

20 May 2003

URGENT MODIFICATION CONSULTATION

MODIFICATION PROPOSAL P128

**Correction of erroneous Energy Contract
Notifications in specifically defined limited
circumstances**

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

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Author **ELEXON**

I DOCUMENT CONTROL

a Authorities

Version	Date	Author	Reviewer	Change Reference
0.1	10/03/03	Dena Harris	Richard Clarke	Initial Draft
0.2	17/03/03	Dena Harris	Modification Group	Discussion
0.3	19/05/03	Dena Harris	Richard Clarke/Justin Andrews	Draft

b Distribution

Name	Organisation
Each BSC Party	Various
Each BSC Agent	Various
The Gas and Electricity Markets Authority	Ofgem
Each BSC Panel Member	Various
energywatch	energywatch
Core Industry Document Owners	Various

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1 INTRODUCTION

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

An electronic copy of this document can be found on the BSC Website, at WWW.ELEXON.CO.UK.

This document seeks views on the Modification Proposal.

Electronic responses should be sent to: Modifications@elexon.co.uk by 12.00 hrs on 30 May 2003 and responses by post should be addressed to the Modifications Department, ELEXON Ltd., 4th floor, 350, Euston Rd., NW1 3AW, again to arrive by 12.00 hrs on 30 May 2003. Responses should be marked 'Response to the P128 Consultation'.

If you have any queries about the issues raised in this consultation paper, please contact either Dena Harris, or Richard Clarke, at ELEXON (tel. (0207)-380-4100) or alternatively email on dena.harris@elexon.co.uk, or richard.clarke@elexon.co.uk

2 BACKGROUND AND TIMESCALES

Modification Proposal P128, 'Correction of erroneous Energy Contract Notifications in specifically defined limited circumstances' ('P128'), was submitted by Gaz de France Marketing Ltd, on 6 May 2003. The Proposal is both retrospective and prospective in nature and seeks to provide 'new entrants' with the same provisions that were allowed for existing entrants following the introduction of paragraph P6 into the Code by Modification Proposal P37.

Modification Proposal P37 'To provide for the remedy of past errors in Energy Contract Notifications and in Metered Volume Reallocation Notifications' ('P37') was concerned with a similar perceived defect, (although it was purely retrospective), and was approved by the Authority on 10 May 2002. Modification Proposal P44, 'Correction of Notification Errors where Parties are able to satisfy a Reasonable and Prudent Operator test' ('P44') was solely prospective, with a fairly wide application, and was rejected by the Authority on 10 May 2002. P128 refers to the Authority's determination with regards to both these proposals.

P128 was submitted with the request that it be treated as an Urgent Modification Proposal.

On the 7 May 2003, the Authority agreed that P128 should be progressed as an Urgent Modification and the following timetable was also agreed:

- *Initial meeting of the P128 Modification Group; 09/05/03*
- *Second meeting of the P128 Modification Group; 16/05/03*
- *Issue Consultation; 20/05/03*
- *Closing date for responses to consultation; 30/05/03*
- *Third meeting of the P128 Modification Group; 02/06/03*
- *Issue draft Urgent Modification Report to the Panel; 06/06/03*
- *Consideration of draft Urgent Modification Report by the Panel; 12/06/03*
- *Issue final Urgent Modification Report to the Authority; 13/06/03*

The objective of this consultation is to receive views as to the merits, or otherwise of P128, including views on detailed aspects of the proposal and draft legal text. This will enable the Modification Group to take into account industry views in determining their recommendation in respect of P128. It will also enable an Alternative Modification Proposal to be formulated, if appropriate. The consultation responses and Modification Group discussions will be used to issue a draft Urgent Modification Report which will be presented to the Panel, at the meeting on 12 June 2003, for their consideration.

A copy of the Modification Proposal is available on the BSC Website (www.ELEXON.co.uk) and is appended in Annex 1.

3 PROPOSER'S VIEW ON EXTENT TO WHICH THE PROPOSED MODIFICATION WOULD BETTER FACILITATE THE APPLICABLE BSC OBJECTIVES

The Proposed Modification is justified by the Proposer on the following principal grounds:

- It would ensure that, as regards the period prior to the adoption of the Modification Proposal, settlement of imbalance obligations will be conducted by reference to Parties' true contract positions as required by Condition C3(2)(b)(ii) of NGC's Transmission Licence rather than by reference to erroneously notified positions. The Proposed Modification would therefore, in the Proposer's opinion, promote the attainment of the objectives specified in Condition C3(3)(a) of that licence (the efficient discharge by NGC of its licence obligations).
- In addition the Proposed Modification is made pursuant to Transmission Licence Condition C3(3)(d) promoting efficiency in the implementation and administration of the balancing and settlement arrangements, in the Proposer's opinion. It is not the purpose of the Code to be implemented in a manner that imposes, and neither it should be possible for any mistake to result in, a penal charge on a BSC Trading Party where there has been no physical imbalance on the Transmission System and no costs or losses have been incurred by other Parties.
- The retrospective effect of the Proposed Modification can therefore be expected to:
 - promote effective competition in generation and supply of electricity, by allowing the BSC Parties, and new entrants and those expanding into new operational areas in particular, to place reliance on the effectiveness of the Code in addressing unfairness (Condition C3(3)(c)) to the extent that those Parties identified above are more likely to make notification errors, then the Proposed Modification may further serve to promote competition from them, by protecting them from the disproportionate consequences of such errors; and
 - as stated above (Condition C3(3)(d)) reducing the risk to Parties of participating in the market and thereby reducing the risk related costs of balancing and settlement activity.

4 MODIFICATION GROUP DISCUSSIONS

The first Modification Group meeting took place on 09/05/03 and the second on 16/05/03. The thoughts and discussions of the SSMG Modification Group, (the Group), from both meetings are recorded here.

4.1 Wording of P128

The Group discussed the wording of the Modification Proposal and a member of the Group queried the wording that stated "The Panel may decline to rectify a notification error in whole or part if it considers that the Party concerned did not at the relevant time have prudent systems and processes in place for checking notifications and/or have failed to take appropriate steps to improve such systems and processes once the error had been discovered." The Modification Group member stated that he believed that the "may" should have been a "shall" to be consistent with paragraph P6.

The Proposer confirmed that they had not intended to change the meaning of the P6 provisions and accepted the clarification.

4.2 Limitation to internal transactions of a single BSC Party

A member of the Group questioned why the Modification Proposal had been limited to strictly defined circumstances. The Proposer indicated that this was because of previous decision letters made in respect of Notification Errors where criteria for the approval of potential future Modifications was laid out.

It was suggested by a member that limiting the Modification Proposal in such a way would unduly favour vertically integrated participants at the expense of other participants.

The Group suggested that an option for a potential Alternative Modification may allow this scope to be widened and that this may address some of the concerns held within the Group in relation to potential discrimination.

4.3 Potential Inconsistency with paragraph P6

A member of the Group observed that there was a potential inconsistency as a result of paragraph P6 allowing claims to be made in respect of MVRNs. The Group agreed that if the Modification Proposal was restricted to single Parties, then it would only apply to ECVNs and that MVRNs were not an issue.

The Group also agreed that an option for consideration in an Alternative Modification that may be considered is widening the scope to include MVRNs.

4.4 Definition of "new entrant"

For the purposes of P128, the Group sought clarification on what Group of participants the Modification Proposal was meant to apply to. The Group then discussed what may have been meant by the term "new entrant". The Group agreed that "new entrant" in this

context, meant a single Party who carried out transactions between their production and consumption accounts for the first time. The Group agreed that the term "new entrant" should no longer be used with regards to the Proposed Modification as it was misleading and thus the term that will now be used is "new internal transactor".

The Group discussed other definitions of new internal transactor one of which was to limit it to participants who had not previously been involved in the industry. This is an option for an Alternative Modification.

4.5 Period for which claims can be made

In referring to the 28 day period defined within the Modification Proposal, the Group noted that this referred to the 28 day period commencing with the first volume delivery between the Production and Consumption Energy Accounts of that Party.

The Group however considered that an option to be considered for any Alternative Modification could include changing this period so that reference was made to the FAA Notification Day as defined within the Settlement Calendar.

A member of the group thought the period should be shorter than this as a prudent operator would check settlement reports and thus identify any errors earlier than this. The Group noted that a change in the timescale could form part of an Alternative Modification.

4.6 Contestability¹

The Group considered whether contestability of the Market would increase given a reduction in risk of entry due to the opportunity for PNE claims. It also considered to what extent this potential increase in contestability would increase competition in the market. The Group considered that it would. They also discussed whether by applying P128 to both new entrants and existing Parties and applying it in retrospect would increase competition. The Group considered that it might have a benefit in terms of perceived risk by potential new entrants

4.7 Period for making claims

The Group considered the period allowed for claims made under paragraph P6 and noted that when introduced, P6 allowed a period of 5 Business Days to make a claim. This had subsequently been extended to 10 days as a result of P83. The Group agreed that the original 5 Business Days claim window was appropriate and was consistent with Modification Proposal P37. The Group agreed that this 5 day claim window would apply to both the Prospective and retrospective elements of the Modification Proposal.

¹ In economic terms, a contestable market is one in which the cost of entry and subsequent cost of potential exit is [relative to reward in the market] low. If a given market is fully contestable, then you can [in theory] have a monopoly in that market which is not able to charge any monopoly rent (i.e. its prices will be at a fully competitive level). If it were to increase prices above this level then others would enter the market at very little cost and take market share from it hence reducing its profits.

4.8 Claims adjudication procedure

The Group discussed the claims adjudication procedure.

No changes were proposed to the wording of P6 in relation to the Claims Adjudication procedure and that it would be up to the Panel to determine whether they wished to appoint a separate Panel sub committee or deal with the claims themselves.

The Group noted that the PNE claims process was a one off process and that an ongoing process for P128 would need to be efficient, economic and timely..

The Group considered it appropriate to retain the P6 provisions of an Authority appeal process for P128.

4.9 Principle of softer rules for new internal transactors

The Group discussed the principle of whether it was appropriate to have softer rules for new internal transactors. They also mentioned there may be potential disincentives on BSC Parties to make correct notifications caused by P128.

The Group also suggested that the issues associated with P128 had been widely publicised within the treatment of P37.

The Group felt that the key difference between P37 and P128 is that at the time of NETA Go-Live, participants did not have a choice as to whether or when they entered the market, whereas subsequent to Go-Live participants could enter the market when they were ready to do so. One member of the Group felt that at Go-Live Parties declared their readiness and thus did have a choice.

In addition reference was made to the increased reporting facilities now available to participants, that were not available at Go-Live.

Some of the Group also commented that it was the responsibility of the participant to ensure they have robust systems and prudent processes in place for contract notification.

4.10 Principle of retrospection

The Group noted the retrospective element within the Modification Proposal and determined that there were no new facts to add to the debate that had not previously been aired in respect to other Modification Proposals such as P37. Some members of the Group felt that it would seem appropriate that a retrospective element was present in the Modification Proposal to enable a consistent approach to be taken for all NETA Settlement Days. However other members considered that an Alternative Modification without retrospection might be better in terms of Applicable BSC Objectives.

Some members of the Group considered that the retrospective aspect of P128 should not be limited to new internal transactors but could be open to all market participants whereas the prospective aspect of P128 could be limited to new entrants. These options could form part of an Alternative Modification.

4.11 Applicable BSC Objectives

The Group agreed that the Proposed Modification may improve competition in the supply and generation of electricity however they felt that incorporating an enduring process may decrease the efficiency of the balancing and settlement arrangements.

They also considered that it was difficult to claim that the retrospective element of P128 would improve competition in the supply and generation of electricity.

4.12 Potential Alternative Modifications

The Group agreed that there may be scope for an Alternative Modification that better facilitates the Applicable BSC Objectives and were asked to bring forward any option in respect of this to their next meeting.

Aspects of Proposed Modification P128 that the Group considered could be changed are shown in the table below;

Feature	Proposed Modification	Option For Alternative Modification
Contract Notifications	ECVN	ECVN and MVRN
Parties included in P128	New internal transactors	All Parties
Type of transaction	Internal transactions only e.g between Production and Consumption Energy accounts	All transactions including trades between Parties
Implementation	Retrospective and prospective	Prospective only Retrospective only
Settlement Periods for which claims can be made	28 calendar days	[date] under 28 calendar days FAA Notification Day

Respondents are asked to provide views with respect to the above issues discussed and to comment on whether there exists a potential Alternative Modification that better facilitates the Applicable BSC Objectives.

4.13 Interaction with P107

The Group discussed the interaction of P107 with P128. P107 limits the timing of the Post Final Settlement Run to 28 months from the Settlement Day. P107 includes a provision to exclude Paragraph P6 of the Code from this limitation. The Group noted that they did not want P128 to be excluded from P107 limitations as part of Paragraph P6, and thus the legal text should be drafted to reflect this.

4.14 Implementation Date

A proposed implementation date was 5 Business Days after an Authority decision. This reflects that for P37.

4.15 Impact Assessments

The Group confirmed that no BSC Agent Impact Assessments should be carried out as this change is a Code change and impacts mainly on ELEXON systems and processes.

4.16 Legal Text

The Group considered the draft legal text and agreed that it addressed the defect identified within the Modification Proposal. The Group noted that the legal text allowed claims to be made for non contiguous contract notifications made within the 28 day window.

5 CONSULTATION QUESTIONS

Your views are invited on the generality of the Proposal and the issues related to it, as presented in this consultation. To help assess the issues we would be grateful if you could answer the consultation questions provided in the proforma attached. The proforma also contains a confidential section for which responses will be presented to the Modification Group only in aggregated form and the Authority in full.

ANNEX 1 MODIFICATION P128

Modification Proposal – F76/01	MP No: 128
<p>Title of Modification Proposal:</p> <p>Correction of Erroneous Energy Contract Volume Notification Errors in specifically defined limited circumstances</p>	
<p>Submission Date: 6th May 2003</p>	
<p>Description of Proposed Modification:</p> <p>Gaz de France Energy Marketing Limited (GdFM) proposes a modification that would amend the Balancing and Settlement Code (BSC) to enable specifically defined past errors in Energy Contract Volume Notifications (ECVNs) to be remedied on an ex-post basis in limited circumstances.</p> <p>This proposal follows modification proposal P37 that addressed past notification errors but limited submission of claims to an initial five-day window, subsequently amended by P83 to ten-days, following adoption of the proposal. The Authority accepted P37 on 10th May 2002.</p> <p>This modification proposal is intended to be retrospective and effective from the close of P37 claims window, and would provide an enduring provision thereafter, to provide new entrants with similar provisions to rectify notification errors as those that existed for existing entrants following the approval of P37.</p> <p>The intent of this modification proposal, for ECVN error corrections, is that claims should be treated in a manner as defined within section P6 of the BSC except that they will be strictly limited and the following conditions must apply:</p> <ul style="list-style-type: none"> • Only ECVN errors involving a single BSC Trading Party will be accepted (where the Party/Counter-Party and the Energy Contract Volume Notification Agent are all the same BSC Party). • The ECVNs are limited to notifications between that Trading Party's Production and Consumption Accounts where one or both have no previous historical usage or notified volumes • Claims will only apply to notifications in respect of the volume delivery periods including and immediately following the first Settlement Day but limited to a maximum of 28 days thereafter • No other BSC Trading Party has incurred a direct financial impact other than those 'windfall gains' flowing through Residual Cashflow Reallocation Cashflow <p>It would be for the Trading Party making the claim to prove to the satisfaction of the Panel that it was the clear intent of the Trading Party to commit to notify accurately the true trading position and that there had been a mistake in giving effect to that commitment.</p>	

Note: At the point of submission of this modification proposal GdFM is of the view that clarification and/or simplification of the content of the ECVAA I022 report could go some way towards ensuring that new Trading Parties, or those who invoke usage of new consumption or production accounts for the first time, avoid causing such errors to occur in future. However we do not seek as part of this modification proposal to directly address this issue we simply note our view in order that consideration of this issue may be appropriate at a later stage under the direction of the panel.

In determining whether or not a notification error should in all circumstances be rectified, the Panel may have regard, amongst other things, to the following factors, where the Panel considers such factors to be relevant:

- That the notification error was directly attributable to the BSC Systems
- The notification error or loss suffered as a result of the error arose from a combination of circumstances that could not have been reasonably foreseen, or
- The magnitude of the loss suffered was wholly disproportionate to the fault or error committed.

The Panel may decline to rectify a notification error in whole or part if it considers that the Party concerned did not at the relevant time have prudent systems and processes in place for checking notifications and/or have failed to take appropriate steps to improve such systems and processes once the error had been discovered.

Where the Panel decided that a notification error should be rectified, it would be required to determine that appropriate adjustments be made to the erroneous notification. These adjustments would bring a notification into line with the true trading position. It is the intention that the corrected notification would then be used for the purposes of Settlement.

A non-refundable administration fee, to be agreed by the Panel, would be payable to Balancing and Settlement Code Company (BSCCo) in respect of each claim. In addition it would be appropriate to subject the Trading Party to an error correction payment, equivalent to 20% of the benefit of the correction, for having a notification error corrected.

Each claim should be considered on a case-by-case basis and to aid efficiency each claim should be resolved quickly thus avoiding additional Settlement Runs. In the case of a retrospective claim such claims should be made within five business days of the implementation date of the modification proposal.

Description of Issue or Defect that the Modification Proposal Seeks to Address:

Condition C3(3) of the NGC transmission licence requires NGC to have in force a document (the Balancing and Settlement Code (BSC)) setting out the terms of the balancing and settlement arrangements. Those arrangements are defined in condition C3(2)(b)(ii) to include arrangements for the settlement of obligations between the BSC Parties:

'arising by reference to the [physical quantities of electricity allocated to BSC Parties], including the imbalances ... between such quantities and the quantities of electricity contracted for sale and purchase between BSC Parties'.

The modification proposal is designed to ensure that the BSC does, in fact, fulfil the requirements of condition C3(2)(b)(ii) of NGC's licence, by providing for each Party's imbalance position to be settled by reference to its true contract position, rather than by reference to a notified position that turns out to have been erroneous.

The BSC places on the contracting Parties the onus of notifying to the Energy Contract Volume Aggregation Agent details of their contractual position in respect of each Settlement Period. Once Gate Closure has been reached for any given Settlement Period, Parties have

only limited opportunity to correct any errors in their contract notifications. This means that, in cases where an erroneous notification has been made, and has not been corrected before Gate Closure, the settlement of imbalances will be effected by reference to the difference between the Party's physical production (or consumption) and the notified amount, rather than by reference to the difference between the Party's physical production (or consumption) and the contract amount. The actual requirements described in Condition C3(2) are therefore not, in fact, achieved, and the affected Party may consequently suffer substantially higher imbalance charges than would apply if the correct contract volumes had been used to calculate settlement liabilities.

In order to achieve full and final settlement, the BSC must provide an effective mechanism for the Settlement Administration Agent to collate information as to each Party's contract position for each Settlement Period, and to calculate settlement liabilities accordingly. In practice, the contracting Parties are best placed to provide information as to their contract position, and it is appropriate that they should be required and incentivised to provide accurate information.

However, there is no good reason why Parties should be denied the opportunity to correct erroneous notifications, including those which have occurred already, provided that:-

- (a) the Parties do so sufficiently soon to avoid any delay in final settlement;
- (b) the opportunity for Parties to rectify erroneous notifications does not unduly diminish incentives to provide accurate notifications in the first place; and
- (c) the opportunity to rectify erroneous notifications is used for its proper purpose – namely, to rectify erroneous notifications of Parties' true trading positions, and not to effect and notify changes in a Party's contract position that occur after Gate Closure.

The modification proposal is designed to introduce into the BSC a provision enabling Parties to rectify notification errors within these limits, in this case with retrospective effect.

Impact on Code:

Section P of the BSC will require modification

Impact on Core Industry Documents:

N/A

Impact on BSC Systems and Other Relevant Systems and Processes Used by Parties:

May require the creation of a new Balancing and Settlement Code Procedure to manage the process

Impact on other Configurable Items:

None

Justification for Proposed Modification with Reference to Applicable BSC Objectives:

The proposed modification is justified on the following principal grounds:

1. It would ensure that, as regards the period prior to the adoption of the modification proposal, settlement of imbalance obligations will be conducted by reference to Parties' true contract positions as required by Condition C3(2)(b)(ii) of NGC's Transmission Licence rather than by reference to erroneously notified positions. The proposed modification would therefore promote the attainment of the objectives

specified in Condition C3(3)(a) of that licence (the efficient discharge by NGC of its licence obligations).

2. In addition the proposed modification is made pursuant to Transmission Licence Condition C3(3)(d) promoting efficiency in the implementation and administration of the balancing and settlement arrangements. It is not the purpose of the BSC to be implemented in a manner that imposes, and neither it should be possible for any mistake to result in, a penal charge on a BSC Trading Party where there has been no physical imbalance on the Transmission System and no costs or losses have been incurred by other Parties.
3. The retrospective effect of the proposed modification can therefore be expected to:
 - a) promote effective competition in the generation and supply of electricity, by allowing the BSC Parties, and new entrants and those expanding into new operational areas in particular, to place reliance on the effectiveness of the BSC in addressing unfairness (Condition C3(3)(c)) to the extent that those Parties identified above are more likely to make notification errors, then the proposed modification may further serve to promote competition from them, by protecting them from the disproportionate consequences of such errors and
 - b) as stated above (Condition C3(3)(d)) reducing the risk to Parties of participating in the BSC and thereby reducing the risk related costs of balancing and settlement activity

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ANNEX 2 DRAFT LEGAL TEXT

See attached document.

Paragraph P6 and its provisions can be viewed on the ELEXON Website,
www.ELEXON.co.uk