



Direct Dial: 020-7901 7435

3 June 2003

The National Grid Company, BSC Signatories and  
Other Interested Parties

Our Ref: MP No P118

Dear Colleague,

**Modification to the Balancing and Settlement Code (“BSC”) - Decision and Direction in relation to Modification Proposal P118: “Increased efficiency in the reporting of Credit Default statements”**

The Gas and Electricity Markets Authority (the “Authority”)<sup>1</sup> has carefully considered the issues raised in the Modification Report<sup>2</sup> in respect of Modification Proposal P118, “Increased efficiency in the reporting of Credit Default statements”.

The BSC Panel (the “Panel”) recommended to the Authority that Proposed Modification P118 should be made, with an Implementation Date of 24 June 2003 if an Authority decision is received before 4 June 2003. If a decision is received on or after 4 June 2003, the Implementation Date should be 15 Business Days after any such Authority decision.

Having carefully considered the Modification Report and the Panel’s recommendation and having regard to the Applicable BSC Objectives and the Authority’s wider statutory duties<sup>3</sup>, the Authority has decided to direct a Modification to the BSC in line with the Modification Proposal P118.

This letter explains the background and sets out the Authority’s reasons for its decision. In addition, the letter contains a direction to National Grid Company plc (“NGC”) to modify the BSC in line with Modification Proposal P118, as set out in the Modification Report.

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

<sup>2</sup> ELEXON document reference P118RR, Version No. 1.0, dated 11 April 2003.

<sup>3</sup> Ofgem’s statutory duties are wider than the matters that the Panel must take into consideration and include amongst other things a duty to have regard to social and environmental guidance provided to Ofgem by the government.

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

## **Background**

If a Trading Party's Credit Cover Percentage ("CCP") as determined by the Energy Contract Volume Aggregation Agent ("ECVAA") becomes greater than 80% for any Settlement Period, the ECVAA informs the Trading Party to that effect through a level 1 default notice. The Trading Party is then provided a Query Period, which ends 24 hours after receipt of the level 1 default notice, during which the Trading Party can query the ECVAA's determination and/or reduce its CCP to an acceptable level. If the ECVAA's determination that the CCP was in excess of 80% is confirmed, then to avoid being put into Level 1 Credit Default, the Trading Party must ensure that its CCP is not greater than 75% for at least one Settlement Period during the time between the expiry of the Query Period and 24:00 hours on the first Business Day after the day in which the Query Period expires. The period between the expiry of the Query Period and 24:00 hours on the first Business Day after the day in which the Query Period expires is called the default cure period.

If a Party enters into Level 1 Credit Default, the BSC requires that the ECVAA inform the Trading Party (and all other Parties, through postings on the Balancing Mechanism Reporting Service {"BMRS"} or BSC Website) as soon as reasonably practicable after 9:00 hours on the day following the expiry of the default cure period. The Modification Report notes that this deferment of notification until after 9:00 hours was written into the BSC on the grounds of practicality, since part of the posting process is done manually. However, following the CVA June 03 BSC Systems Release and the implementation of Change Proposal 703, the ECVAA system will be capable of reporting Credit Default notices automatically to the Balancing Mechanism Reporting Agent, which in turn will automatically publish them on the BMRS.

To benefit from this new capability, Modification Proposal P118, "Increased efficiency in the reporting of Credit Default statements" was raised by the BSCCo on behalf of the Panel on 19 February 2003.

## **The Modification Proposal**

Modification Proposal P118 seeks to modify the BSC so as to allow for the posting of Level 1 Credit Default notices as soon as practicable after the expiry of the default cure period. The justification for the Modification Proposal was that it would better facilitate achievement of the Applicable BSC Objective<sup>4</sup> C3 (3) (d).

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<sup>4</sup> The Applicable BSC Objectives, as contained in Standard Condition C3 (3) of National Grid Company's Transmission Licence, are:

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

It was considered that the prompt reporting of Level 1 Credit Default, in conjunction with the automation of the reporting process, would constitute a more efficient implementation of the BSC.

The Panel considered the Initial Written Assessment at its meeting of 13 March 2003 and agreed to submit Modification Proposal P118 directly to the Report Phase. ELEXON published a draft Modification Report on 18 March 2003, which invited respondents' views by 27 March 2003.

### **Respondents' views**

ELEXON received six responses to the consultation on Modification Proposal P118. Four responses (representing 21 Parties) expressed support for the Proposed Modification, one response (representing 6 Parties) opposed the Proposed Modification and the remaining respondent (representing 1 Party) provided a "No Comment" response.

The respondent who opposed the Proposed Modification did so on the basis that automatic reporting without checking if a Party is in Level 1 Credit Default risks incorrectly damaging Parties' reputations and the removal of the time between the expiry of the default query period and 9:00 hours on the following day from the process may hamper a Party's ability to resolve its credit position.

The respondents' views are summarised in the Modification Report for Modification Proposal P118, which also includes the complete text of all respondents' replies.

### **Panel's recommendation**

The Panel met on 10 April 2003 and considered the Modification Proposal P118, the draft Modification Report and the consultation responses received.

The Panel recommended that the Authority should approve the Proposed Modification and that, if approved, the Proposed Modification should be implemented on 24 June 2003 if an Authority decision is received before 4 June 2003, or the Implementation Date should be 15 Business Days after any such Authority decision received on or after 4 June 2003.

### **Ofgem's view**

Having carefully considered the Modification Report and the Panel's recommendation, Ofgem considers, having regard to the Applicable BSC Objectives and its statutory duties, that Modification Proposal P118 will better facilitate achievement of the Applicable BSC Objectives.

Ofgem considers that the elimination of the requirement for manual intervention in the Credit Default reporting process will better facilitate the efficient administration of this aspect of the BSC, thereby better facilitating Applicable Objective (d). Ofgem notes that the modification of the process in this manner does not affect the requirement to have an authorisation notice from BSCCo in force before such notices can be posted on the BMRS or the BSC Website, so that the existing safeguards to Parties' reputations remain unaffected by the implementation of this

Modification Proposal. Further, Ofgem considers that there is sufficient time between the origination of the level 1 default notice and the expiry of the default cure period for erroneous determinations to be corrected and that it is otherwise in the interests of all Parties to report verified Credit Defaults in as prompt a manner as processes allow.

### **The Authority's decision**

The Authority has therefore decided to direct that the Proposed Modification P118, as set out in the Modification Report for Modification Proposal P118, should be made and implemented.

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

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

The Implementation Date for Modification Proposal P118 is 24 June 2003.

In accordance with Condition C3 (5) (b) of NGC's Transmission Licence, NGC shall modify the BSC in accordance with this direction of the Authority.

If you have any questions, please contact me on the above number.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'D. Edward', written in a cursive style.

**David Edward**  
**Head of Electricity Code Development**

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