

Meeting name BSC Panel

Date of meeting 14 October 2004

Paper Title SSMG ISSUE 12: 'TIMESCALES FOR WITHDRAWAL FROM THE BSC'

Purpose of Paper For Information

Synopsis Issue 12 was raised on 21 September 2004 by Uskmouth Power Company Limited, such that potential improvements to the current withdrawal process could be considered. The Settlement Standing Modification Group (SSMG) met on 27 September 2004 to consider Standing Issue 12. This paper summarises the SSMG's discussions and conclusions. The SSMG concluded that there appeared to be inefficiencies in the current withdrawal process and that there may be merit in a Modification Proposal being raised to allow a Non-Supplier Trading Party to withdraw from the Code prior to completion of the Final Reconciliation Run.

1. BACKGROUND

- 1.1 The criteria for withdrawal from the Balancing and Settlement Code ('the Code') are contained in Section A5. Under paragraph A5.1.3(b), a Party may not withdraw until the Final Reconciliation Run (RF) has been carried out in relation to the last Settlement Day on which such a Party traded¹. Therefore, a Party must typically wait approximately 14 months to withdraw from the Code.
- 1.2 Uskmouth Power Company Limited raised Issue 12 on 21 September 2004, such that potential improvements to the current withdrawal process could be considered. In particular, so that the possibility of reducing the existing withdrawal timescales by enabling certain Parties, under specified circumstances, to withdraw from the Code prior to the completion of RF could be considered.
- 1.3 The Settlement Standing Modification Group (SSMG) met on 27 September 2004 to consider Issue 12.
- 1.4 A copy of the issue as submitted by Uskmouth Power Company Limited is attached as Annex 1.

2. POTENTIAL MODIFICATION PROPOSAL

- 2.1 The representative of Uskmouth Power Company Limited ('the Proposer's Representative') highlighted three perceived flaws in the current withdrawal process:

¹ Note that this is one amongst several criteria for withdrawal contained in A5.

(a) Legal Risk: 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 to another Party), are bound by any modifications to the Code until withdrawal.

(b) Administrative Inefficiency: the current withdrawal process for many Parties results in considerable and unnecessary administrative costs and effort for the withdrawing Party and for ELEXON over the 14 month withdrawal period.

(c) Timescale Based on Non Half Hourly Market: the 14 month withdrawal timescale seems to have been designed around a reconciliation process based on settling NHH Metered Volumes. However, there appears to be no compelling reason to require Parties not involved in the Supplier Volume Allocation ('SVA') arrangements to adhere to this extended withdrawal timetable.

2.2 To address these perceived flaws, Uskmouth Power Company Limited is considering submitting a Modification Proposal that would facilitate more timely and efficient withdrawal from the Code². This potential Modification Proposal would allow certain Parties to withdraw from the Code prior to the completion of RF. The key features of this potential proposal are as follows:

(a) Eligibility: Parties who are not responsible for any meters or are only responsible for Central Volume Allocation ('CVA') registered meters, would be entitled to exercise a right to withdraw prior to the completion of RF, provided that they met all other withdrawal criteria (see A5.1.3).

(b) Early Withdrawal Option: eligible Parties would be entitled to withdraw upon completion of the Second Reconciliation Run (R2) from the last Settlement Day.

(c) Security Against Potential Reconciliation Charges: Eligible Parties exercising the right to withdraw after R2 would be required to leave a cash deposit, any remainder of which would be refundable upon completion of the Reconciliation process, as security against potential reconciliation charges accrued between R2 and RF.

2.3 The SSMG, acting as a Standing Modification Group in accordance with F2.4.23, considered the Code issue and the potential Modification Proposal tabled to address that issue identified by Uskmouth Power Company Limited.

2.4 This paper summarises the SSMG's discussions and conclusions on the key elements of the proposed early withdrawal option – eligibility, withdrawal criteria and the security deposit.

3. ELIGIBILITY FOR EARLY WITHDRAWAL

3.1 The Proposer's Representative indicated that the option to withdraw upon completion of R2 would be available only to those Parties with no registered meters and those with CVA registered meters alone. The rationale for this restriction is that the positions of such Parties would have been largely settled by R2 and that the primary purpose of 14 month Settlement timetable was

² Modification Proposal P178 'Reduction in the BSC Withdrawal Timescale for Parties who have Settled the Vast Majority of their Trading Debts' was submitted by Uskmouth Power Company Limited on 4 October 2004.

to facilitate the reconciliation arising from NHH SVA meters. Unlike Parties with SVA registered meters, which typically show larger variations in Metered Volumes between R2 and RF.

- 3.2 In addition, because R2 is approximately three months (i.e. 85 days) after a Settlement Day, Parties seeking to withdraw from the Code will have had sufficient time by R2 to transfer any assets (e.g. BM Units and meters) to another Party. As 'Change of BM Unit Ownership' (COBO) takes 30 days.
- 3.3 The SSMG noted that the potential for accruing reconciliation charges between R2 and RF was likely to be lower for Parties without SVA registered meters. Therefore, the SSMG agreed that restricting an early withdrawal option to such Parties would provide greater security to the market than were it also open to Parties with SVA registered meters. However, the SSMG noted that such a solution would need to exclude Parties which had no SVA registered meters at the point of application for withdrawal but had previously transferred SVA registered meters for which the last Settlement Day had not passed.
- 3.4 The SSMG agreed that any assessment of a Modification Proposal similar to the proposed early withdrawal option would need to explore the materially of disputes upheld within R2 compared to materiality of disputes upheld within RF.
- 3.5 The SSMG noted that the existing definition of "Non-Supplier Trading Party" in paragraph M.2.3A.7 of the Code might be able to be used for the purposes of defining eligibility for an early withdrawal option. The definition is as follows:

"[A] Non-Supplier Trading Party shall be a Trading Party which is not:

(a) a Supplier; or

(b) a Subsidiary Party in Metered Volume Reallocation Notification where the Lead Party in the Metered Volume Reallocation Notification was a Supplier where the percentage value is greater than zero;

and in all cases this shall have been the case for any Settlement Day for which a Final Reconciliation Settlement Run has not been performed".

4. WITHDRAWAL CRITERIA

- 4.1 The Proposer's Representative proposed that Parties eligible for early withdrawal should still need to meet all the other existing withdrawal criteria (i.e. all those aside from RF having been completed). The criteria are contained in A5.1.3 and, in summary, preclude a Party from withdrawing where:

(a) sums accrued and payable under the Code remain to be paid by that Party³;

³ Note that as a result of Approved Alternative Modification P127 'Optional de-registration by insolvent Party', a Party in Default solely for reasons of insolvency or administration may have this withdrawal criterion, in relation to the Base Monthly Charge accruing after the Withdrawal Notice, waived by the Panel.

- (b) Metering Systems and/or BM Unit (excluding Base BM Units) are still registered in the Party's name under the Code and/or MRA; and
 - (c) such a Party is in Default and that Default is capable of remedy but has not been remedied⁴.
- 4.2 In addition, the Proposer noted that Parties in administration or who are insolvent may and should still be able to qualify for the early withdrawal option provided that they met the relevant criteria.
- 4.3 The SSMG agreed that any early withdrawal option should remain subject to having satisfied the existing exit criteria, to ensure that no additional and unnecessary risk is introduced into the trading arrangements.

5. SECURITY DEPOSIT

- 5.1 In acknowledgement that all Parties remain liable for further reconciliation charges (even after withdrawal in the case of Extra Settlement Determination, see Section A5.3.3(b)), the Proposer's Representative indicated that the proposed early withdrawal option would need to include a requirement that the withdrawing Party leave a deposit as security against any potential reconciliation charges accruing against that Party between R2 and RF. For each Reconciliation run between withdrawal and RF, the deposit could then be used to settle any charges accrued by the withdrawn Party without the need to send bills and pay potentially minimal amounts of money. After RF, the Party would receive a final settlement bill and any monies remaining from the deposit would be credited to them.
- 5.2 The Proposer's Representative outlined five possible methodologies for the calculation of the deposit:
- (a) Average percentage difference between R2 and RF Metered Volumes for the withdrawing Party (taken over the previous year) scaled to the withdrawing Party's associated Metered Volumes and multiplied by the Credit Assessment Price (CAP);
 - (b) Average percentage difference between R2 and RF Metered Volumes for all BM Units in the past year, scaled to the withdrawing Party's associated Metered Volumes and multiplied by CAP;
 - (c) Code defined value reviewed annually by the Panel;
 - (d) Deposit based on a Party's reconciliation charges between R2 and RF for the past year plus x%; and
 - (e) Deposit based the average reconciliation charges for all Parties between R2 and RF over the past year plus x%.

⁴ Similarly, as a result of Approved Alternative Modification P127, this criterion may be waived by the Panel in the case of a Party in Default solely for reasons of insolvency or administration.

- 5.3 The Proposer's Representative noted that under methodologies (a) and (b) a minimum amount (e.g. £1000) would need to be set for non-physical traders because these Parties do not have metered volumes. As an additional safeguard, the level of this fixed deposit could be 'ratcheted' up if Parties reconciliation charges prove to exceed the level of the deposit (i.e. withdrawn Parties would be required to deposit funds to comply with the revised deposit level).
- 5.4 Some members of the SSMG expressed doubt as to what mechanism would exist to recover funds owed by a Party who had exited the Code and whose deposit had been exceeded, noting that in respect of such Parties ELEXON would have the status of an unsecured creditor. However, the Proposer's Representative noted that under A5.3.3(b) Parties are still liable for reconciliation charges even after having exited from the Code.
- 5.5 The SSMG noted that whilst a withdrawing Party can currently transfer its assets (e.g. BM Units), reconciliation liabilities may not be transferred. Therefore if a Party is billed, but does not pay, its debts are spread across all Parties' Default Funding Shares. If the cash deposit of a Party who withdrew at R2 was not enough, and the Party refused to lodge further amounts (given that it would no longer be subject to Code obligations) its liabilities would therefore be picked up by all Parties.
- 5.6 The SSMG requested legal advice from ELEXON on the issue of the recovery of outstanding monies from Parties that have withdrawn from the Code. ELEXON Legal provided the following advice:
- **Withdrawn Parties:** in the event of a withdrawn Party with outstanding payments under the BSC, ELEXON would have the option of initiating legal action to recover any monies owing.
 - **Withdrawn Parties in Administration:** in the event of a withdrawn Party going into administration with outstanding payments under the BSC, ELEXON's ability to recover the outstanding monies would be determined by the rules governing insolvency law, and how the administrator in question decides to exercise its powers of repayment (as determined by insolvency law) to creditors of the withdrawn Party.
- 5.7 The SSMG indicated a preference for options (b) and (e) over options (a) and (d), because these methodologies were based on average market positions rather than individual positions. Average-based methodologies would reduce the impact on ELEXON, by allowing a single annual calculation to be made and the result used to determine the deposit required by any Party exercising the option of early withdrawal.
- 5.8 One member of the SSMG noted a preference for a mechanistic methodology as opposed to a deposit set and reviewed by the Panel. This member believed the former would provide greater certainty and transparency for market participants and potential new entrants.
- 5.9 Another member of the SSMG suggested an alternative methodology might be to calculate a deposit based on the BSCCo Charges which a Party would be liable for were it to remain a Party to the Code until the completion of RF.
- 5.10 The SSMG agreed that an early withdrawal option would need to be made contingent on the withdrawing Party leaving a deposit as security against potential liabilities in order to protect the

market. Furthermore, the SSMG agreed with the Proposer's Representative that a cash deposit placed with the FAA appeared to be a pragmatic form for the proposed deposit.

- 5.11 ELEXON Finance clarified that VAT would still apply to deductions from any cash deposit amount placed with the FAA and noted that the administration of deposit proposed would constitute an additional overhead. In addition, ELEXON Finance noted that the Code already allowed for cash to be lodged up front with ELEXON to cover future payments.

6. FURTHER ISSUES

- 6.1 The SSMG noted that were the proposed early withdrawal option introduced, BSC Systems would still need to retain identifiers for withdrawn Parties against which to allocate reconciliation charges or credits accrued between withdrawal and RF. ELEXON indicated that such a facility was already required and in operation for withdrawn Parties for the purpose of allocating any liabilities arising after RF (e.g. from upheld Trading Disputes).
- 6.2 The SSMG noted that the proposed early withdrawal option would be available to insolvent Parties provided that they met the proposed withdrawal criteria.

7. CONCLUSIONS

- 7.1 The SSMG concluded that there appeared to be inefficiencies in the withdrawal process that could potentially be viewed as a barrier to competition. As a consequence, the SSMG agreed that there may be merit in a Modification Proposal being raised to allow a Non-Supplier Trading Party to withdraw from the Code prior to completion of the Final Reconciliation Run.

Roger Salomone

ELEXON Change Delivery

List of enclosures

Annex 1: Issue 12

Annex 2: Issue 12 Membership

ANNEX 1: ISSUE 12

Issue for SSMG
 From Uskmouth Power Company Limited
 Represented by Lisa Waters, Waters Wye Associates

Timescales for Withdrawal from the BSC

The current process for withdrawing from the BSC has a number of flaws:

1. Companies who have (or are trying) to withdraw from the BSC are concerned about the ongoing risks that they face as a result of being party to a contract when they are no longer operational in the market. They often do not have the staff or expertise to monitor the BSC and just want to pay their bills and make a timely exit from the market. In all cases they have terminated all other contracts, transferred assets and wound up operations months before they can leave the BSC.
2. The withdrawal process for many parties results in considerable administrative costs for both Elexon and the withdrawing party for the purposes of chasing small amounts of money for the required 14 months for withdrawal. These costs are being paid by all parties.
3. Ease of exit from a market seems as important as ease of entry if the market is to encourage competition and keep the BSC as a contract between parties who are actually operating in the market.
4. The current 14 months to withdraw seems to have been designed around the reconciliation process that relates only to NHH meter registrants. There appears to be no compelling reason to treat parties not subject to SVAA activity in the same way.

To improve the efficiency of the process and to limit the costs and risks for all parties Uskmouth Power Company Limited is considering a modification to facilitate a more timely and efficient exit from the market for those players who have settled all of their trading debts as best as they are able given the reconciliation process.

Purpose: Allow parties who are non-physical traders or are only responsible for CVA registered meters to withdraw from the BSC after the second reconciliation run (R2) after the last settlement day, on the condition they have met all the other criteria for withdrawal (Section A 5.1.3). In effect the modification would alter A5.1.3(b)).

Accepting that all parties remain liable for further reconciliation (even after withdrawal – Section A 5.3.3(b)), the current thinking was to require parties withdrawing before the final reconciliation to leave a cash deposit with Elexon. This deposit would then be adjusted with each reconciliation (both deposits and withdrawals) and a final settlement statement and any remaining money would be returned to the party after the 14 months.

Issues:

There are a number of areas where we would welcome views prior to drafting a modification.

Withdrawal timing – R2 is about 3 months (D+85) after the final trades of these parties. In the case of physical players it would allow their assets to have transferred to another party (COBO is 30 days). Meter errors should also have been dealt with and we expected most material disputes could have been raised and resolved.

Definition of eligible parties – if the modification defines parties as those with no registered meters and those with meters registered in CVA systems does this cause any problems? The 14 months seems to be based on the NHH reconciliations, but to define a “generator” seems to open a lot of legal issues.

Alternatively we could not define the party, but leave it as any party not subject to any SVAA allocation runs, this then includes both physical and non-physical players who see the majority of their settlement at the SF.

Withdrawal criteria – the modification would not be attempting to get parties who owe money, have meters etc out of the BSC leaving liabilities. Our initial view was that the withdrawal criteria (A5.3.1) should still apply.

Cover for final bills – as all parties seem to be impacted by each reconciliation (though the amounts concerned are minimal) the withdrawing party could leave a cash deposit with Elexon to cover reconciliations between withdrawal and the final reconciliation (RF).

The calculation of the deposit could use:

1. The percentage difference between the SF and RF CVA meter reads for the withdrawing party, taken over the past year, multiplied by CAP.
2. The average percentage difference between SF and RF CVA meter reads for all BM Units in the past year, then scale it to the withdrawing party's BM Units multiplied by CAP.

For both these options a minimum amount (£1000) would need to be set for non-physical players. This number could be reviewed annually by the Panel and/or ratcheted if any player subsequently goes over the deposit. The ratchet could be set as a multiple of the amount that the initial deposit was exceeded (so say $5 \times x$ where x is the amount over the £1000 the party's liabilities climbed to).

3. Just use a set amount for all players that is reviewed annually by the Panel. Again a ratchet could be put in place to keep deposits above liabilities.
4. Calculate the value of each party's liabilities between SF and RF for the past year and require that amount of deposit + x%.
5. Calculate the average liability for all parties, subject to CVA systems, between SF and RF and use the average +x% as the deposit.

Options 1 and 4 seems to involve more work for Elexon in calculating amounts for each party (with some cost), where options 2 and 3 the calculation could be done annually and applied to all parties. Option 3 may lead to concerns about the level of the deposit, but would be easier.

Form of deposit – the initial view was that a cash deposit placed with FAA and administered in the same was as all cash deposits would be pragmatic.

Settlement – for each reconciliation between withdrawal and RF the deposit could be used to settle the party without the need to send bills and collect/pay minimal amounts of money. After the RF the party would receive a final settlement bill (an aggregation of all the bills they would currently receive) and all remaining money would be returned to them.

Party ids – Central systems will have to maintain the ids to allocate the continued flows of moneys to/from the deposit. At the point of withdrawal the party would have to give contact details to Elexon for the purposes of managing any issues associated with the deposit and to send the final settlement position to. If the basis of the deposit calculation is to cover all charges parties should want to stay in touch with Elexon to retrieve all money after 14 months. Do we need to define companies that are no longer parties to the BSC, but who are party to reconciliation?

Points to Note

Disputes – the BSC does not allow a party to withdraw when it has sums accrueable or payable that are subject to a dispute. This would not be altered. All parties can raise disputes after the 14 months anyway (P131 allows 20 months) so there is always the potential for a reconciliation involving a dispute impacting a party who has already withdrawn. All parties are still liable reconciliation charges even after they withdraw and this would also not change (Section A 5.3.3(b)).

Insolvent parties – this modification would be designed only to allow parties who have paid their bills to withdraw from the BSC and would require them to still deposit cash for the purposes of fulfilling the existing BSC obligations. If a party is in administration, but in this position they should be able to withdraw.

Voluntary – no party would be forced to go down this route, it would be voluntary and would allow withdrawal to be considered any time after R2 if a party met the criteria.

Liabilities – Are there any liabilities apart from financial liabilities that need to be considered?

Remaining Debts – Elexon may be concerned that if a deposit is exceeded they will have no route to pursue a company and would be acting as unsecured creditors. Our experience suggests that the amounts of money concerned are so small as to be uneconomic for Elexon for to pursue. It must also be remembered that at the current time a party can reduce its credit to zero (given the minimum amount rules) and not pay bills. Companies do not seem to have done this, but we recognise that the deposit must be sufficient to cover all reasonably foreseen bills.

Before submitting a modification we would welcome the views of parties on the points outline above any other areas they feel should be considered. If parties wish to contact Lisa Waters directly they can do so on 020 8286 8677.

21 September 2004

ANNEX 2: ISSUE 12 MEMBERSHIP

The membership of the SSMG for the consideration of Issue 12 was as follows:

Member	Organisation	Email	27/09/04
Roger Salomone	ELEXON (Chairman)	roger.salomone@elexon.co.uk	✓
Kathryn Coffin	ELEXON (Lead Analyst)	kathryn.coffin@elexon.co.uk	✓
Lisa Waters	Waterswyte Consulting	lisa@waterswyte.co.uk	✓
Helen Bray	EDF Energy	helen.bray@edfenergy.com	✓
Ben Willis	Npower	ben.willis@npower.com	✓
Neil Smith	E.ON UK	neil.c.smith@eon-uk.com	✓
Mark Manley	British Gas Trading	Mark.Manley@centrica.co.uk	✓

In addition the following attendees were present at the meeting held on 27 September 2004:

Attendee	Organisation	Email	27/09/04
Melanie Henry	ELEXON	melanie.henry@elexon.co.uk	✓
Charlotte Hutchinson	ELEXON	charlotte.hutchinson@elexon.co.uk	✓
Neena Sukumaran	ELEXON	neena.sukumaran@elexon.co.uk	✓