

| | | | |
|------------------------|---|----------------------|---------------|
| Modification proposal: | Balancing and Settlement Code (BSC) P322: Revised Implementation Arrangements for Mandatory Half Hourly Settlement for Profile Classes 5-8 | | |
| Decision: | The Authority ¹ directs that P322 Alternative proposal be made ² | | |
| Target audience: | National Grid Electricity Transmission Plc (NGET), Parties to the BSC and other interested parties | | |
| Date of publication: | 24 June 2015 | Implementation Date: | 3 August 2015 |

Background to the modification proposal

On 29 October 2014, we approved BSC Modification P272 'Mandatory Half Hourly Settlement for Profile Classes 5-8'.³ This mandates that sites in Profile Classes (PCs) 5-8 with advanced meters are settled half-hourly (HH) from 1 April 2016.

On 20 March 2015, Elexon wrote to us on behalf of the BSC Panel⁴ to request, in accordance with Section F, Paragraph 2.11.8, of the BSC that we delay the P272 Implementation Date from 1 April 2016 to 1 April 2017. This was because of concerns around the risk to settlement accuracy from moving large numbers of sites to HH settlement in short timescales and the likely interruption of supply contracts where a consumer is moved to HH settlement and has a contract that extends beyond 1 April 2016.

We responded to the BSC Panel on 20 April 2015.⁵ Our letter explained that, while we shared some of the BSC Panel's concerns about the risks to settlement and consumers associated with the current P272 Implementation Date, we had decided not to approve its request. We were concerned that, on its own, an extension to the deadline would not address these risks. We also said we would be open to consideration of alternative solutions that address the risks to consumers.

The modification proposal

Npower raised P322 'Revised Implementation Arrangements for Mandatory Half Hourly Settlement for Profile Classes 5-8' on 28 April 2015 to propose new arrangements for migrating sites in PCs 5-8 to HH settlement. It requested that P322 be treated as an Urgent Modification Proposal, which was agreed by the BSC Panel at an ad-hoc meeting on 29 April 2015. We approved the BSC Panel's recommendation that P322 be treated as an Urgent Modification Proposal on 7 May 2015.⁶

The proposed solution ('P322 Proposed') introduces the following requirements:

- From 5 November 2015, a supplier must move sites in PCs 5-8 with advanced meters to HH settlement within 45 business days of customer acquisition or contract renewal, except where it has entered into a contract between 29 October

¹ The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

² This document is notice of the reasons for this decision as required by section 49A of the Electricity Act 1989.

³ Our P272 decision can be found on our website: <https://www.ofgem.gov.uk/publications-and-updates/balancing-and-settlement-code-bsc-p272-mandatory-half-hourly-settlement-profile-classes-5-8>

⁴ The BSC Panel is established and constituted pursuant to and in accordance with Section B of the BSC.

⁵ Our letter to the BSC Panel is available on our website: <https://www.ofgem.gov.uk/ofgem-publications/94555/lettertobscpanel-pdf>

⁶ Our letter to the BSC Panel is available on our website: <https://www.ofgem.gov.uk/ofgem-publications/94773/p322authoritydecisiononurgency-pdf>

2014 and the P322 Implementation Date that takes effect on or after 5 November 2015.

- Where the supplier has entered into a contract for a site between 29 October 2014 and the P322 Implementation Date that takes effect on or after 5 November 2015, this site must be settled HH by 1 April 2016.
- From 2 November 2017, all sites in PCs 5-8 with advanced meters must be settled HH.
- By 31 August 2015, a supplier must submit a migration plan showing how it will migrate its sites in PCs 5-8 with advanced meters to HH settlement.
- The Performance Assurance Board (PAB)⁷ must approve each migration plan. Where a supplier's plan is approved, it must adhere to it and provide regular updates on progress against the plan.

The proposer envisages that, if P322 Proposed is approved, the P272 Implementation Date will be moved to 2 November 2017. This would align with the P322 Proposed requirement that all sites in PCs 5-8 with advanced meters must be migrated to HH settlement by 2 November 2017. The proposer considers that P322 Proposed better facilitates applicable objectives (c) and (d) of the BSC.⁸

The workgroup established by the BSC Panel to assess P322 developed an alternative solution ('P322 Alternative'). This is identical to P322 Proposed, except in two respects:

- P322 Alternative removes the exception to the requirement that, from 5 November 2015, a supplier must move sites in PCs 5-8 with advanced meters to HH settlement within 45 business days of customer acquisition or contract renewal. In P322 Proposed, the exception applies where the supplier has entered into a contract between 29 October 2014 and the P322 Implementation Date that takes effect on or after 5 November 2015.
- P322 Alternative does not specify the date by which all sites in PCs 5-8 with advanced meters must be settled HH, instead referring to the P272 Implementation Date. However, the workgroup recommended that this date should be set to 1 April 2017.

BSC Panel recommendation

On 11 June 2015, the BSC Panel unanimously agreed that both P322 Proposed and P322 Alternative would better facilitate objectives (c) and (d) of the BSC. It also recommended by majority that P322 Alternative should be approved. This is based on the assumption that, alongside approval of P322 Alternative, we would extend the P272 Implementation Date by at least 12 months. Therefore, the BSC Panel also wrote to us directly on 12 June 2015 to request, in accordance with Section F, Paragraph 2.11.8, that we delay the P272 Implementation Date to 1 April 2017.

The Authority's decision

We have considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 11 June 2015. We have considered and taken into

⁷ The PAB reports to the BSC Panel and is responsible for BSC performance assurance.

⁸ As set out in Standard Condition C3(3) of NGET's Transmission Licence, see: <http://epr.ofgem.gov.uk/index.php?pk=folder380751>

account the responses to ELEXON's consultation that are attached to the FMR.⁹ We have concluded that:

- Implementation of P322 Proposed or P322 Alternative will better facilitate the achievement of the applicable objectives of the BSC.
- Implementation of P322 Alternative will better facilitate the achievement of the applicable objectives compared to P322 Proposed.
- Directing that P322 Alternative be made is consistent with the Authority's principal objective and statutory duties.¹⁰

Reasons for the Authority's decision

We consider that both P322 Proposed and P322 Alternative will better facilitate BSC objectives (c) and (d), and that P322 Alternative best facilitates these objectives overall. We consider that both P322 Proposed and P322 Alternative could have a modest negative impact against BSC objective (a) and are neutral against the other applicable objectives. We set out our assessment against each objective that is affected below.¹¹

Alongside this letter, we have written to the BSC Panel accepting its request to extend the P272 Implementation Date to 1 April 2017.¹²

BSC Objective (c) – promoting effective competition in the supply of electricity and (so far as is consistent therewith) promoting such competition in the sale and purchase of electricity

We agree with the majority of the workgroup that P322 Proposed and P322 Alternative, in conjunction with an extension to the P272 Implementation Date, will better facilitate competition in the supply of electricity to consumers in PCs 5-8. This is because they will avoid undermining confidence and engagement in the market, which is critical to ensuring there is competitive pressure on suppliers.

Originally, suppliers were required to move all their sites in PCs 5-8 to HH settlement by 1 April 2016. Information gathered by the P322 workgroup from 19 suppliers shows that around 45 per cent of sites with advanced meters and fixed-term contracts have contracts that will not expire by this date.¹³ When these sites move to HH settlement, the costs incurred to serve them will change. Therefore, there is a risk that suppliers will reflect any cost changes by interrupting the contracts they hold with the relevant customers. This could undermine engagement in the market, particularly if the supplier raises prices unexpectedly and the consumer is unable to shop around for other offers because it cannot leave the contract or must pay a penalty to do so.

P322 Proposed and P322 Alternative will help to avoid this scenario. Both envisage an extension to the P272 Implementation Date, which enables suppliers to move most sites to HH settlement at contract end unless the customer wishes to migrate sooner. At the

⁹ BSC modification proposals, modification reports and representations can be viewed on the Elexon website at www.elexon.com

¹⁰ The Authority's statutory duties are wider than matters which the Panel must take into consideration and are detailed mainly in the Electricity Act 1989.

¹¹ We assess P322 Proposed and P322 Alternative against the baseline. We include P272 as part of the baseline as it has already been approved.

¹² Our Letter to the BSC Panel can be found on our website: <https://www.ofgem.gov.uk/licences-codes-and-standards/codes/electricity-codes/balancing-and-settlement-code-bsc>

¹³ The suppliers that provided information to the P272 workgroup supply approximately two-thirds of sites in PCs 5-8. Our focus is on fixed-term contracts because they may prevent a consumer from terminating early or charge them to do so. This is generally not the case for rolling contracts.

same time, both P322 Proposed and P322 Alternative require that, from 5 November 2015, a supplier must move sites in PCs 5-8 with advanced meters to HH settlement within 45 business days of customer acquisition or contract renewal. This mitigates the risk that, as a result of extending the P272 Implementation Date, suppliers continue to agree contracts that assume a site is settled non-half-hourly (NHH) until the last possible moment. Suppliers that behave in this way may be able to grow market share (for some customers, HH settlement will mean an increase in energy costs) at the expense of those who are taking steps to implement P272 in a timely way by migrating sites to HH settlement at contract end. Moreover, if a supplier continues to sign contracts that assume a site is NHH settled, these contracts may need to be interrupted later to the detriment of consumer engagement in the market.

We note that around 30 per cent of PCs 5-8 sites with advanced meters and fixed-term contracts have contracts that expire before 5 November 2015. Those with current-transformer (CT) meters can move to HH settlement on contract expiry. However, some suppliers have said they will not be ready to do this. Moreover, it is unlikely that those with whole-current (WC) meters move to HH settlement before 5 November 2015, when new HH Distribution Use of System (DUoS) tariffs become available.¹⁴ Where a supplier is unable to move to HH settlement, those sites that are covered by fixed-term contracts that expire before 5 November 2015, we expect them to treat the relevant customers fairly. In particular, if they sign another fixed-term contract, we expect that this would either expire before the P272 Implementation Date or make clear to the consumer when and how the terms of the contract may need to change as a result of moving to HH settlement in advance of the P272 Implementation Date.

One member of the workgroup said that neither P322 Proposed nor P322 Alternative would better facilitate objective (c) of the BSC because they create pricing uncertainty for consumers. We understand this uncertainty may arise because only the existing supplier will know whether a site has a CT or WC meter, which affects the DUoS charges it incurs. As a result, other suppliers may not be able to offer a contract to the consumer. We consider this problem exists now in the absence of P322 Proposed and P322 Alternative. Hence we do not agree that they create additional pricing uncertainty for consumers. However, we encourage the industry to take steps to make available as a priority information on whether a site has a CT or WC meter.

Assessment of P322 Proposed against P322 Alternative

The proposer envisages that, if P322 Proposed is approved, the P272 Implementation Date would move to 2 November 2017. However, the BSC Panel recommended that we approve P322 Alternative and agree that the P272 Implementation Date is extended to 1 April 2017. Information gathered by the P322 workgroup from suppliers shows that nearly 95 per cent of sites in PCs 5-8 with advanced meters and fixed term contracts have contracts that expire by 2 November 2017, compared to nearly 90 per cent on 1 April 2017.

As a result, P322 Alternative puts a slightly higher number of consumers at risk of contract interruption assuming that the P272 Implementation Date is extended to 1 April 2017 as per the BSC Panel's request, which could affect their engagement in the market. However, we consider that this impact is limited for two reasons:

- First, we note that suppliers can give affected consumers significant forewarning of potential changes to their contracts, assuming that these consumers are migrated to HH settlement as close as possible to 1 April 2017. This avoids

¹⁴ BSC Modification P300 introduces new Measurement Classes that enable sites with WC meters to access new HH DUoS tariffs. It will be implemented on 5 November 2015.

unexpected short-notice changes to contracts and gives time for the consumer to budget accordingly.

- Second, by 1 April 2017, suppliers will have had more time to develop the products they offer to sites in PCs 5-8 that move to HH settlement. Therefore, the consumer may have a range of options if its supplier changes the existing contract on moving to HH settlement. The extended implementation timetable for P272 will help mitigate the risk of suppliers not engaging customers at the point of contract interruption if this occurs and simply increasing prices, rather than offering a range of products and services.

The proposer also said that P322 Proposed would reduce the potential for contract interruption by explicitly making allowances for contracts that are agreed before 3 August 2015 on the assumption a site continues to be NHH settled but take effect after 5 November 2015. The proposer was concerned that, without this, contracts for these sites may be interrupted. We do not share this concern. P322 Alternative allows the PAB to approve a migration plan that does not comply with the requirement to move sites to HH settlement. Whilst we would expect this to happen only in exceptional circumstances, it allows for flexibility, where appropriate, including potentially where contracts that have already been agreed prior to P322 Implementation Date take effect after 5 November 2015.

On balance, taking all the above into account, we find that both P322 Proposed and P322 Alternative better facilitate objective (c).

BSC Objective (d) – promoting efficiency in the implementation and administration of the balancing and settlement arrangements

We agree with the majority of the workgroup that P322 Proposed and P322 Alternative will promote objective (d) of the BSC. More than half of the 13 suppliers, that responded to the BSC Panel's 17 February 2015 consultation on an extension to the P272 Implementation Date, said they were unable to implement P272 by 1 April 2016. Moreover, suppliers planned to move the majority of sites to HH settlement in less than five months. This would create a material risk of errors occurring during the Change of Measurement Class (CoMC) process that is used to move sites from NHH to HH settlement, to the detriment of efficient implementation of the BSC.

P322 Proposed and P322 Alternative, in conjunction with an extension to the P272 Implementation Date, enable a more orderly migration of sites in PCs 5-8 with advanced meters to HH settlement. Suppliers will be able to spread out the CoMC process for sites over a longer period, reducing the risks of errors. At the same time, at a minimum, they must move a site to HH settlement on contract expiry or customer acquisition. This prevents suppliers from continuing to settle their sites NHH until the last possible moment, which would materially increase the risks of errors occurring during the CoMC process. Moreover, P322 Proposed and P322 Alternative both include requirements for suppliers to submit and report on their migration plans that must be approved by PAB. This enables much closer scrutiny of the transition, which helps to promote efficiency in the implementation of P272 and hence the BSC.

Two respondents to Elexon's consultation said they will not have the systems and processes in place to move sites in PCs 5-8 with advanced meters to HH settlement from 5 November 2015. One of these respondents also said that this date did not give sufficient time for new DUoS tariffs to be assessed. The workgroup selected 5 November 2015 because this is the earliest point at which an appropriate HH DUoS tariff is available for all sites in PCs 5-8. We consider that suppliers have had significant time to put in place necessary systems and processes since our decision to approve P272 on 29 October

2014. Moreover, if the requirement to migrate sites to HH settlement on customer acquisition or contract expiry were to fall later, suppliers may continue to settle their sites NHH and hence increase the risk that large numbers of sites are migrated in a short period of time. Finally, we note that new DUoS tariffs for CT and WC metered sites in 2015/16 were published before the start of this charging year. On balance, we consider that 5 November 2015 is an appropriate date.

Assessment of P322 Proposed against P322 Alternative

The majority of the workgroup said that P322 Alternative better facilitates objective (d) compared to P322 Proposed because it provides a simpler solution that is more straightforward to implement. We agree with this view.

We note that P322 Proposed gives clarity now that suppliers have until 1 April 2016 to migrate to HH settlement consumers who agreed contracts before 3 August 2015 that take effect after 5 November 2015. While it could be argued that this helps suppliers to develop their migration plans more efficiently compared to P322 Alternative, it adds additional complexity. Moreover, P322 Alternative has allowed time for suppliers to refine migration plans in advance of the 5 November 2015 based on feedback from PAB. Therefore, the benefit of earlier certainty from P322 Proposed is small.

On balance, we consider that P322 Alternative better facilitates objective (d) of the BSC compared to P322 Proposed.

BSC Objective (a) – the efficient discharge by the Transmission Company of the obligations imposed upon it by the Transmission Licence

In its response to Elexon's consultation, NGET stated that P322 is neutral against objective (a). However, NGET did raise a concern about a related modification to the Connection and Use of System Code, Modification Proposal 241 (CMP241). NGET raised CMP241 to avoid sites in PCs 5-8 with advanced meters being overcharged for use of the transmission network in the year that they move to HH settlement. We approved CMP241 on 30 March 2015.¹⁵

Where a site moves to HH settlement before the start of the charging year that precedes the P272 Implementation Date, CMP241 allows the supplier to decide whether it is treated as NHH or HH for transmission charging purposes. When CMP241 was raised, the P272 Implementation Date was 1 April 2016, such that NGET expected only a small number of sites would have moved to HH settlement in the preceding charging year (ie, before 1 April 2015). However, if the P272 Implementation Date is extended, many more sites will be in this position. If suppliers want large numbers of these sites to be treated as a HH site for transmission charging purposes, NGET is concerned about its ability to implement CMP241 and hence its ability to discharge efficiently its licence obligation to set cost-reflective transmission charges.

From the evidence available to us at this time, there is the potential for P322 Alternative and P322 Proposed to increase the costs of implementing CMP241. Therefore, we consider that both will have a modest negative impact against objective (a) of the BSC. However, we consider this is outweighed by both facilitating BSC objectives (c) and (d). P322 Proposed and P322 Alternative, in conjunction with an extension to the P272 Implementation Date, will effectively mitigate material risks to consumers that arise from delivering P272 by 1 April 2016. While this affects NGET's ability to discharge efficiently

¹⁵ Our decision letter can be found here: <https://www.ofgem.gov.uk/ofgem-publications/94323/cmp241decisionletterfinal30march2015-pdf>

its licence obligations, we consider it is able to address any issues effectively. We would encourage NGET to take steps to do so in a timely way.

Decision notice

In accordance with Standard Condition C3 of NGET's Transmission Licence, the Authority hereby directs that modification proposal BSC P322 Alternative: *Revised Implementation Arrangements for Mandatory Half Hourly Settlement for Profile Classes 5-8* be made.

Rob Church – Partner, Retail Markets

Signed on behalf of the Authority and authorised for that purpose