being able to fully 'wind up' its operations after R2, since it would need to receive the Confirmation Notices and pay any VAT due to Customs.
- In respect of Confirmation Notices stating that amounts have been paid from a Party (i.e. ELEXON Clear invoicing the Party) the withdrawn Party would be entitled to reclaim the VAT included in the amount paid (debit from the deposit) from Customs via its VAT return. If the Party was not registered for VAT then it would be unable to reclaim these amounts.

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<sup>12</sup> See Modification Proposal P170 'Amendments to the Balancing and Settlement Code, and to the systems and processes that support it, to allow compliance with the changed application of VAT to Trading Charges' for further details.

The Party would not be able to predict whether its future Reconciliation Charges would result in credits to or debits from its deposit (indeed for VAT purposes there may be both input and output tax relating to a single Confirmation Notice). It would appear that the Party would therefore not be able to fully wind up its operations after R2, since it would need to receive all Confirmation Notices and account for any VAT self-billed by ELEXON Clear regardless of its VAT registration status.

BSCCo summarised that the potential ability or inability for a Party to wind up its operations after R2 lies outside the vires of the Code, and therefore the scope of P178. However, BSCCo's understanding is that any Party which chose to do so might be non-compliant with its wider ongoing obligations under VAT law.

### **SSMG discussions**

The SSMG considered whether making the Reconciliation Charges deposit non-refundable as a potential Alternative Modification would avoid these VAT issues and enable a withdrawn Party to wind up its operations after R2. However, the Group noted BSCCo's advice that VAT transactions would still arise at the point of the cash flow (i.e. with every credit or debit by the FAA), and that the same issues would therefore apply to a non-refundable amount. The Group therefore agreed not to progress this option further – also noting that such an approach would in effect represent a charge for early withdrawal.

The Proposer's Representative suggested that withdrawn Parties might be able to avoid the requirement to remain a legal entity for VAT purposes by 'pre-paying' VAT through Customs and Excise. BSCCo advised that, although different methods of VAT pre-payment may exist, the Party would still be required to check its position and account for its VAT accordingly.

The SSMG noted that, since a withdrawn Party's ongoing VAT liabilities lay outside the scope of the Code they could not therefore be included in its assessment of P178 against the Applicable BSC Objectives. However, a majority of members considered that they would appear to negate one of the main potential benefits of the Proposal for Withdrawing Parties. The Proposer's Representative disagreed – arguing that the ability for a Party to wind up its operations was a peripheral issue for P178, and that the main rationale for the Modification Proposal was to allow a Party to exit the legal contract of the Code (see Section 1.3.7 below).

The SSMG noted that potential cost-savings for the FAA were within the scope of its assessment, and a majority of members considered that the requirement for it to continue issuing Confirmation Notices would reduce any potential administrative savings from P178. The Proposer's Representative noted that there would still be administrative savings from the suppression of Advice Notes for the withdrawn Party.

### **1.3.7 Withdrawn Party's exit from future legal obligations under the Code**

The Proposer's Representative reiterated their view that the current requirement for a non-operational Non-Supplier Trading Party to remain bound to the contract of the Code until RF results in unwarranted legal liabilities for such Parties, who will not necessarily have the staff or expertise to monitor their Code obligations – particularly as these could be changed by any Code modifications approved between R2 and RF.

Since all Parties remain liable for any accrued financial liabilities even after their withdrawal, it was queried whether the risk of any continuing or modified non-financial Code liabilities would be material to a non-operational Non-Supplier Trading Party. The Proposer's Representative cited the example of the retrospective Past Notification Error (PNE) claims process introduced by Modification Proposal P37



and modified by other subsequent Proposals.<sup>13</sup> However, the Group noted that the liabilities introduced by this process were also financial, and that a Party lodging a claim would have been prevented from withdrawing prior to its determination since its claims fee would have been counted as an accrued sum. Moreover, the Group noted BSCCo's advice that upheld PNE claims had impacted both existing and withdrawn Parties via RCRC – and that the obligation to pay any resulting invoices would not have therefore have been avoided had P178 been in place.

The Proposer's Representative also argued that company directors have a duty to monitor their organisation's obligations under any contract to which it is a party – and that this creates understandable anxieties for directors of non-operational companies who might no longer have the resources to do so, or for administrators of Parties in receivership who may have no necessary knowledge of the BSC arrangements. However, one member of the SSMG noted that any director or administrator had the ability to appoint advisors if this was a concern.

Moreover, other members of the SSMG noted that, whilst a Party could negotiate its way out of a bilateral contract with its counterparty, the Code was a multilateral contract where one Party's early withdrawal could impact all remaining signatories. These members therefore queried whether it was appropriate for a Party to be able to terminate its legal liabilities under the Code whilst the effects of its previous participation in that contract could still have a material impact on remaining Parties. These members considered that the value to an individual Party in being able to achieve an early withdrawal could be a loss to remaining Parties – particularly given the potential risk that the P178 withdrawal deposit could underestimate the Withdrawing Party's future charges (see below). One member of the Group was concerned that P178 might create the ability for a Party to achieve the benefits of early withdrawal only for it to rejoin the Code at a later point.

### **1.3.8 Risk of underestimation of withdrawn Party's actual Reconciliation Charges**

The SSMG noted the potential risk that a withdrawing Non-Supplier Trading Party's future Reconciliation Charges could be underestimated under P178, and therefore that its actual liabilities might exceed its original deposit amount. The Group noted that, under the proposed ratchet mechanism, an additional pre-payment amount would be requested from the Party – but accepted that there remained a risk that the ratchet amount might not be paid.

The SSMG noted that any unpaid Reconciliation Charges which could not be recovered from a Party which had withdrawn at R2 under P178 would be recouped from all remaining Parties. The Group noted BSCCo's advice that if the Party was in administration, BSCCo would rank with the Party's other creditors and would be paid according to priority as determined by law and the Party's administrators. BSCCo clarified that it does not hold details of the ownership structure of Code signatories, and that the Code does not provide for the transfer of liabilities to another Party. The Group therefore noted that if the original Party had wound up its operations, and no longer constituted a 'legal entity', BSCCo would have no powers to pursue a parent company.

The Proposer's Representative argued any non-payment of the P178 ratchet request would be covered by the Code's existing provision in A5.3.3 for a Party to be pursued for its financial liabilities even after its withdrawal. The Proposer's Representative noted that, under the current process, Parties who withdraw at RF may still accrue liabilities as a result of Post-Final Settlement ('DF') Runs or Extra Settlement Determinations (ESDs) – and argued that the risk of non-payment would not be materially increased if Non-Supplier Trading Parties with small future liabilities were allowed to withdraw from R2 onwards.

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<sup>13</sup> Modification Proposal P37 'To provide for the remedy of past errors in Energy Contract Notifications and in Metered Volume Reallocation Notifications'.

The Proposer's Representative also noted that requiring a company to remain a Party to the Code until RF offers no guarantee that the Party will pay its accrued charges – even if the Party is placed in Default. It was suggested that the risk of non-payment under P178 might therefore actually be less than currently, since the Withdrawing Party would have 'pre-paid' at least the bulk of its future Reconciliation Charges at R2.

The Proposer's Representative also reiterated their view it would not be in the interests of a withdrawn Non-Supplier Trading Party to refuse to pay the ratchet request, since they would want to avoid being issued with further Advice Notes. In addition, the Proposer's Representative argued that it was likely that either the withdrawn Party or its parent or sister companies would still be trading with remaining Parties in other markets, and would therefore not wish to damage their reputation with potential counterparties. However, one member of the SSMG questioned whether it was appropriate for a Party to be able to avoid further Code obligations under P178 whilst still operating in other markets. Notwithstanding the VAT issues associated with the deposit, it was also suggested that if the Code could not prevent a Party from winding up its operations after withdrawing at R2 then this was an argument against P178 – since the FAA was unlikely to be able to retrieve payment of any Reconciliation Charges not covered by the deposit from a Party that no longer constituted a 'legal entity'.

A majority of SSMG members considered that it was not possible to accurately estimate a Withdrawing Party's future charges – arguing that if it was possible to do so these charges would be settled earlier in the reconciliation timetable, with the result that later Settlement Runs would not be required. These members noted that similar conclusions had been drawn by the Modification Groups for previous Modification Proposals P127, P132 and P152.<sup>14</sup> Given that the proposed ratchet mechanism could not guarantee payment of a withdrawn Party's future liabilities, these members considered that the P178 process would not offer adequate assurance to the rest of the market that they would not be picking up elements of other Party's post-R2 charges – and that the current withdrawal timescales should therefore be retained. These members also considered that it could be easier for BSCCo to pursue payment by a Party which was still a Code signatory, than one which had withdrawn and might no longer constitute a legal entity.

The Proposer's Representative disagreed, and argued that it was unfair to base assessment of P178 on the presumption that a withdrawn Party would seek to default on its future payments.

### **1.3.9 Risk of Trading Disputes entering Settlement after R2**

The SSMG noted that a Party could be prevented from withdrawing from the Code if any sums accrued by the Party prior to its Withdrawal Date had not been paid. However, the Group noted BSCCo's legal advice that the Code did not prevent a Party's withdrawal on the grounds of contingent liabilities – for example, the pending outcome of a Trading Dispute. The Group noted that the determination of a Dispute had the potential to affect all Parties via their Metered Volumes, imbalance charges and RCRC, and that there was therefore the risk that a Trading Dispute entering Settlement after R2 could have a material financial impact on a withdrawn Party which was not covered by its Reconciliation Charges deposit.

The SSMG noted BSCCo's advice that it was not possible to provide analysis of when the majority of upheld Trading Disputes enter Settlement, or the average materiality through RCRC of an upheld Dispute for a Non-Supplier Trading Party, since this information is not held by BSCCo. However, the Group noted the total materiality of upheld Disputes in each BSC Year as outlined in the table below.

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<sup>14</sup> Modification Proposal P132 'Redefinition of Credit Cover Requirements to account for Reconciliation Charges' sought to require a Withdrawing Party to retain Credit Cover in order to protect against its future liabilities relating to Reconciliation Runs, Trading Disputes or PNE claims. The P132 Modification Group concluded that it was not possible to predict future Reconciliation and Trading Dispute liabilities.

### Total materiality of upheld Trading Disputes per BSC Year

BSC Year	Number of Disputes upheld	Total materiality for all Parties (including Suppliers)
2002-2003	29	£3.8 million
2003-2004	30	£6.04 million
2004-2005*	12*	£7.4 million*

\*As at 25 October 2004.

The SSMG noted that one example of a Trading Dispute being settled after R2 was DA223, which relates to the Emergency Instruction issued on 19 May 2004 (the 'Damhead Creek' Dispute) and is due to be settled in the R3 run on 15 December 2004 (subject to Pending Modification Proposal P181).<sup>15</sup> BSCCo advised that, whilst the exact materiality of the Dispute for individual Parties remains confidential, the average amount payable by Non-Supplier Trading Parties as a result of DA223 is estimated to be approximately £60,000 – with the materiality for individual Non-Suppliers ranging from under £10 to six-figure amounts. The sum of all amounts payable by Non-Suppliers as a result of DA223 is estimated to be over £600,000 (the largest upheld Trading Dispute since NETA Go-Live). The SSMG noted that these estimated materiality figures include both the direct impact of imbalance prices for Non-Supplier Trading Parties who were 'long' during the relevant Settlement Periods, and the indirect impact on Non-Suppliers through RCRC.

The Proposer's Representative argued that the Damhead Creek Dispute was a result of exceptional circumstances, and that it was reasonable to expect most Disputes to have been settled by R2. Moreover, the Proposer's Representative did not believe the risk of a minority of Disputes entering Settlement after R2 to be materially greater than the current risk that a withdrawn Party may be affected by a Dispute which is the subject of a DF run or an ESD, and noted that BSCCo could pursue a Party for any necessary amount via the P178 'ratchet' mechanism and (if this was unpaid) under A5.3.3.

However, the other members of the SSMG remained concerned that a Dispute entering Settlement in the R3 or RF runs could have a material impact on a withdrawn Non-Supplier Trading Party via its RCRC – and that this could lead to the amount being recovered from remaining Parties through the Party's refusal, or inability, to pay the ratchet request. The members considered that, although extreme examples, events like the Damhead Creek Dispute or PNE claims process demonstrated how a Party's liabilities might significantly change after R2. These members therefore reiterated their view that it was not possible to accurately estimate a Withdrawing Party's future liabilities, and that it was therefore not desirable to allow Parties to withdraw prior to RF.

#### 1.3.10 Outstanding BSCCo Charges of withdrawn Party

The SSMG noted the intention of the Proposer that a Non-Supplier Trading Party would only be able to withdraw after R2 if it met all the other withdrawal criteria contain in A5.1.3 of the Code. However, the Group noted that one of these criteria is that a Party may not withdraw if (at 1700 hours on the day which is 2 Business Days prior to its Withdrawal Date) the final determination has not been carried out in respect of BSCCo Charges for the BSC Year in which the Party's last Settlement Day fell, or if the due date for payment of any resulting amounts has not yet passed.

The SSMG noted that this was not an issue for a Party withdrawing at RF since the current withdrawal timescale (14 months) would span the full BSC Year in which the Party last traded. However, the

<sup>15</sup> Modification Proposal P181 'NGC Emergency Instruction re Damhead Creek 19.05.04: Deferral of Settlement Process'.

Group considered that if this requirement remained unchanged it could defeat the intention of early withdrawal under P178, since a withdrawing Non-Supplier Trading Party would have to remain a Party to the Code until some months after the end of the financial year in which its last Settlement Day fell.<sup>16</sup> The Group therefore agreed that the existing Code withdrawal criteria should be amended under the Proposed Modification to a requirement for the withdrawing Non-Supplier Trading Party to have paid only those BSCCo Charges accrued by its Withdrawal Date.

The SSMG noted that each Party's share of Monthly Net Main Costs is a proportion of its share of Annual Net Main Costs for the BSC Year. The Group noted that this proportion is adjusted from month to month according to the Party's weighted cumulative average Main Funding Share (based on its latest Initial Settlement ('SF') Run energy volumes), BSCCo's latest forecast of the full year costs, and the number of months remaining in the BSC Year. A Party's final share of Annual Net Main Costs is therefore not known until the final determination of actual BSCCo Charges following the end of the BSC Year. The Group noted that a Party which withdrew at R2 under P178 would have no further SF volumes, and therefore a Main Funding Share of zero. However, the Group noted that it would still accrue amounts up to the end of the BSC Year as a result of adjustments in the BSCCo Charges paid prior to its Withdrawal Date.

The SSMG noted that allowing a Non-Supplier Trading Party to withdraw part-way through a BSC Year would therefore create a shortfall in BSCCo's cost recovery if its subsequent invoices were unpaid. The Group considered that this risk of non-payment was the same as that for the Reconciliation Charges deposit ratchet request, in that any BSCCo Charges unpaid by the withdrawn Party would be recouped from all remaining Parties.

The SSMG therefore unanimously agreed that it would be desirable for the P178 withdrawal deposit amount to incorporate an estimate of a withdrawing Non-Supplier Trading Party's future BSCCo Charges, so that these would also be 'pre-paid'. However, the Group noted BSCCo's advice that this would require a separate additional deposit to be lodged with BSCCo, since the FAA is unable to hold money in respect of BSCCo Charges. The Group noted BSCCo's legal advice that this two-deposit solution would form an Alternative Modification for P178.

The SSMG were mindful of the Panel's request (via its Terms of Reference) for simplicity in the P178 solution, but agreed that this needed to be balanced against the potential risks posed by the Modification Proposal. The Group agreed that an Alternative Modification incorporating an additional deposit for a Withdrawing Party's future BSCCo Charges would reduce some of the risks of non-payment associated with the Proposed Modification, and should therefore be progressed. Details of the Alternative Modification can be found in Sections 1.5-1.7.

The Proposer's Representative stated that they had not considered the issue of BSCCo Charges in detail prior to raising P178. However, they clarified that they were happy to support the progression of this Alternative since they believed that the benefit for the Withdrawing Party of avoiding further invoices would be reduced unless it was able to pre-pay its future share of BSCCo Charges.

For the Proposed Modification, the SSMG agreed that BSCCo would invoice the withdrawn Party for its remaining share of Annual Net Main Costs and Annual Default Costs following the final determination of BSCCo Charges at the end of the BSC Year, and noted that the Party would continue to be liable for these amounts under paragraph A5.3.3 of the Code.

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<sup>16</sup> Due to the timescales required to publish that year's audited accounts, undertake the final determination of BSCCo Charges, and invoice the Party for any adjusted amounts.

## 1.4 Assessment of whether the Proposed Modification would better facilitate the Applicable BSC Objectives

### Majority view against Proposed Modification

The majority view of the SSMG is that the Proposed Modification would not better facilitate the achievement of the Applicable BSC Objectives and, specifically, that it would have a negative impact on Applicable BSC Objectives (c) and (d).

The arguments put forward against Objective (c) were as follows:

- It is not possible to accurately estimate a Non-Supplier Trading Party's future Reconciliation Charges between R2 and RF. The SSMG has been unable to identify a more accurate methodology for this estimation than basing it on the Withdrawing Party's historic Reconciliation Charges, which may not be reflective of its future level of liabilities – not least since these can be significantly affected by any Trading Disputes entering Settlement after R2, the number and materiality of which cannot be predicted. This view is consistent with the arguments previously expressed by the Modification Groups for P127, P132 and P152.
- The P178 Reconciliation Charges deposit calculation therefore contains the risk that a withdrawing Non-Supplier Trading Party's future charges could be materially underestimated. Although P178 contains a 'ratchet' mechanism for requesting an additional pre-payment in the event of any shortfall, there is the risk that the withdrawn Party either refuses or is unable to pay this increased amount – leading to it being recouped from all remaining Parties.
- A non-operational Non-Supplier Trading Party, which is planning to withdraw at RF under the current withdrawal timescales, may already simplify its exit without increasing the risks to other Parties. Under the existing route such Parties may already lodge cash with the FAA as pre-payment towards their Trading Charges, and reduce their Credit Cover to the Minimum Eligible Amount (or amount estimated to cover future Reconciliation Charges, if in insolvency or administration). The requirement to remain a Party until RF would therefore not appear to be a barrier to competition.
- The Code is a multilateral contract, and the aim of the current withdrawal timescales is to protect the market against the potential 'bad debts' of any one Party. The current arrangements are applied equally to all (a 'level playing field'), and therefore do not unduly discriminate against any one class of Party. Competition would be adversely affected if Parties were able to withdraw after R2 with the potential risk that their future charges might not be paid and might be recovered from remaining Parties – since this could create benefits for Non-Suppliers at the expense of the rest of the market (a potential 'cross-subsidy').
- A potential barrier to exit is not necessarily a barrier to entering the market, since Parties sign up to the Code with the expectation that the market will prove profitable and therefore that they will be in it for the long term. Moreover, the current withdrawal timescales may be viewed as less of a barrier to entry than the potential impact of allowing some Parties' early withdrawal.
- The withdrawal deposit under the Proposed Modification does not include an estimation of the Withdrawing Party's future share of BSCCo Charges. Although these would be invoiced to the Party, there is the risk that they would not be paid and would be recovered from remaining Parties – strengthening the argument that the Proposed Modification would create a cross-subsidy.
- Despite the Reconciliation Charges deposit, a withdrawing Non-Supplier Trading Party would not be able to achieve a final financial settlement at R2 under the Proposed Modification – since it might still receive a ratchet request (up to RF), invoices for BSCCo Charges (up to the

end of the BSC Year) or invoices for further DF runs or ESDs in respect of any of its Settlement Days (beyond RF).

The arguments put forward against Objective (d) were as follows:

- The requirement to issue Confirmation Notices for VAT purposes after R2 would reduce any potential administrative cost and efficiency savings for the FAA. Moreover, any potential savings for the FAA would be outweighed by the costs of implementing and operating the processes for the Reconciliation Charges deposit.
- Any potential benefits to BSCCo of not having to chase Parties, or process payment Defaults, for small amounts of Reconciliation Charges between R2 and RF would be outweighed by the ELEXON implementation and operational costs for the Proposed Modification;
- One member stated their view that the proposed P178 processes would be inefficient, and that the simplest, most efficient and least-risk way to leave the Code was under the current arrangements.

### **Minority view in support of Proposed Modification**

The Proposer's Representative continued to believe that the Proposed Modification would better facilitate the achievement of both Applicable BSC Objectives (c) and (d).

The arguments put forward in support of Objective (c) were as follows:

- The Proposed Modification would remove barriers to exit for Non-Supplier Trading Parties by introducing a simpler and more timely withdrawal route for those Parties who had paid the vast majority of their Reconciliation Charges by R2, and whose future Reconciliation Charges and risk to the market would therefore be small.
- The Proposed Modification would reduce the effort required for Withdrawing Parties to process invoices for small amounts of Reconciliation Charges between R2 and RF, and to monitor the ongoing or changing legal liabilities of a contract under which their company is no longer operational. It would also remove the administrative costs to the FAA of issuing Advice Notes.
- Compared with the current arrangements, the Proposed Modification would reduce the risk of unpaid Reconciliation Charges being recouped from other Parties – since these would have been pre-paid.

The arguments put forward in support of Objective (d) were as follows:

- The Proposed Modification would reduce the effort required for BSCCo to pursue small amounts of money and manage any unintentional payment Defaults between R2 and RF – allowing it to more appropriately target resources on those Parties who are operational in the market.

## **1.5 Alternative Modification**

This section outlines the solution requirements developed by the SSMG to support the Alternative Modification. More detail regarding the Group's rationale in developing these requirements can be found in Section 1.7.

The Alternative Modification was developed by the SSMG at its final meeting after its consideration of the responses to the Assessment Procedure consultation. Although the majority of respondents did not identify an Alternative Modification which they believed to be better than the Proposed Modification, the SSMG considered the Alternative to be consistent with the intention of respondents that the P178 deposit should include elements of BSCCo Charges (see Section 6.2).

### 1.5.1 Solution overview – the 'BSCCo Charges deposit'

The Alternative Modification developed by the SSMG is the same as the Proposed Modification outlined in Section 1.2, except for the addition of two further withdrawal criteria in A5.1.3. These are that a Non-Supplier Trading Party withdrawing after R2 must also have:

- Paid the Base Monthly Charge for each calendar month commencing after its Withdrawal Date but prior to the Payment Date for the RF run for its final Settlement Day; and
- Lodged a refundable cash deposit with BSCCo to cover its estimated future share of Annual Net Main Costs in the BSC Year in which its last Settlement Day fell (hereafter referred to as the 'BSCCo Charges deposit').

More detail regarding this solution can be found in Section 1.6 below.

## 1.6 Issues raised by the Alternative Modification

The issues associated with the Alternative Modification are the same as those outlined for the Proposed Modification in Section 1.3, with the exception of the treatment of BSCCo Charges (see below).

### 1.6.1 BSCCo Charges deposit

#### a) Annual Net Main Costs deposit

##### Calculation

A majority of SSMG members agreed that each Withdrawing Party should be required to 'pre-pay' its remaining share of BSCCo's overall costs (Annual Net Main Costs) in that BSC Year, in order to reduce the risk that these costs might be unpaid after its withdrawal and recouped from remaining Parties (see Section 1.3.10 for more detail). The Proposer's Representative did not believe this risk of non-payment to be material, but agreed that pre-payment was necessary in order to deliver the full benefit to a withdrawing Non-Supplier Trading Party of avoiding the administrative burden of managing invoices after R2. The SSMG noted that this would be an entirely new process for BSCCo, since it does not currently accept advance payments of BSCCo Charges.

The SSMG considered the method by which the remaining Monthly Net Main Costs of a withdrawing Non-Supplier Trading Party should be estimated, and unanimously agreed that the simplest calculation of a Party's estimated BSCCo Charges deposit would be as follows:

*(Estimated Annual Net Main Costs \* Party's average Main Funding Share in BSC Year) – BSCCo Charges paid by the Party prior to its Withdrawal Date*

The estimated Annual Net Main Costs would be based on BSCCo's Annual Budget for that BSC Year.

The Group noted that this calculation would return a BSCCo Charges deposit amount of zero for non-physical traders (who do not have Main Funding Shares) and any Party which had not traded in the BSC Year (since its last Settlement Day would have fallen in the previous BSC Year). The Group agreed that this was appropriate, since such Parties would not be subject to any further Annual Net Main Costs. Under the Alternative Modification, non-physical traders and Parties which had not traded in the BSC Year would therefore only be required to lodge the Reconciliation Charges deposit and pay the Base Monthly Charge for months remaining until RF.

##### Administration

The SSMG agreed that at the payment due date for each remaining invoice month of the BSC Year, and at the final determination of BSCCo Charges for that BSC Year, BSCCo would either debit or credit the Party's BSCCo Charges deposit with the following:

- The difference between the amount already paid by the Party in respect of its Annual Net Main Costs for the BSC Year and the latest estimate or actual amount payable by the Party; and
- The VAT applicable to the debited/credited amount.

The SSMG noted BSCCo's advice that the VAT issues identified for the Proposed Modification in relation to the Reconciliation Charges deposit (see Section 1.3.6) would also apply to the BSCCo Charges deposit under the Alternative. The Group therefore noted that BSCCo would still be required to issue invoices to the withdrawn Party in respect of its 'pre-paid' Base Monthly Charges and Monthly Net Main Costs, in order to comply with its VAT regulations – and that this would reduce the potential administrative cost-savings of the pre-payment to BSCCo (and potentially to the withdrawn Party). However, the Proposer's Representative argued that the ability to pre-pay its future BSCCo Charges would still reduce a Withdrawing Party's administrative costs in managing invoices after R2.

The SSMG noted that BSCCo is required by the Code to undertake a final determination of BSCCo Charges for each BSC Year, and notify each Party of any resulting adjustments in its payments. The Group therefore agreed that any remaining money from the BSCCo Charges deposit should be returned to the withdrawn Party following this final determination. The Group noted BSCCo's advice that if any surplus money could not be returned to the Party (due to it having wound up its operations as a company), this money would be redistributed to all remaining Parties via their General Funding Shares on a default basis. The Group agreed with BSCCo's suggestion that the existing statement of the Party's final share of that year's charges should also serve as the final statement of the debits from/credits to its BSCCo Charges deposit.

The SSMG considered whether interest should be paid to the withdrawn Party in respect of its BSCCo Charges deposit. However, the SSMG noted BSCCo's advice that (unlike the FAA) BSCCo has no existing system in place for calculating interest in relation to BSCCo Charges, since it has no process for accepting advance payments. The Group noted that there would be costs in establishing such an interest system, and considered that these would outweigh the benefits of paying interest on the deposit. Moreover, the Group noted that – since ELEXON Limited is a 'net-nil' company (i.e. not for profit, not for loss) – any money paid in interest to a withdrawn Party would itself form part of BSCCo's overheads for that BSC Year, and would therefore be recovered from all remaining Parties. The SSMG therefore agreed that interest should not be paid to a withdrawn Party in relation to its BSCCo Charges deposit.

The SSMG agreed that if a withdrawn Party's BSCCo Charges deposit proved to be insufficient to cover its actual share of Annual Net Main Costs, the Party should be invoiced by BSCCo for the deficit amount following the final determination of charges at the end of the BSC Year. The Group noted that the withdrawn Party would remain liable for these charges under paragraph A5.3.3 of the Code, but that any non-payment would result in the money being recouped from all remaining Parties via their General Funding Shares on a default basis.

The SSMG noted that the reasons for any shortfall in a withdrawn Party's BSCCo Charges deposit would be a budget overspend by BSCCo as a result of unforeseen circumstances in that BSC Year, or unpredictable Defaults by Parties (see below). The Group also noted BSCCo's advice that a deficit in a Party's BSCCo Charges deposit could not be covered using a surplus in its Reconciliation Charges deposit and vice versa, since BSCCo and the FAA may only hold money for the purposes of BSCCo Charges and Credit Cover/Trading Charges respectively.

Those members of the SSMG who did not support the Proposed Modification due to the perceived risk of non-payment of future charges therefore also did not support the Alternative, since they believed that it still did not go far enough towards covering the 'worst-case scenario'. Similarly, the Proposer's Representative argued that this risk would be minimal, as it would not be in the interests of the Party to avoid payment.



## **b) Remaining Annual Default Costs**

The SSMG considered the process that should be followed in respect of the withdrawn Party's share of Annual Default Costs (the costs under which unpaid amounts of a Party in Default are recovered by BSCCo from all other Parties).

The SSMG agreed that it would not be possible to estimate a Party's future share of Annual Default Costs, since it was not possible to predict how many Parties would enter Default in any BSC Year. The Group therefore agreed that the withdrawn Party should be invoiced for its share of these charges following the final determination of BSCCo Charges for the BSC Year. Again, the Group noted that – whilst the Party would remain liable for these charges – any non-payment would be recouped from remaining Parties.

## **c) Base Monthly Charge payment**

It was queried whether the BSCCo Charges deposit under the Alternative Modification should seek to include any Specified BSC Charges (fixed charges reflecting elements of BSCCo's administration of the BSC arrangements). The SSMG considered that most of these would not be relevant to a Withdrawing Party (e.g. charges for BM Unit ownership), but that there could be a case for requiring a Party withdrawing earlier than RF under P178 to pay the Base Monthly Charge for those months in which it would have been required to remain a Party under the current arrangements. The Group noted that, since the Base Monthly Charge is currently set at £250, this would be a maximum of £2,750 for a Party withdrawing at R2 (11 months before RF).

The Proposer's Representative questioned whether a Party should be required to pay any Base Monthly Charges which fell after its early withdrawal, since they believed this charge to reflect BSCCo's costs in providing support to Code signatories and therefore was not appropriate for a Party which had left the Code. However, the other members of the Group argued that the Base Monthly Charge goes towards recovery of BSCCo's overall costs in a BSC Year, and that a Party withdrawing early under the Alternative Modification should be required to pay this charge for each month between its early withdrawal and RF in order to cover the costs to BSCCo of administering the BSCCo Charges deposit and P178 withdrawal process. The Proposer's Representative accepted this view, and the Group therefore unanimously agreed that the Base Monthly Charge should be included.

The SSMG agreed that if these Base Monthly Charge payments by the Withdrawing Party were intended to cover BSCCo's costs in administering the deposit, then this element should be a non-refundable charge separate to the BSCCo Charges deposit itself.

## **1.7 Assessment of whether the Alternative Modification would better facilitate the Applicable BSC Objectives**

The majority view of the SSMG is that the Alternative Modification is superior to the Proposed Modification, for the following reasons:

- The Alternative Modification would reduce the risk of non-payment of some elements of a Withdrawing Party's BSCCo Charges through the addition of a second pre-payment deposit; and
- The Alternative Modification would reduce the administrative effort required by the Withdrawing Party in managing invoices for some elements of BSCCo Charges after R2.

One member of the Group abstained on the grounds that they were unsure whether the Alternative was better than the Proposed Modification due to the increased ELEXON implementation costs it would entail.

However, the majority view of the SSMG was that the Alternative Modification would not better facilitate the achievement of the Applicable BSC Objectives *when compared with the current Code baseline*. Although these members agreed that the Alternative would have a less detrimental impact on the Applicable BSC Objectives than the Proposed Modification, they considered that it would still negatively impact Objectives (c) and (d) – since it would still retain the other disadvantages of the Proposed Modification (see below).

### **Majority view against Objectives (c) and (d)**

The arguments put forward against Objective (c) were as follows:

- It is not possible to accurately estimate a Non-Supplier Trading Party's future Reconciliation Charges between R2 and RF, or its remaining share of BSCCo Charges for the BSC Year. The SSMG has been unable to identify a more accurate methodology for the estimation of the deposits than basing them on the Withdrawing Party's historic Reconciliation Charges, historic Main Funding Shares and BSCCo's Annual Budget, which may not be reflective of the actual future level of liabilities.
- In the case of Reconciliation Charges, these can be significantly affected by any Trading Disputes entering Settlement after R2, the number and materiality of which cannot be predicted. The P178 Reconciliation Charges deposit calculation therefore contains the risk that a withdrawing Non-Supplier Trading Party's future charges could be materially underestimated. Although P178 contains a 'ratchet' mechanism for requesting an additional pre-payment in the event of any shortfall, there is the risk that the withdrawn Party either refuses or is unable to pay this increased amount – leading to it being recouped across all remaining Parties.
- A non-operational Non-Supplier Trading Party, which is planning to withdraw at RF under the current withdrawal timescales, may already simplify its exit without increasing the risks to other Parties. Under the existing route such Parties may already lodge cash with the FAA as pre-payment towards their Trading Charges, and reduce their Credit Cover to the Minimum Eligible Amount (or amount estimated to cover future Reconciliation Charges, if in insolvency or administration). The requirement to remain a Party until RF would therefore not appear to be a barrier to competition.
- In the case of BSCCo Charges, a budget overspend by BSCCo (due to unforeseen circumstances) may lead to a shortfall between the withdrawn Party's BSCCo Charges deposit and its actual liabilities. There is therefore the risk that, if the withdrawn Party refuses or is unable to pay its increased BSCCo Charges, this shortfall would be recouped from all remaining Parties.
- Moreover, the Withdrawing Party's share of Annual Default Costs could not be predicted since these would depend upon the number of Parties being placed in Default during the BSC Year. The Withdrawing Party's share of Annual Default Costs would therefore not be included in the deposit, but would be invoiced to the Party following the end of the BSC Year – reducing the administrative savings for the withdrawn Party, whilst containing the risk that these would not be paid and would be recouped across all remaining Parties.
- The Code is a multilateral contract, and the aim of the current withdrawal timescales is to protect the market against the potential 'bad debts' of any one Party. The current arrangements are applied equally to all (a 'level playing field'), and therefore do not unduly discriminate against any one class of Party. Competition would be adversely affected if Parties were able to withdraw after R2 with the potential risk that their future charges might not be paid and might be recovered from remaining Parties – since this could create benefits for Non-Suppliers at the expense of the rest of the market (a potential 'cross-subsidy').

- A potential barrier to exit is not necessarily a barrier to entering the market, since Parties sign up to the Code with the expectation that the market will prove profitable and therefore that they will be in it for the long term. Moreover, the current withdrawal timescales may be viewed as less of a barrier to entry than the potential impact of allowing some Parties' early withdrawal.
- Although the Alternative Modification reduces the risk of non-payment of some elements of BSCCo Charges, it therefore still does not provide adequate protection to remaining Parties when compared with the current arrangements.
- Despite the pre-payment deposits, a withdrawing Non-Supplier Trading Party would not be able to achieve a final financial settlement at R2 under the Alternative Modification – since it might still receive a ratchet request for the Reconciliation Charges deposit (up to RF), invoices for further DF runs or ESDs in respect of any of its Settlement Days (after RF), or invoices for any outstanding BSCCo Charges such as Annual Default Costs (following the end of the BSC Year).

The arguments put forward against Objective (d) were as follows:

- The requirement to issue VAT invoices after R2 would reduce any potential administrative cost and efficiency savings for the FAA and BSCCo. Moreover, any potential savings for the FAA and BSCCo in not having to chase Parties for charges between R2 and RF would be outweighed by the costs of implementing and operating the processes for the Reconciliation Charges and BSCCo Charges deposits.

#### **Minority view in support of Objectives (c) and (d)**

The Proposer's Representative believed that the Alternative Modification would better facilitate the achievement of Applicable BSC Objectives (c) and (d), when compared to both the Proposed Modification and the current Code baseline.

The arguments put forward in support of Objective (c) were as follows:

- As for the Proposed Modification, the Alternative Modification would remove barriers to exit by introducing a simpler and more timely withdrawal route for those Parties who had paid the vast majority of their Reconciliation Charges by R2, and whose future Reconciliation Charges and risk to the market would therefore be small.
- As for the Proposed Modification, the Alternative would reduce the effort required for Withdrawing Parties to process invoices for small amounts of Reconciliation Charges between R2 and RF, and to monitor the ongoing or changing legal liabilities of a contract under which their company is no longer operational. It would also remove the administrative costs to the FAA of issuing Advice Notes.
- As for the Proposed Modification, the Alternative would reduce the risk (compared with the current arrangements) of unpaid Reconciliation Charges being recouped from other Parties, since these would have been pre-paid.
- The Alternative Modification would also have the advantage over the Proposed Modification of reducing the administrative effort required by the Withdrawing Party to manage invoices for some elements of BSCCo Charges after R2 – thus going further towards removing barriers to a timely exit for Non-Supplier Trading Parties.

The arguments put forward in support of Objective (d) were as follows:

- Compared with the Proposed Modification, the Alternative (by including pre-payment of BSCCo Charges) would further reduce the effort required for BSCCo to pursue small amounts of

money and manage any unintentional payment Defaults between R2 and RF – allowing it to more appropriately target resources on those Parties who are operational in the market.

## 1.8 Governance and regulatory framework assessment

The SSMG noted the advice of BSCCo that, although outside the vires of the Code and therefore of the scope of P178, a Party which fully 'wound up' its operations as a company after withdrawing from the Code at R2 might be non-compliant with its wider obligations under VAT law (see Section 1.3.6).

## 2 COSTS<sup>17</sup>

This section outlines the costs for implementing and operating the solutions for the Proposed and Alternative Modifications. For more detail regarding the activities contained in these costs, please refer to Sections 4 and 5.

### 2.1 Costs of progressing P178 through the Modification Procedures

#### PROGRESSING MODIFICATION PROPOSAL

<b>Meeting Cost</b>	£1,500
<b>Legal/Expert Cost</b>	£1,000
<b>Impact Assessment Cost</b>	£5,000
<b>ELEXON Resource</b>	50 man days £9,840

<sup>17</sup> Clarification of the meanings of the cost terms in this section can be found in Annex 7 of this report.

## 2.2 Implementation costs – Proposed Modification

### IMPLEMENTATION COSTS – Proposed Modification P178

		Stand Alone Cost	P178 (Proposed) Incremental Cost	Tolerance
<b>Service Provider<sup>18</sup> Cost</b>	Change Specific Cost	£2,700	£2,700	+/- 0%
	Release Cost	£0		+/- 0%
	Incremental Release Cost	£0	£0	+/- 0%
	<b>Total Service Provider Cost</b>	<b>£2,700</b>	<b>£2,700</b>	<b>+/- 0%</b>
<b>Implementation Cost</b>	External Audit	£0	£0	+/- 0%
	Design Clarifications	£0	£0	+/- 0%
	Additional Resource Costs	£0	£0	+/- 0%
	Additional Testing and Audit Support Costs	£0		+/- 0%
<b>Total Demand Led Implementation Cost</b>	<b>£2,700</b>	<b>£2,700</b>	<b>+/- 0%</b>	

<b>ELEXON Implementation Resource Cost</b>		182 man days £40,040	102 man days £22,440	+/- 10%
<b>Total Implementation Cost</b>		<b>£42,740</b>	<b>£25,140</b>	<b>+/- 10%</b>

<sup>18</sup> BSC Agent and non-BSC Agent Service Provider and software costs.

## ONGOING SUPPORT AND MAINTENANCE COSTS – Proposed Modification P178

	Stand Alone Cost	P178 (Proposed) Incremental Cost	Tolerance
Service Provider Operation Cost	£375 per withdrawal	£375 per withdrawal	+/- 0%
Service Provider Maintenance Cost	£0	£0	+/- 0%
ELEXON Operational Cost	£440 (2 man days) per withdrawal	£440 (2 man days) per withdrawal	+/- 10%

### 2.3 Implementation costs – Alternative Modification

## IMPLEMENTATION COSTS – Alternative Modification P178

		Stand Alone Cost	P178 (Alternative) Incremental Cost	Tolerance
<b>Service Provider Cost</b>	Change Specific Cost	£2,700	£2,700	+/- 0%
	Release Cost	£0		+/- 0%
	Incremental Release Cost	£0	£0	+/- 0%
	<b>Total Service Provider Cost</b>	<b>£2,700</b>	<b>£2,700</b>	<b>+/- 0%</b>
<b>Implementation Cost</b>	External Audit	£0	£0	+/- 0%
	Design Clarifications	£0	£0	+/- 0%
	Additional Resource Costs	£0	£0	+/- 0%
	Additional Testing and Audit Support Costs	£0		+/- 0%
<b>Total Demand Led Implementation Cost</b>		<b>£2,700</b>	<b>£2,700</b>	<b>+/- 0%</b>

<b>ELEXON Implementation Resource Cost</b>		188 man days £41,360	108 man days £23,760	+/- 10%
<b>Total Implementation Cost</b>		£44,060	£26,460	+/- 10%

### ONGOING SUPPORT AND MAINTENANCE COSTS – Alternative Modification

	Stand Alone Cost	P178 (Alternative) Incremental Cost	Tolerance
Service Provider Operation Cost	£375 per withdrawal	£375 per withdrawal	+/- 0%
Service Provider Maintenance Cost	£0	£0	+/- 0%
ELEXON Operational Cost	£1,320 (6 man days) per withdrawal	£1,320 (6 man days) per withdrawal	+/- 10%

### 3 RATIONALE FOR MODIFICATION GROUP'S RECOMMENDATIONS TO THE PANEL

The majority recommendation of the SSMG is that neither the Proposed Modification nor the Alternative Modification should be made.

Although the Group unanimously agreed that the Alternative Modification would better facilitate the achievement of the Applicable BSC Objectives when compared with the Proposed Modification, the majority view of the Group is that the Alternative would not better facilitate the achievement of the Applicable BSC Objectives when compared with the current Code baseline. Moreover, the majority view of the Group is that both the Proposed and Alternative Modifications would have a negative impact on Applicable BSC Objectives (c) and (d), for the reasons set out below:

- It is not possible to accurately estimate future Reconciliation Charges or BSCCo Charges, and both the Proposed and Alternative Modifications therefore create the risk of an unpaid shortfall being recovered from remaining Parties (a potential anti-competitive 'cross-subsidy' compared with the 'level playing field' of the current arrangements); and
- Any potential cost or efficiency savings resulting from the Proposed or Alternative Modifications for BSCCo, the FAA and the withdrawn Party would be outweighed by the costs of calculating and administering the withdrawal deposit(s).

The minority view of one member of the Group was that both the Proposed and Alternative Modifications would better facilitate the achievement of Applicable BSC Objectives (c) and (d) compared with the current Code baseline, but that the Alternative would better facilitate these objectives when compared with the Proposed Modification and should therefore be made.

In the event of an Authority decision to approve either the Proposed or Alternative Modification, the SSMG unanimously recommends an Implementation Date of 29 June 2005 (if an Authority decision is received on or before 9 March 2005) or 2 November 2005 (if an Authority decision is received after 9 March 2005 but on or before 6 July 2005).

More detail regarding the recommendations of the SSMG is contained in Sections 1.2-1.7 above, whilst the rationale for the proposed Implementation Date can be found in Section 9.

## 4 IMPACT ON BSC SYSTEMS AND PARTIES

The SSMG has identified the following areas of impact which would result from implementation of the Proposed Modification and Alternative Modification.

### 4.1 BSCCo

ELEXON function	Impact of Proposed Modification	Impact of Alternative
<b>Customer Services Management</b>	<p><b>Implementation effort:</b></p> <p>Support to CVA Programme in implementation of amendments to BSCP65, attendance at walkthroughs, plus changes to local working instructions.</p> <p><b>Operational effort:</b></p> <p>Overall operational responsibility for management of P178 withdrawal process, including determination of whether each Withdrawing Party is a Non-Supplier Trading Party and requesting the calculation of its deposit amount.</p>	As for Proposed Modification.
<b>CVA Operations</b>	<p><b>Implementation effort:</b></p> <p>Input into review process for BSCCo and BSC Agent documentation changes, attendance at walkthroughs, changes to local working instructions, and introduction of a record of all Parties withdrawing after R2.</p> <p><b>Operational effort:</b></p> <p>Overall operational responsibility for management of P178 Reconciliation Charges deposit calculation and administration of deposit by the FAA.</p>	As for Proposed Modification.
<b>Market Monitoring</b>	<p><b>Implementation effort:</b></p> <p>Addition of P178 Reconciliation Charges deposit calculation to TOMAS system and documentation.</p> <p><b>Operational effort:</b></p> <p>Operational responsibility for running P178 Reconciliation Charges deposit calculation for each Withdrawing Party using TOMAS.</p>	As for Proposed Modification.



ELEXON function	Impact of Proposed Modification	Impact of Alternative
<b>Finance</b>	<p><b>Implementation effort:</b></p> <p>Minor changes to local working instructions, introduction of a spreadsheet record of all Parties withdrawing after R2 (in order to track future BSCCo Charges), and support to CVA Programme in implementation of amendments to BSCP301.</p> <p><b>Operational effort:</b></p> <p>Operational responsibility for invoicing/pursuing any BSCCo Charges accrued by a Party post-withdrawal, including allocation of any unpaid charges to remaining BSC Parties.</p>	<p><b>Implementation effort:</b></p> <p>Development of a new local working instruction detailing BSCCo's management of the BSCCo Charges deposit, introduction of new spreadsheet records relating to this deposit, support to CVA Programme in implementation of amendments to BSCP301, and attendance at walkthroughs.</p> <p><b>Operational effort:</b></p> <p>Operational responsibility for management of the BSCCo Charges deposit and Base Monthly Charge payments, invoicing the withdrawn Party for its share of Annual Default Costs following the end of the BSC Year, and allocating any unpaid charges to remaining BSC Parties.</p>
<b>CVA Programme</b>	<p><b>Implementation effort:</b></p> <p>Management of P178 implementation, including amendment of documentation, progression of Code Subsidiary Document changes through review cycle and Panel Committee approval, and undertaking walkthroughs of new P178 withdrawal process.</p> <p><b>Operational effort:</b></p> <p>None.</p>	As for Proposed Modification.
<b>Corporate Assurance</b>	<p><b>Implementation effort:</b></p> <p>Provision of implementation assurance to CVA Programme.</p> <p><b>Operational effort:</b></p> <p>None.</p>	As for Proposed Modification.

## 4.2 BSC Systems

### 4.2.1 BSC software

P178 has no impact on any BSC software, since the Reconciliation Charges deposit would be administered by the FAA using existing software functionality and a combination of new and existing manual processes. Please note that the implementation and operational effort by the CRA and FAA would be the same for both the Proposed and Alternative Modifications.

### 4.2.2 BSC Agent processes

#### a) CRA

##### Implementation effort

The following changes would be required to support the implementation of both the Proposed and Alternative Modifications:

- Addition of the dates for the R2 and R3 runs for the Withdrawing Party's last Settlement Day to the withdrawal checklist provided to BSCCo in accordance with BSCP65, in order for BSCCo to confirm that the Party is eligible to withdraw and to run the Reconciliation Charges deposit calculation using these dates (this information is currently only provided by the CRA in relation to RF); and
- Amendment to CRA local working instructions to reflect the above additional withdrawal checks.

All other information on the withdrawal checklist would remain unchanged.

No changes to CRA systems would be required to maintain the IDs of those Parties which had withdrawn at R2, in order to allocate subsequent adjustments in Settlement data, since this functionality already exists for Parties which withdraw at RF but may be subject to further DF runs or ESDs.

##### Operational effort

None.

#### b) FAA

The following changes and activities would be required to support the implementation and operation of both the Proposed and Alternative Modifications:

##### Implementation effort

- Amendment of documentation to record the FAA's management of the P178 Reconciliation Charges deposit (see Section 5).

##### Operational effort

- Increase in the daily management of prepayment funds;
- Management of the 'ratchet request' (assumed to be an infrequent occurrence);
- Increase in the processing of Default Funding Shares for either recouping a shortfall (in the event of non-payment) or redistributing a surplus (in the event that the Party no longer exists) in the withdrawn Party's Reconciliation Charges deposit;

- Additional manual task to suppress the issue of Advice Notes to a Party which withdraws after R2; and
- Production of a final statement for each Party withdrawing after R2, containing details of the debits from/credits to its Reconciliation Charges deposit.

### 4.3 Parties and Party Agents

#### 4.3.1 Parties

P178 has no direct impact upon Parties' systems, processes or documentation.

A Non-Supplier Trading Party would be able to achieve an earlier withdrawal from the Code following R2 – providing that the Party met the P178 withdrawal criteria, including lodging cash as security against its future financial liabilities. However, any Reconciliation Charges or BSCCo Charges which could not be recovered from the Party as a result of its early withdrawal would be recouped from all remaining Parties.

#### 4.3.2 Party Agents

P178 has no impact on any Party Agents.

## 5 IMPACT ON CODE AND DOCUMENTATION

### 5.1 Balancing and Settlement Code

Code Section	Impact of Proposed Modification	Impact of Alternative Modification
Section A 'Parties and Participation'	Introduction of a shortened withdrawal process for Non-Supplier Trading Parties, along with requirement to lodge Reconciliation Charges deposit and pay all BSCCo Charges accrued to date.	As for Proposed Modification, plus additional requirement to lodge BSCCo Charges deposit and pay Base Monthly Charge for each month between the Party's Withdrawal Date and the RF Payment Date for its last Settlement Day.
Section D 'BSC Cost Recovery and Participation Charges'	No impact.	Introduction of process for lodging, drawing from and returning the BSCCo Charges deposit.
Section N	Documentation of process for lodging, drawing from and returning the Reconciliation Charges deposit. Amendment to reflect suppression of Advice Notes for a Party which withdraws after R2.	As for Proposed Modification.
Annex X-1 'General Glossary'	Changes to define any new terms, such as the Reconciliation Charges deposit and ratchet.	As for Proposed Modification, plus definition of BSCCo Charges deposit.

## 5.2 Code Subsidiary Documents

Item	Impact of Proposed Modification	Impact of Alternative Modification
BSCP65 'Registration of Parties and Exit Procedures'	Introduction of a shortened withdrawal process for Non-Supplier Trading Parties (including changes to withdrawal checklist), along with requirement to lodge Reconciliation Charges deposit and pay all BSCCo Charges accrued to date.	As for Proposed Modification, plus additional requirement to lodge BSCCo Charges deposit.
BSCP301 'Clearing, Invoicing and Payment'	Documentation of process for lodging, drawing from and returning the Reconciliation Charges deposit. Amendment to reflect suppression of Advice Notes for a Party which withdraws after R2.	As for Proposed Modification.
FAA Service Description	See above.	As for Proposed Modification.

## 5.3 Impact on other configurable items

Item	Impact of Proposed Modification	Alternative Modification
FAA URS	Documentation of process for managing P178 Reconciliation Charges deposit and ratchet request.	As for Proposed Modification.
EPFAL Interface Definition and Design Part 1 <sup>19</sup>	As above.	As for Proposed Modification.

## 5.4 BSCCo Memorandum and Articles of Association

No impact.

## 5.5 Impact on Core Industry Documents and supporting arrangements

No impact.

## 6 SUMMARY OF CONSULTATION RESPONSES

7 responses (representing 42 Parties) were received to the P178 Assessment Procedure consultation. One respondent had no comment on any of the questions raised in the consultation document.

A summary of the consultation responses is provided on the following page, whilst full copies of the consultation responses are attached as Annex 3.

<sup>19</sup> EPFAL is the company which provides the FAA agent service.

Q.	Consultation question	Respondent 1 (1 Party)	Respondent 2 (5 Parties)	Respondent 3 (15 Parties)	Respondent 4 (1 Party)	Respondent 5 (10 Parties)	Respondent 6 (9 Parties)	Respondent 7 (1 Party)
1.	Do you believe that the Proposed Modification P178 would better facilitate the achievement of the Applicable BSC Objectives?	Yes	Yes (subject to use of Deposit Option 3)	No	No	No	No	No comment
2.	Do you support the solution developed by the Modification Group for the administration of the 'withdrawal deposit' by the FAA?	Yes	Yes	Yes	Yes	Yes	Yes	No comment
3.	Which of the following four options do you believe to be the most appropriate calculation for the 'withdrawal deposit'?  <b>Deposit Option 1:</b> Average Credited Energy Volume change scaled to Party; <b>Deposit Option 2:</b> Average Reconciliation Charges change scaled to Party; <b>Deposit Option 3:</b> Party-specific estimated Reconciliation Charges (P152 calculation); <b>Deposit Option 4:</b> Amount to be set by the Panel.	Option 3 or 4	Option 3	No preference expressed	None	Option 3	No preference expressed	No comment
4.	Do you believe that the calculations under Deposit Options 1 and 2 should seek to cover a) Average; or b) High than average changes?	Average	Higher than average	Other - should seek to cover 'worst case' scenario	Other – should seek to cover 'worst case' scenario	Higher than average	Higher than average	No comment
5.	Do you believe that a standard minimum deposit amount should be set for non-physical traders under Deposit Options 1 and 2?	Yes	Yes	Yes	Yes	Yes	No preference expressed	No comment

Q.	Consultation question	Respondent 1 (1 Party)	Respondent 2 (5 Parties)	Respondent 3 (15 Parties)	Respondent 4 (1 Party)	Respondent 5 (10 Parties)	Respondent 6 (9 Parties)	Respondent 7 (1 Party)
6.	Do you believe that a standard minimum deposit amount should be set under Deposit Option 3 for Parties which have not traded in the past 12 months?	No	Yes	Yes	Yes	Yes	No preference expressed	No comment
7.	Do you believe a 'ratchet' mechanism to be appropriate?  If yes, please indicate whether you believe this should be:  <b>Ratchet Option A:</b> The original amount scaled to the number of months remaining until RF;  <b>Ratchet Option B:</b> The deficit amount multiplied by the number of months remaining until RF;  <b>Ratchet Option C:</b> A set multiple of the deficit amount (e.g. 5, 10).	Yes – Option C	Yes – either Options A or B	Unsure – would prefer deposit calculation which removes need for ratchet	Yes – Option C	No – would prefer deposit calculation which removes need for ratchet	No preference expressed	No comment
8.	Do you believe there to be an Alternative Modification which, when compared with the Proposed Modification, would better facilitate the achievement of the Applicable BSC Objectives in relation to the defect identified by the Modification Proposal?	No	Yes	No	No	No	No	No comment
9.	Do you believe there to be any other issues that the Modification Group has not identified and that should be considered as part of the Assessment Procedure for P178?	Yes – appeals mechanism?	No	No	No	No	No	No comment

## **6.1 Modification Group's summary of the consultation responses**

### **6.1.1 Applicable BSC Objectives**

#### **Majority view against Objectives (c) and (d)**

A majority of respondents considered that the Proposed Modification would not better facilitate the achievement of Applicable BSC Objectives (c) and (d).

The arguments expressed by respondents against Objective (c) were that:

- The current withdrawal timescales apply equally to all, and therefore do not discriminate against any type of Party.
- The 14-month withdrawal period aims to protect other Parties due reimbursements from a Party that has ceased trading, and competition would be damaged by a reduction in this timescale. Potential Parties are more likely to accede to the Code if they have the comfort and knowledge that fellow participants are in for the longer term, and hence are more likely to settle their outstanding bills, rather than join, trade for a few weeks and then leave. Potential new entrants to the market may place less emphasis upon the exit process from the Code but more emphasis on the potential risks that they could face as part of being a signatory. The current withdrawal timescales might therefore be viewed as less of a barrier to entry than the risks posed by other Parties' early withdrawal under P178.
- Any process that attempts to estimate a Non-Supplier Trading Party's future liabilities could miscalculate those liabilities, and therefore have a detrimental impact on competition. Respondents mainly expressed concern over instances where the calculation could underestimate actual liabilities, with the potential result that remaining Parties could be exposed to a 'bad debt'. Whilst this might be an infrequent occurrence, the impact of the Emergency Instruction on 19 May 2004 represents an example of what could happen to significantly change a Party's liabilities in the later part of the Reconciliation timetable.
- The existing informal process by which Parties may lodge cash with the FAA as pre-payment towards their Trading Charges already offers a route by which a Party which expects to withdraw at RF may simplify its exit without increasing the risk to other Parties. This existing ability is therefore more appropriate than early withdrawal under P178.
- If it was possible to know exactly the amount of Parties' future charges, then these would be settled earlier and later Settlement Runs would not be required.
- If anything, there is an argument for extending, rather than shortening, the current withdrawal timescale – since all Settlement Days since Go-Live have had a further DF run, and in some cases an ESD.

The arguments expressed by respondents against Objective (d) were that:

- The proposed deposit mechanisms would result in more work and increased costs for BSCCo and the FAA when compared against the current arrangements, and would therefore be detrimental to efficiency.
- The achievement of the main potential benefit of P178 – that Parties would be able to wind up their company in a more efficient manner – would be prevented by the need for a Party to remain a legal entity after R2 in order to comply with VAT law.

### **Minority view against Objective (c) but in support of Objective (d)**

Two respondents who did not support the Proposed Modification due to a perceived detrimental impact on Applicable BSC Objective (c), considered that it might better facilitate the achievement of Applicable BSC Objective (d). However, they considered that this positive impact would be minimal, since any efficiency gains would largely be offset by the costs of administering the withdrawal deposit.

### **Minority view in support of Objectives (c) and (d)**

A minority of respondents did consider that the Proposed Modification would better facilitate the achievement of both Applicable BSC Objectives (c) and (d). The argument expressed by these respondents was that Parties who are no longer active in the market should be able to exit the Code in a timely manner, since this would improve competition and enable more efficient administration of the Code. One respondent qualified its support for the Proposed Modification as being subject to the use of the Deposit Option 3 (P152) calculation.

## **6.1.2 Reconciliation Charges deposit**

### **a) Administration**

All respondents agreed with the solution developed by the SSMG for the administration of the Reconciliation Charges deposit by the FAA. One respondent considered that, since the FAA already has an informal process for dealing with pre-payment of Trading Charges, the formalisation of such a process for the P178 deposit would be relatively low cost.

### **b) Calculation**

Three respondents believed that the Party-specific, P152-based calculation (Deposit Option 3) would be the most appropriate calculation to use under P178. One of these respondents considered that Deposit Option 4 based on the Option 3 calculation would also be acceptable, since this would allow the flexibility to fine-tune the calculation in light of operational experience.

Arguments expressed by respondents in support of Deposit Option 3 were that:

- It would give the best estimate of a Party's actual indebtedness over the period to be considered (the time from withdrawal to RF), making it less likely that the ratchet mechanism would need to be utilised; and
- It would be clearly linked to the individual Withdrawing Party's historic data rather than an overall average of other Parties' data, and therefore would appear to offer a more accurate calculation – giving greater protection to remaining Parties against the risk of underestimation.

Arguments put forward against Deposit Options 1, 2 and 4 were that:

- Option 1 would be unsuitable as it is linked to CAP which may not fully reflect the funds involved, potentially leaving the market exposed to paying any shortfall between the deposit level and the eventual outturn;
- Option 2 would be unsuitable as it is linked to the withdrawing 'Party's GC at its last day of trading', which may be open to abuse by the withdrawing Party which might seek to reduce its GC and thus its exposure to the deposit;
- Both Options 1 & 2 would lead to security levels that either over- or under-represent the Party's actual liabilities;
- The use of averages in Options 1 and 2 would create a risk of underestimation that would lead to the use of a 'ratchet' process to recover any shortfall;



- Option 4 would be too arbitrary and would not provide enough structure to consistently estimate the level of 'withdrawal deposit' for Parties wishing to leave; and
- Option 4 is not specifically linked to any historical behaviour, and thus potentially leaves the market exposed to paying any shortfall between the deposit level and the eventual outturn.

Three respondents did not express a specific opinion as to which deposit option was preferable. One of these respondents was happy to support the option chosen by the Group and considered all options to be arbitrary, as they believed that if it was possible to know the amount of future charges these would be settled earlier in the reconciliation timetable - hence their lack of support for P178.

One respondent stated that whichever deposit option was chosen it should be set to cover the 'worst-case scenario'. This respondent argued that an insufficient deposit could only result in one of two outcomes: the utilisation of an inefficient and complex ratchet process, or the cross-subsidy created by recouping the amount from remaining Parties.

One respondent had concerns with all the options that had been developed, since it believed all had the potential to be non-reflective of a Party's future trading charges. This respondent considered that all four options would produce an arbitrary number, which might overestimate or underestimate the future liability. The respondent argued that Options 1 and 2 would be based on an average, and therefore might well produce an underestimate – whilst a Party's historic charges (Option 3) would not necessarily be representative of their future liabilities.

### **c) Whether Deposit Options 1 and 2 should cover average or higher-than-average liabilities**

A majority of respondents considered that Options 1 and 2 should seek to cover higher-than-average changes.

The arguments expressed in support of this view were that:

- An insufficient deposit could only result in one of two outcomes; the utilisation of an inefficient and complex ratchet process, or the cross-subsidy created by recouping the amount from remaining Parties; and
- Both Deposit Options 1 and 2 would not be specifically linked to the withdrawing Party's historical behaviour, and therefore would potentially leave the market exposed to paying any shortfall between the deposit level and the eventual outturn. A higher, rather than an average, figure would be more likely to ensure that the exposure of the market was reduced.

One respondent considered that the calculation under Options 1 and 2 should seek to cover average debts. This respondent argued that the Code should not impose onerous penalties on Parties who wish to pay their bills and withdraw.

Two respondents stated that whichever deposit option was chosen it should seek to cover the 'worst-case scenario', in order to protect remaining Parties from being exposed to a bad debt. However, these respondents considered that it would be impossible to accurately estimate a Party's future Reconciliation Charges and therefore to have assurance of protection against the worst-case charges. For this reason, these respondents did not support P178.

### **d) Whether Options 1 and 2 should have a standard minimum deposit**

A majority of respondents considered that a standard minimum deposit amount should be set for non-physical traders under Options 1 and 2, whilst one respondent did not express a preference.

The arguments expressed by these respondents were that:

- The minimum amount would be needed to cover the future Reconciliation Charges of such Parties; and
- Since the modification seeks to help Parties to withdraw leaving no debts, it would be equitable to require some form of security from all Withdrawing Parties.

One respondent suggested that any standard minimum deposit amount should be directly linked to the Withdrawing Party's historical behaviour (based on the Option 3 approach) and should err on the side of caution by being set at a higher level than that directly achieved by the Option 3 calculation - i.e. the Option 3 figure plus 'X%'. The respondent argued that the 'X%' should be set by the Panel, who could take advice from BSCCo based on what the maximum % shortfall would have been if P178 (Deposit Option 3) had been in effect when past Parties had withdrawn from the BSC.

One respondent did not express a preference, stating that they were happy to support whichever approach was chosen by the Modification Group.

#### **e) Whether Deposit Option 3 should have a standard minimum deposit amount**

A majority of respondents considered that a standard minimum deposit amount should be set under Deposit Option 3 for Parties which had not traded in the past 12 months, in order to cover their estimated future charges.

However, one respondent did not consider that a standard minimum deposit amount should be set under Deposit Option 3 for Parties which have not traded over the past 12 months, since the respondent believed that if the Party had not traded for that amount of time the chances of them owing any significant money would be extremely small. The respondent considered that it would be inefficient for the Code to administer a tiny deposit in order to retrieve a minimal amount of money, since the administrative costs would be likely to significantly outweigh the benefits and these would be costs that other Parties would ultimately pay.

One respondent suggested that the need for a minimum deposit would be avoided if the Deposit Option 3 calculation was based on the Party's last 12 months of trading rather than the 12 months prior to its withdrawal. This approach was subsequently adopted by the SSMG.

One respondent did not express a preference, stating that they were happy to support whichever approach was chosen by the Modification Group.

#### **f) Ratchet calculation**

A majority of respondents supported the introduction of a ratchet mechanism for the following reasons:

- It provides some additional assurance and protection to the remaining Parties against the risk of unpaid liabilities;
- It should ensure that the Withdrawing Party pays all its bills in a timely manner; and
- If it were not in place then the shortfall could grow and, if unpaid, would amount to a cross-subsidy since the amount would be recouped from remaining Parties.

Two respondents stated their preference for Ratchet Option C (a set multiple of the deficit amount). These respondents considered that the ratchet amount (like the original withdrawal deposit) would be an arbitrary number, and this option would therefore be equally as valuable as the others whilst offering the additional benefit of simplicity.

One respondent believed that either Option A or Option B might be suitable (subject to clarification on the details). It believed that Option C would be unsuitable as it would be an arbitrary amount and therefore less reflective of the likely shortfall going forward.

Two respondents expressed a preference for a calculation for the original deposit amount which would remove the need for a ratchet mechanism altogether, by covering the 'worst-case scenario' at the outset. These respondents considered that the task of having to chase a withdrawn Party for additional unforeseen charges would pose a considerable risk to remaining Parties who would have to pick up any unpaid costs.

One of these respondents also outlined what they considered to be the following issues with the ratchet mechanism:

- There was no reason to suggest that a Withdrawing Party would be willing to pay an additional ratchet request once it had left the Code;
- The ratchet mechanism would further complicate the arrangements, which seems counterintuitive for a modification seeking to improve efficiency.

The other respondent commented that it cannot be guaranteed that disputes such as Damhead Creek will be one-off/rare events that the larger Parties in the market are capable of withstanding. This respondent considered that whatever arrangements were put in place for the P178 withdrawal deposit must be robust enough to cope with any future disputes, and to provide all Parties with enough assurance that they will not have to pick up any costs as a result of allowing another Party to withdraw from the Code early.

One respondent did not express a preference, stating that they were happy to support whichever approach was chosen by the Modification Group.

### **6.1.3 Alternative Modification**

A majority of respondents did not believe there to be an Alternative Modification which, when compared with the Proposed Modification, would better facilitate the Applicable BSC Objectives in relation to the defect identified by the Modification Proposal.

One respondent did not believe that any Alternative could be developed that was better than the current Code baseline. Another respondent did not believe there to be any Alternative which could accurately estimate a Parties' future charges, since if it was possible to do so these would be settled earlier in the reconciliation timetable and later Settlement Runs would not be required.

One respondent did suggest an Alternative Modification, whereby the Deposit Option 3 calculation would be based on the Withdrawing Party's last 12 months of trading. This respondent accepted BSCCo's clarification that this variation could be progressed under the Proposed Modification, and this calculation was subsequently adopted by the SSMG as the solution for the Reconciliation Charges deposit calculation.

### **6.1.4 Additional comments**

One respondent made an additional comment that if Options 1 or 2 were used to calculate the Reconciliation Charges deposit it might be worth considering an appeals mechanism. For example, if the calculation covered higher-than-average liabilities – leaving a Party with a deposit that was significantly greater than it would reasonably expect to pay – the Party would be able to appeal the deposit amount to the Panel.

## **6.2 Comments and views of the Modification Group**

The SSMG noted the views expressed by the respondents to the Assessment Procedure consultation, which largely mirrored the discussions of the Group as outlined in Sections 1.3 and 1.4.

The SSMG unanimously agreed to adopt Deposit Option 3 and Ratchet Option C as the final calculation for the P178 Reconciliation Charges deposit, and that Panel involvement in the deposit calculation would not be desirable. The Group also unanimously agreed with the suggestion of one respondent that the Deposit Option 3 calculation be based on the Party's last 12 months of trading, so that a minimum deposit amount was not required.

At its final meeting for P178 the SSMG noted that an Alternative Modification had not been identified by respondents, but that many of the responses had referenced the inclusion of elements of the Withdrawing Party's BSCCo Charges in its withdrawal deposit. The Group therefore asked BSCCo to clarify whether BSCCo Charges could be incorporated as part of the Proposed Modification. BSCCo clarified that this would require an Alternative Modification (see Section 1.3.10), and the SSMG therefore agreed to progress such an Alternative – as a majority of members believed that this would potentially be superior to the Proposed Modification, and would be consistent with the intent of the consultation responses. Details of the Alternative Modification can be found in Sections 1.5-1.7.

## **7 SUMMARY OF TRANSMISSION COMPANY ANALYSIS**

### **7.1 Analysis**

The Transmission Company did not believe P178 would have any impact on its ability to discharge its responsibilities under the Transmission Licence, its systems or processes, or any Core Industry Document.

The Transmission Company expressed its view that further Modification Group consideration of the potential risks and benefits was required before concluding whether P178 would better facilitate the achievement of the Applicable BSC Objectives. This further consideration was undertaken by the SSMG at its final meeting.

A copy of the Transmission Company's analysis and impact assessment is contained in Annex 4.

### **7.2 Comments and views of the Modification Group**

The SSMG noted the analysis provided by the Transmission Company.

## **8 SUMMARY OF EXTERNAL ADVICE**

None was commissioned. However, BSCCo has sought informal advice from ELEXON's tax advisor regarding the potential VAT implications of the P178 deposit for a withdrawn Party – although these lie outside the vires of the Code (see Section 1.3.10).

## **9 IMPLEMENTATION APPROACH**

The SSMG noted the implementation costs for the Proposed and Alternative Modifications as outlined in Section 2. The Group noted that, as a documentation-only change, the BSC Agent costs for P178 would be the same whether the modification was implemented as part of scheduled release or as a stand-alone project. However, the Group noted that the ELEXON resource effort would differ, and therefore unanimously agreed that P178 should be implemented with other changes as part of an existing scheduled release, in order to incur only 'incremental' rather than 'stand-alone' costs.

The SSMG noted that the implementation lead time would be the same for the Proposed and Alternative Modifications, and noted BSCCo's advice that the first available release to deliver P178 would be June 2005. The Group therefore unanimously agreed the following proposed Implementation Dates for both the Proposed and Alternative Modifications:

- 29 June 2005, if an Authority decision is received on or before 9 March 2005; or
- 2 November 2005 if the Authority decision is received after 9 March 2005 but on or before 6 July 2005.

The SSMG noted that, since all withdrawal criteria must be met 2 Business Days prior to a Party's Withdrawal Date, the earliest Withdrawal Date for a Non-Supplier Trading Party which met all P178 criteria would be 2 Business Days following the Implementation Date.

Two members of the SSMG expressed disappointment in the level of costs quoted for the implementation and operation of the Proposed Modification, since these members considered the activities involved to be existing processes (for example, the FAA already administers 'pre-payments' for Trading Charges, whilst BSCCo already manages the withdrawal process and P152 calculation). BSCCo clarified that the Proposed Modification would be an extension of these existing functions, and would therefore require the documentation and operation of additional processes as outlined in Sections 4 and 5 (for example, an addition in the daily management of prepayment funds by the FAA, additional withdrawal criteria checks by BSCCo, and additional effort by BSCCo in calculating the withdrawal deposit). In respect of the Alternative Modification, the SSMG noted that the increased costs reflected the additional ELEXON effort required to manage the BSCCo Charges deposit. The Group noted that this would be an entirely new process, since there is no existing process for advance payment of BSCCo Charges.

## 10 DOCUMENT CONTROL

### 10.1 Authorities

Version	Date	Author	Reviewer	Change Reference
0.1	29/11/04	Kathryn Coffin	Dena Harris	For peer review
0.1	29/11/04	Kathryn Coffin	SSMG	For SSMG review
0.2	01/12/04	Kathryn Coffin	Sarah Parsons	For technical review
0.3	02/12/04	Kathryn Coffin	Change Delivery	For quality review
1.0	03/12/04	SSMG	BSC Panel	For Panel decision
2.0	13/12/04	Kathryn Coffin		Reissued to clarify BSCCo Charges

### 10.2 References

Ref	Document	Owner	Date	Version
1	Panel Paper 84/001(g): 'Issue 12 – Timescales for withdrawal from the BSC' <a href="#">ELEXON - BSC Panel Paper Meeting number 084 - 14/10/04</a>	BSCCo	08/10/04	1.0
2	Initial Written Assessment for Modification Proposal P178 'Reduction in the BSC withdrawal timescale for Parties who have settled the vast majority of their trading debts' <a href="#">ELEXON - Modification Proposal 178</a>	BSCCo	08/10/04	1.0
3	Assessment Consultation for Modification Proposal P178 'Reduction in the BSC withdrawal timescale for Parties who have settled the vast majority of their trading debts' <a href="#">ELEXON - Modification Proposal 178</a>	BSCCo	15/11/04	1.0
4	Requirements Specification for Modification Proposal P178 'Reduction in the BSC withdrawal timescales for Parties who have settled the vast majority of their trading debts'	BSCCo	12/11/04	1.0

Ref	Document	Owner	Date	Version
	<a href="#">ELEXON - Modification Proposal 178</a>			

## ANNEX 1 DRAFT LEGAL TEXT

Draft legal text for the Proposed and Alternative Modification has been issued to the SSMG for review, and will be provided to the Panel prior to its meeting on 9 December 2004.

## ANNEX 2 MODIFICATION GROUP DETAILS

Member	Organisation	26/10/04	24/11/04
Roger Salomone	ELEXON (Chair)	✓	
Dena Harris	ELEXON (Chair)		✓
Kathryn Coffin	ELEXON (Lead Analyst)	✓	✓
Lisa Waters	Waters Wye Associates (Proposer's Representative)	✓	✓
Helen Bray	EDF	✓	
Garth Graham	Scottish and Southern Energy		✓
Mark Manley	British Gas Trading	✓	✓
Neil Smith	EON	✓	✓
Louisa Stuart-Smith	Npower	✓	✓

Attendee	Organisation	26/10/04	24/11/04
Steve Mackay	Ofgem	✓	✓
Ben Willis	Npower	✓	
Tom Woods	FAA	✓	
Melanie Henry	ELEXON (Lawyer)		✓
Mike Bishop	ELEXON (technical support)	✓	
Anh Chu	ELEXON (technical support)		✓
Charlotte Hutchinson	ELEXON (technical support)	✓	✓

### P178 Modification Group Terms of Reference

Modification Proposal P178 will be considered by the Settlement Standing Modification Group in accordance with the following Terms of Reference.

P178 – Reduction in the BSC withdrawal timescale for Parties who have settled the vast majority of their trading debts

### ASSESSMENT PROCEDURE

The Modification Group will carry out an Assessment Procedure in respect of Modification Proposal P178 pursuant to section F2.6 of the Balancing and Settlement Code.

The Modification Group will produce an Assessment Report for consideration at the BSC Panel Meeting on 9 December 2004.

The Modification Group shall consider and/or include in the Assessment Report as appropriate:

- **Eligibility for withdrawal after R2** – whether it is appropriate for the shortened withdrawal process proposed by P178 to be made available to all Non-Supplier Trading Parties (as defined in M2.3A.7), or if any alternative/additional criteria should be developed.
- **Timing of withdrawal** – whether the point of withdrawal at R2 should be following the completion of the run or its corresponding Payment Date, and whether a Party which does not withdraw at R2 should be able to subsequently withdraw at another point prior to RF (consideration to include the timing of such withdrawal and any additional BSC Agent costs which could result from this ability).
- **Calculation of withdrawal deposit** – consideration of the four potential options outlined in the Modification Proposal, and which of these would adequately provide for a Non-Supplier Trading Party's Reconciliation Charges between R2 and RF (or alternatively, consideration of any potential Alternative Modification). Also, consideration of the following areas:
  - Whether the deposit amount should seek to cover 'average' or 'worst case' costs;
  - Whether the responsibility for calculating the deposit should lie with BSCCo, the Panel or the FAA, and (if the FAA) whether this calculation should be automatic or manual;
  - Whether the deposit amount/calculation should be 'hard-wired' in the Code; and
  - The process, frequency and responsibility for reviewing the deposit amount/calculation.
- **Administration of withdrawal deposit** – development of the FAA system and/or documentation requirements for administration of the withdrawal deposit (including financial factors such as VAT, interest and auditability), consideration of any issues arising from the suppression of Advice Notes or Confirmation Notices, and how any BSCCo costs incurred by a Party following its withdrawal at R2 would be recouped.
- **'Ratchet' process** – whether the 'ratchet' mechanism suggested by the Modification Proposal would be appropriate, whether the responsibility for exercising the mechanism would lie with BSCCo, the Panel or the FAA, and whether the original deposit calculation should be revised for all Parties as a result of a ratchet being employed for an individual Party.
- **Risk of non-payment of 'ratchet' amount by withdrawn Party** – consideration of the potential risk of non-payment of a 'ratchet' request by a Party which has withdrawn at R2.
- **Eligibility of Parties in insolvency/administration** – whether the risk of non-payment of a 'ratchet' request would be increased in the case of Parties who are insolvent or in administration, since the amount of money recovered by BSCCo (who would rank with the Party's other creditors) would be determined by the administrators in such circumstances.
- **Risk of Trading Disputes entering Settlement after R2** – the extent of the risk that could arise if a Dispute with a significant impact upon all Parties (e.g. via RCRC) enters Settlement after R2 and is not covered by the deposit left by a Withdrawing Party (e.g. the Damhead Creek incident, which will enter Settlement at R3).
- **BSC Agent impact assessments** – consideration of impacts on the FAA (administration of withdrawal deposit) and the CRA (requirement to maintain Party IDs, and impact on completion of withdrawal checklists).

- **Background of previous Modifications P127, P132 and P152** – consideration of any issues relevant to P178 which were previously discussed in the context of these Modification Proposals.
- **Additional points raised by the BSC Panel on 14 October 2004**
  - The Panel Chairman requested that the Modification Group seek to develop the least-cost solution, in order to avoid implementation/operational costs which are disproportionate to the actual Reconciliation Charges concerned.

### **ANNEX 3 ASSESSMENT CONSULTATION RESPONSES**

Attached as separate document Annex 3A.



## ANNEX 4 TRANSMISSION COMPANY ANALYSIS

Q	Question	Response
1	Please outline any impact of the Proposed Modification (and, if applicable, any Alternative Modification) on the ability of the Transmission Company to discharge its obligations efficiently under the Transmission Licence and on its ability to operate an efficient, economical and co-ordinated transmission system.	The Proposed Modification has no impact the ability of the Transmission Company to discharge its obligations under the Transmission Licence.
2	Please outline the views and rationale of the Transmission Company as to whether the Proposed Modification (and, if applicable, any Alternative Modification) would better facilitate achievement of the Applicable BSC Objectives.	We believe that at this stage of the assessment process it is not possible to conclude whether the Proposal meets the applicable objectives and that as the Mod Group has identified there is a need for further consideration of the benefits of the proposal against the potential risks.
3	Please outline the impact of the Proposed Modification (and, if applicable, any Alternative Modification) on the computer systems and processes of the Transmission Company, including details of any changes to such systems and processes that would be required as a result of the implementation of the Proposed Modification (and, if applicable, any Alternative Modification).	None identified.
4	Please outline any potential issues relating to the security of supply arising from the Proposed Modification (and, if applicable, any Alternative Modification).	None identified.
5	Please provide an estimate of the development, capital and operating costs (broken down in reasonable detail) which the Transmission Company anticipates that it would incur in, and as a result of, implementing the Proposed Modification (and, if applicable, any Alternative Modification).	None identified.
6	Please provide details of any consequential changes to Core Industry Documents and/or the System Operator Transmission Owner Code that would be required as a result of the implementation of the Proposed Modification (and, if applicable, any Alternative Modification).	None identified.
7	Any other comments on the Proposed Modification (and Alternative Modification if applicable).	None

**ANNEX 5 BSC AGENT IMPACT ASSESSMENT**

<b>NETA Change Form</b>		
<b>Title</b>		<b>Version No.</b>
Reduction in the BSC withdrawal timetable for Parties who have settled the vast majority of their trading debts		0.1
		<b>LogicaCMG Reference</b>
		ICR629
<b>ELEXON Reference</b>	<b>Date CP Received</b>	<b>Date IA Issued</b>
P178	15 Nov 2004	22 Nov 2004
<b>LogicaCMG Contact Name</b>	<b>Baseline for Impact Assessment</b>	
Neil Riddleston	P178 Requirement Specification v1.0, dated 12 Nov 2004	
<b>Price Breakdown</b>		
<b>Item description</b>	<b>Remarks</b>	<b>Price (ex VAT)</b>
Change Specific		£2,700
Incremental Release Costs		£0
Fixed Release Costs		£0
<b>Total Price (ex VAT)</b>		<b>£2,700</b>
<b>Price Tolerance</b>		0%
<b>Justification for Price Tolerance</b>		
N/A		
<b>Project Duration</b>		4 weeks
<b>Cut Off Date for Inclusion in Specified Release (if applicable)</b>		
N/A		
<b>Operational Price (ex VAT)</b>		£375 per event
<b>Rationale</b>		

Additional FAA operational tasks: 0.5 days per withdrawal event at Team Leader grade.

<b>Annual Maintenance Price (ex VAT)</b>	£0
<b>Rationale</b>	
The Annual Maintenance Price is zero under the agreement commencing on 1 January 2005.	

<b>Validity Constraints</b>	
<ul style="list-style-type: none"> <li>• Price and duration assume that this change is developed in isolation and the effects of other changes are excluded.</li> <li>• No allowance is included for the final solution being different from the baseline.</li> <li>• No allowance is included for supporting Release Audit activities. Any effort will be charged at contracted T&amp;M rates</li> <li>• No allowance is included for supporting ELEXON assurance activities. Any effort will be charged at contracted T&amp;M rates</li> <li>• No allowance is included for End to End/Participant Testing activities. Any effort will be charged at contracted T&amp;M rates</li> <li>• No allowance is included for Walkthrough activities. Any effort will be charged at contracted T&amp;M rates</li> <li>• No allowance is included to support ELEXON in parallel run testing activities</li> </ul> <p>The validity period for this quote is 30 days and the offer is based on the following payment schedule:</p> <ul style="list-style-type: none"> <li>• LogicaCMG will invoice in full for this change on deployment or within one month of the change being ready for deployment</li> </ul>	
<b>Authorised Signature</b>	<b>Date Signed</b>

<b>Requirements and Solution</b>
<b>Brief Summary of Change</b>
<p>Currently, a non-Supplier Trading Party cannot withdraw from the BSC until the Final Reconciliation (RF) Settlement Run has occurred for the last day of trading for the Party (this is approximately 14 months later).</p> <p>The changes would allow a non-Supplier Trading Party to withdraw from the BSC any time after the Second Reconciliation (R2) Settlement Run has occurred for the last day of trading for the Party (this is approximately 3 months later).</p>
<b>LogicaCMG's Proposed Solution</b>
<p>Manual procedure changes are required to the CRA and the FAA and are described below. There are no software changes required.</p> <p><u>CRA</u></p> <p>The 'Withdrawal Checklist' that is produced by the CRA and sent to BSCCo will have the R2 and R3 (Third Reconciliation) Settlement Run dates added as extra fields. LWI will be updated to reflect this change. All other information on the 'Withdrawal Checklist' will remain unchanged and the method by which all other information on the 'Withdrawal Checklist' is determined will remain unchanged.</p>

<p><u>FAA</u> The EPFAL IDD, FAA URS and EPFAL Credit and Billing Procedures will be updated to document the additional operational tasks described in the 'Operational Solution and Impact' section.</p>					
<p><b>Deviation from ELEXON's Solution / Requirements</b></p>					
<p>None</p>					
<p><b>Operational Solution and Impact</b></p>					
<p><u>CRA</u> None</p>					
<p><u>FAA</u> The following additional operational tasks are involved:</p> <ol style="list-style-type: none"> <li>1. Increase in the daily management of prepayment funds. The FAA currently manages approximately 30 prepayments for Parties under an informal arrangement for which the FAA do not charge.</li> <li>2. Management of the 'ratchet' request. This is expected to be an infrequent occurrence. There is no material difference in the effort required between Ratchet Option A, B or C.</li> <li>3. Increase in the processing of Default Funding Shares for either recouping money from Parties or redistributing money to Parties if the withdrawn Party no longer legally exists.</li> <li>4. Additional manual task to stop the sending of Advice Notes to the withdrawn Party.</li> <li>5. Production of a Final Statement to be issued to the withdrawn Party with details of credits/debits from their prepayments. It is assumed that any interest due to the withdrawn Party will only be paid at the time of the Final Statement.</li> </ol>					
<p><b>Testing Strategy</b></p>					
Unit		Change Specific		End to End	
Module		Operational Acceptance		Participant Testing	
System		Performance		Parallel Running	
Regression		Volume		Deployment/ Backout	
<p>Other:</p>					
<p><b>Validated Assumptions</b></p>					
<ol style="list-style-type: none"> <li>1. <i>BSCCo will determine whether a Party is a Non-Supplier Trading Party and therefore eligible to withdraw early.</i></li> <li>2. <i>BSCCo will instruct the withdrawing Party to cancel their receipt of Settlement Reports, so that they will not receive Settlement Reports after their last day of trading.</i></li> </ol>					
<p><b>Outstanding Issues</b></p>					
<p>What procedure does BSCCo follow, if the withdrawing Party does not cancel their receipt of Settlement Reports as instructed?</p>					
<p><b>Changes to Service</b></p>					
<p><b>Services Impacted</b></p>					

	BMRA	CDCA	CRA	ECVAA	SAA	TAA	FAA
Software							
IDD Part 1 (Docs)							X
IDD Part 1 (S'Sheet)							
IDD Part 2 (Docs)							
IDD Part 2 (S'Sheet)							
URS							X
SS							
DS							
MSS							
OSM							
LWIs			X				X
RTP	None						
Comms	None						
Other	None						
<b>Nature of Documentation Changes</b>							
See 'LogicaCMG's Proposed Solution' section.							
<b>Nature / Size of System Changes</b>							
Documentation only							
<b>Deployment Issues, e.g. Outage Requirements:</b>				None			
<b>Impact on Service Levels:</b>				None			
<b>Impact on System Performance:</b>				None			
<b>Responsibilities of ELEXON</b>							
Within reasonable levels, ELEXON will make available appropriate staff to assist LogicaCMG during the development of this change.							
<b>Acceptance Criteria</b>							
Documentation only change.							
<b>Any Other Information</b>							
None.							
<b>Attachments</b>							

## ANNEX 6 CLARIFICATION OF COSTS

There are several different types of costs relating to the implementation of Modification Proposals. ELEXON implements the majority of Approved Modifications under its CVA or SVA Release Programmes. These Programmes incur a base overhead which is broadly stable whatever the content of the release. On top of this each Approved Modification incurs an incremental implementation cost. The table of estimated costs of implementing the Proposed/Alternative Modification given in Section 2 of this report has three columns:

- **Stand Alone Cost** – the cost of delivering the Modification as a stand alone project outside of a CVA or SVA release, or the cost of a CVA or SVA release with no other changes included in the release scope. This is the estimated maximum cost that could be attributed to any one Modification’s implementation.
- **Incremental Cost** - the cost of adding that Modification Proposal to the scope of an existing release. This cost would also represent the potential saving if the Modification Proposal was removed from the scope of a release before development had started.
- **Tolerance** – the predicted limits of how certain the cost estimates included in the template are. The tolerance will be dependent on the complexity and certainty of the solution and the time allowed for the provision of an impact assessment by the Service Provider(s).

The cost breakdowns are shown below:

PROGRESSING MODIFICATION PROPOSAL	
<b>Meeting Cost</b>	This is the cost associated with holding Modification Group meetings and is based on an estimate of the travel expenses claimed by Modification Group members.
<b>Legal/Expert Cost</b>	This is the cost associated with obtaining external expert advice, usually legal advice.
<b>Impact Assessment Cost</b>	Service Provider Impact Assessments are covered by a pre-determined monthly contractual charge. Therefore the cost included in this report is an estimate based on the level of impact assessment that the modification is expected to require and may not reflect the actual cost attributed to the modification, which will be based on a percentage of the contractual impact assessment costs for each month that it is assessed.
<b>ELEXON Resource</b>	This is the ELEXON Resource requirement to progress the Modification Proposal through the Modification Procedures. This is estimated using a standard formula based on the length of the Modification Procedures.

<b>SERVICE PROVIDER<sup>20</sup> COSTS</b>	
<b>Change Specific Cost</b>	Cost of the Service Provider(s) Systems development and other activities relating specifically to the Modification Proposal.
<b>Release Cost</b>	Fixed cost associated with the development of the Service Provider(s) Systems as part of a release. This cost encompasses all the activities that would be undertaken regardless of the number or complexity of changes in the scope of a release. These activities include Project Management, the production of testing and deployment specifications and reports and various other standard release activities.
<b>Incremental Release Cost</b>	Additional costs on top of base Release Costs for delivering the specific Modification Proposal. For instance, the production of a Test Strategy and Test Report requires a certain amount of effort regardless of the number of changes to be tested, but the addition of a specific Modification Proposal may increase the scope of the Test Strategy and Test Report and hence incur additional costs.

<b>IMPLEMENTATION COSTS</b>	
<b>External Audit</b>	Allowance for the cost of external audit of the delivery of the release. For CVA BSC Systems Releases this is typically estimated as 5% of the total Service Provider Costs, with a tolerance of +/- 20%. At present the SVA Programme does not use an external auditor, so there is no External Audit cost associated with an SVA BSC Systems Release.
<b>Design Clarifications</b>	Allowance to cover the potential cost of making any amendments to the proposed solution to clarify any ambiguities identified during implementation. This is typically estimated as 2.5% of the total Service Provider Costs, with a tolerance of +/- 100%.
<b>Additional Resource Costs</b>	<p>Any short-term resource requirements in addition to the ELEXON resource available. For CVA BSC Systems releases, this is typically only necessary if the proposed solution for a Modification Proposal would require more extensive testing than normal, procurements or 'in-house' development.</p> <p>For SVA BSC Systems releases, this will include the management and operation of the Acceptance Testing and the associated testing environment.</p> <p>This cost relates solely to the short-term employment of contract staff to assist in the implementation of the release.</p>
<b>Additional Testing and Audit Support Costs</b>	Allowance for external assistance from the Service Provider(s) with testing, test environment and audit activities. Includes such activities as the creation of test environments and the operation of the Participant Test Service (PTS). For CVA BSC Systems releases, this is typically estimated as £40k per release with at tolerance of +/-25%. For SVA BSC Systems releases this is estimated on a Modification Proposal basis.

<sup>20</sup> A Service Provider can be a BSC Agent or a non-BSC Agent, which provides a service or software as part of the BSC and BSC Agent Systems. The Service Provider cost will be the sum of the costs for all Service Providers who are impacted by the release.

### TOTAL DEMAND LED IMPLEMENTATION COSTS

This is calculated as the sum of the total Service Provider(s) Cost and the total Implementation Cost. The tolerance associated with the Total Demand Led Implementation Cost is calculated as the weighted average of the individual Service Provider(s) Costs and Implementation Costs tolerances. This tolerance will be rounded to the nearest 5%.

### ELEXON IMPLEMENTATION RESOURCE COSTS

Cost quoted in man days multiplied by project average daily rate, which represents the resources utilised by ELEXON in supporting the implementation of the release. This cost is typically funded from the "ELEXON Operational" budget using existing staff, but there may be instances where the total resources required to deliver a release exceeds the level of available ELEXON resources, in which case additional Demand Led Resources will be required.

The ELEXON Implementation Resource Cost will typically have a tolerance of +/- 5% associated with it.

### ONGOING SUPPORT AND MAINTENANCE COSTS

<b>ELEXON Operational Cost</b>	Cost, in man days per annum multiplied by project average daily rate, of operating the revised systems and processes post-implementation.
<b>Service Provider Operation Cost</b>	Cost in £ per annum payable to the Service Provider(s) to cover staffing requirements, software or hardware licensing fees, communications charges or any hardware storage fees associated with the ongoing operation of the revised systems and processes.
<b>Service Provider Maintenance Cost</b>	Cost quoted in £ per annum payable to the Service Provider(s) to cover the maintenance of the amended BSC Systems.