

Phase

Initial Written Assessment

Definition Procedure

Assessment Procedure

Report Phase

Implementation

P362 'Introducing BSC arrangements to facilitate an electricity market sandbox'

This Modification proposes to enable Parties to be derogated from specific obligations in the Balancing and Settlement Code to enable pre-competitive and innovative products and services to be tested in the live environment for a limited period of time.



The BSC Panel recommends **approval** of the P362 **Alternative** Modification and **rejection** of the P362 **Proposed** Modification

This Modification is expected to impact:

- BSC Parties
- Party Agents
- BSC Panel
- Transmission Company
- Ofgem
- Non-BSC Parties
- ELEXON



Contact

Ivar Macsween

020 7380 4270

ivar.macsween@elexon.co.uk



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About This Document

This is the P362 Final Modification Report, which ELEXON has submitted to the Authority on behalf of the BSC Panel. It includes a summary of the Workgroup's assessment, the Panel's full views and the responses to both the Workgroup's Assessment Consultations and the Panel's Report Phase Consultation. The Authority will consider this report and will decide whether to approve or reject P362.

There are ten parts to this document:

- This is the main document. It provides details of the solution, impacts, costs, benefits/drawbacks and proposed implementation approach. It also summarises the Workgroup's key views on the areas set by the Panel in its Terms of Reference, and contains details of the Workgroup's membership and full Terms of Reference.
- Attachment A contains the redlined changes to the BSC for P362 Proposed Modification.
- Attachment B contains the redlined changes to the BSC for P362 Alternative Modification.
- Attachment C contains the P362 business requirements.
- Attachment D contains the Code Subsidiary Document (CSD) for the P362 Proposed Modification Proposal.
- Attachment E contains the CSD for the P362 Alternative Modification Proposal.

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- Attachment F contains a high-level end to end process map.
- Attachment G contains the collated responses received to the first Assessment Procedure Consultation.
- Attachment H contains the collated responses received to the second Assessment Procedure Consultation.
- Attachment I contains the full responses received to the P362 Report Phase Consultation.

Why Change?

Appropriate provisions do not currently exist within the Balancing and Settlement Code (BSC) to enable pre-competitive or proof of concept testing for innovative products or services in the live BSC Settlement environment. The absence of an arrangement to facilitate such testing hinders the development and trialling of innovations within the electricity market. Therefore the current arrangements act as a barrier to innovation and competition.

Solution

Proposed Solution

P362 seeks to enable BSC Parties to be derogated against specific BSC obligations in order to trial pre-competitive and innovative products and services. Ofgem will act as the point of entry to coordinate applications across the industry. This is designed to improve the customer experience and reduce the burden for applicants, particularly where applications require derogation from more than one industry code.

ELEXON will receive applications via Ofgem and prepare relevant information for the Panel's consideration. The Panel will make a recommendation to Ofgem whether to approve or reject the derogation application. Ofgem will then decide whether to grant the derogation and synchronise derogations across the impacted codes and licences.

Anyone can apply for derogation, however non-Parties will be required to accede to the BSC and complete the relevant market entry processes before the derogation can be effective. This is because you cannot be derogated from something you are not a party to.

BSC Companies (referred to as BSCCo or ELEXON within this document) and the Transmission Company (TC) cannot apply for, or be granted, BSC Derogation.

Alternative Solution

The P362 Alternative Modification is identical to the P362 Proposed Modification except that the TC can apply for, and be granted, BSC Derogation.

Impacts & Costs

P362 is a document only change that will directly impact the BSC Panel, Ofgem and ELEXON. They will need to implement new processes and products to operate the sandbox service.

P362 will indirectly impact (no material implementation effort) BSC Parties, non-BSC Parties, the TC and Party Agents who may choose to participate in the sandbox. The implementation impact and costs for the Proposed and Alternative solutions are the same.

Implementation

P362 is proposed for implementation five Working Days after approval, as a standalone BSC Release.

Recommendation

The BSC Panel unanimously agrees that the P362 Alternative solution **would** better facilitate Applicable BSC Objectives (c) and (d) compared to the current baseline and the P362 Proposed solution, and should therefore be **approved**.



What is a sandbox?

A sandbox is a term most often used in software development or computer security management. For example, it may refer to a testing environment that isolates untested code changes and outright experimentation from the production environment or repository. In computer security, a sandbox is a security mechanism for separating running programs, usually in an effort to mitigate system failures or software vulnerabilities from spreading.

However, in a regulatory or code environment it means a time limited exemption or derogation from particular rules or obligations to achieve specific aims, subject to given criteria and process.

Background

The industry is experiencing levels of change not seen since privatisation. These changes are many and varied, originating from consumers and prosumers, from existing or new market entrants, from European or Government policy, or from technology and data driven solutions. In all cases ELEXON is determined to do what it can to ensure the BSC is not a barrier to innovation and change.

The Panel, at its meeting on 12 October 2017, noted that the BSC does not have an electricity market sandbox or derogation process ([Panel Paper 271/04](#)). ELEXON believes the absence of an electricity market sandbox and process hinders the development and trialling of innovations within the electricity market.

ELEXON recommended to the Panel, at its meeting on 9 November 2017, that P362 should be raised to introduce a sandbox and derogation process into the BSC. The Panel agreed and raised P362 at this meeting (in accordance with BSC Section F2.1.1(d)).

Existing sandboxes

Ofgem launched its [Innovation Link](#) in December 2016. It provides fast, frank feedback to help innovators understand the regulatory implications of their business propositions. As part of this initiative, Ofgem have established a [regulatory sandbox](#).

Currently, Ofgem's regulatory sandbox does not extend to the BSC. However, in January 2018, Ofgem agreed to co-ordinate sandbox applications, including working with ELEXON and other interested Code Administrators¹ to:

- Develop a single point of entry for applicants;
- Operate a sifting process ahead of applications being forwarded to relevant Code Administrators; and
- Coordinate the feedback process on early, valid applications.

In its latest [sandbox application round](#) on 2 October 2017, Ofgem called for other industry bodies to adopt sandbox approaches to removing barriers.

Ofgem's regulatory sandbox has four eligibility criteria (innovation, consumer benefit, background research, and need for support). From its first sandbox round, Ofgem is currently in discussions with four innovators to grant regulatory sandbox access. The ideas put forward include peer-to-peer local energy trading platforms and trialling an innovative tariff supported by smart home technology.

Financial Conduct Authority (FCA)

Additionally, the FCA started operating a regulatory sandbox in June 2016. The FCA have found after the first year of operating their sandbox that it has reduced time and cost of getting innovations to market and helped facilitate access to finance. The FCA's sandbox offers guarantees of non-enforcement in place of derogations, and restricted authorisation in place of reduced market access requirements (which could be a type of requested derogation).

¹ At the time of consultation Ofgem is working with a number of Code Administrators, including ELEXON, to develop a cross-code sandbox process. There is not currently a date by when this work should be complete.

Existing BSC derogations

Whilst all BSC Parties must comply with the BSC, currently some obligations may be waived or met in a different way than that envisaged by the BSC. For example, the Metering Dispensation process, detailed in [Section L](#) of the BSC, allows Registrants of Metering Systems to apply for a Metering Dispensation if the associated Metering Equipment will not or does not comply with the applicable [Code of Practice \(CoP\)](#) (a BSC Code Subsidiary Document (CSD)). If granted, the Metering Dispensation allows the Registrant to deviate from the requirements in the relevant CoP.

Similarly, where a Party wishes to register a Balancing Mechanism (BM) Unit that does not meet the conditions required by BSC Section K, the responsible Party can apply to the Panel (delegated to the Imbalance Settlement Group (ISG)) for an exemption from these conditions. This type of BM Unit application is referred to as a non-standard BM Unit application. Where granted, it allows the Party to derogate from the Standard BM Unit requirements.

What is the issue?

Under the current BSC framework, provisions do not exist to enable pre-competitive or proof of concept testing for innovative products/business models in the live BSC Settlement environment.

The current BSC arrangements can pose a barrier to innovative business ideas. The BSC rules are necessary for the robust operation of balancing and Settlement across the Total System. In order for the BSC to be enforced fairly to all Parties, all Parties are required to comply with the rules. However, small projects with little or no impact on Settlement might find the full BSC uneconomic to comply with for a proof of concept trial.

Currently, the only option open to participants, looking to test new ways of doing things under the BSC, is to raise a BSC Modification (with the exception of the limited derogation options already facilitated within the BSC arrangements, such as the Metering Dispensations and non-standard BM Unit applications processes).

Progressing Modifications would likely be more resource intensive for both industry and ELEXON given the prescribed BSC Change process and associated governance. The BSC Change Process was not designed for the trialling of new products or business ideas. These governance constraints limit the ability to trial in the live environment and evaluate the benefits that innovative projects may deliver. For the avoidance of doubt, the issue is not the current BSC Change process, which should remain unchanged and unaffected by this Modification.

Increasingly, market participants that have not acceded to the BSC arrangements wish to have the ability to test new ways of working to allow them to establish whether it is economically viable and efficient for them to become a full part of the BSC framework. ELEXON have already been approached by companies interested in electric vehicle charging solutions, peer to peer trading platforms and local community energy schemes to discuss how their projects interact with and could be accommodated by the BSC.

The BSC should be able to accommodate the trialling of innovative concepts and technological advances that could subsequently be incorporated into the BSC framework. A new process is needed so that an individual BSC Party, class of Party, or non-BSC party can be exempted from specific BSC obligations to trial innovative products or ideas to test or prove the new product or idea for a fixed period of time.

Proposed solution

P362 'Introducing BSC arrangements to facilitate an electricity market sandbox' seeks to provide Parties with:

- The ability to test products and services in the live market;
- Reduced time to market at potentially lower cost; and
- Support in identifying and implementing new arrangements that can better facilitate the Applicable BSC Objectives.

P362 aims to enable industry participants, that have pre-competitive innovative products or services that are facing barriers to entry, to have the ability to be derogated from relevant obligations, in order to test and develop the product or service. Derogation will be subject to eligibility criteria being met.

Sandbox projects will be required to demonstrate how they will better facilitate the Applicable BSC Objectives. They are expected to be conducted on a small scale and for a limited duration. They should not have an adverse impact or pose a significant risk to Settlement or Parties.

BSCCo and the TC are not permitted to apply for derogation, or to be granted derogation.

P362 introduces a number of new defined terms, which can be found in the draft BSC legal text in Section Annex X-1 in Attachment A.

High level end-to-end process

In order to request derogation, applicants will submit an application to Ofgem, who will assess and evaluate the application against its eligibility criteria (innovation, consumer benefit, background research, and need for support). Those applications that meet the criteria will be passed to participating Code Administrators for assessment. Code Administrators will confirm if its respective code is impacted. If it is impacted, the Code Administrator will follow its own sandbox process (where available) to provide a recommendation to Ofgem on whether to grant derogation and any associated conditions. Ofgem will decide whether to derogate from the relevant codes and licences, and if so the conditions for that derogation. Where Ofgem want to amend the conditions, they will send the application back to the Panel for re-evaluation.

Attachment E contains a high-level process map for the proposed solution.

Role of the applicant and Derogated Party

Before the application is progressed by ELEXON, the applicant will be required to provide key information. For example, the proposed BSC obligations they seek derogation from, the Derogation Period, reporting and monitoring considerations and a Transition Plan.

The Transition Plan should provide a timeline of key activities needed to exit the sandbox. This plan is expected to be triggered following the end of the agreed Trial Period. However, it may be triggered at any time due to project issues, failure or non-compliance.

The applicant may be asked to pay an application fee, set by the Panel from time to time. However, it is expected this fee will initially be set at zero. The applicant may also be asked to pay certain costs associated with the derogation, such as paying for additional

ELEXON resources or compliance checks. These will be agreed as part of the application process.

If Ofgem approve the application and derogate the Party they will become a 'Derogated Party'. The Derogated Party will be expected to provide updates throughout the Derogation Period, as agreed upfront. The updates will feed into a lessons learned report for that particular project.

Role of ELEXON and the BSC Panel

ELEXON will conduct an evaluation of the application received from Ofgem. The evaluation will be submitted to the Panel in a 'Sandbox Report', which will form the basis for the Panel recommending to Ofgem whether to derogate or not. ELEXON must evaluate:

- The risks and impacts;
- The 'Sandbox Eligibility Criteria';
- The sections of the Code that need to be derogated;
- The length of the derogated period; and
- The applicant's Derogation Period.

The Panel shall consider the Sandbox Report and determine whether to recommend to Ofgem:

- That the proposed derogation be granted or rejected;
- What, if any conditions should be set for the proposed derogation; and
- That the Derogation Period and the Transition Plan be approved or amended.

In making its recommendation the Panel will consider, as they do for BSC Modifications, whether the derogation would better facilitate the Applicable BSC Objectives. They will also consider the scope of the derogation and a number of further criteria detailed in a BSC subsidiary document. The Panel may also be called upon to prioritise Applications, if for example there are high volumes of Applications.

Sandbox eligibility criteria

In assessing the derogation, ELEXON and the Panel will consider the impact and potential risk to Settlement and Parties. ELEXON will issue an impact assessment to industry for between 10 and 15 Working Days. Responses will be considered and included in the Sandbox Report and published on the BSC website. Other criteria that the Panel must consider are:

- The risks that granting the derogation poses to Settlement;
- The impact on other BSC Parties of granting the derogation;
- Whether the derogation request has reasonably assessed the minimum scope and timeline required to effectively trial the project;
- Whether the derogation being requested is materially similar to a derogation which is currently in force; and

- The impact of any imminent changes to the BSC.

Derogation conditions

The Panel may recommend to Ofgem conditions it believes are appropriate. These conditions will constrain the scope of the derogation to limit its impact and mitigate risks. Typically these will include:

- The total number of customers/ Metering System Identifiers (MSIDs) involved in the trial;
- The geographical area of the trial (e.g. single Grid Supply Point (GSP), single feeder, single site);
- The Meter classes that can be engaged in the trial;
- The total average consumption/generation of the MSIDs involved in the trial; and
- Any other parameters relevant to the derogation being requested.

Amendments to derogations

The Panel will also be able to recommend to Ofgem that derogations are amended or removed, following a similar approach taken for the original recommendation.

The Derogation Period

Derogations will be granted for two distinct periods: a 'Trial Period' and a 'Transition Period'. Together they will be known as the 'Derogation Period'. Diagram 1 below shows the Derogation Period timeline and limits.

Applications must include the length of time needed to test or trial the product or service, along with a rationale. This should be the shortest amount of time necessary to test the proposal and raise a Modification. This Trial Period can be extended for exceptional circumstances, but cannot be extended beyond the maximum Trial Period allowed of **two years**. The Derogated Party will need to provide relevant information to inform the decision. Ofgem can extend the Trial Period. At the request of the Derogated Party or ELEXON, the Panel will recommend to Ofgem whether to extend the Trial Period or not, before Ofgem makes a decision.

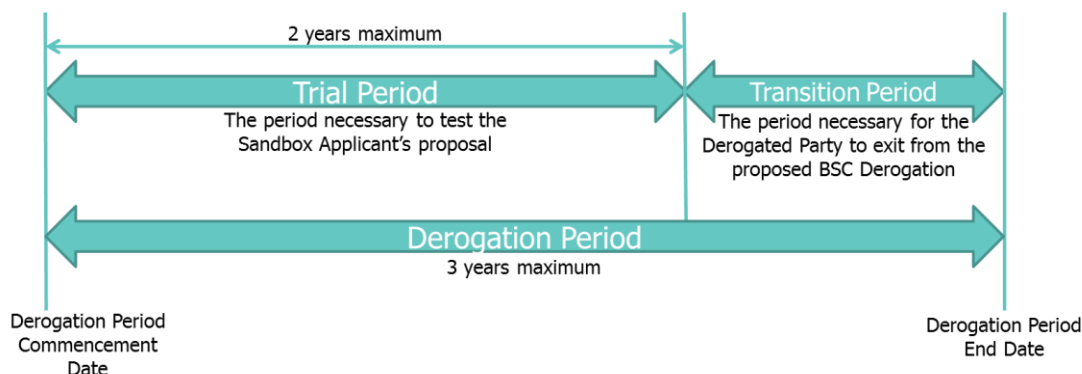
The Transition Period is the period during which the Party exits from the sandbox, either returning to the previous state or putting in place permanent arrangements via a BSC Modification. The Transition Period can be extended for exceptional circumstances and using the same approach as the Trial Period extensions.

Modifications

Where a BSC Modification is raised during the Trial Period to address the barriers/issues faced by the Derogated Party, and is not yet implemented, rejected or withdrawn, the Derogation Period may be extended to a maximum of **three years**. If the Modification is rejected or withdrawn the exit provisions within the Transition Plan will be triggered. It will be the responsibility of the Derogated Party (or any other Party) to raise a BSC

Modification. Where a Modification is not raised during the Trial Period, the Transition Period cannot be extended.

Diagram 1: Derogation Period



Appendix 3 contains further worked examples, including extensions to Derogation Periods.

Reporting and monitoring

In addition to the pre-agreed monitoring and reporting for each Derogated Party, ELEXON will produce a report, from time to time and at least annually, outlining lessons learned from the sandbox service. For example, metrics and statistics on the sandbox service, costs, key themes that have emerged, or any changes that has been, or need to be, made to the sandbox service.

More detail on the solution can be found in Attachment C (business requirements) and Attachment A (draft legal text).

Alternative solution

The Workgroup developed an Alternative Modification Proposal, which is identical to the Proposed Modification, except that the TC can apply for a BSC Derogation and be granted a BSC Derogation.

The Workgroup's discussions in developing the alternative solution are set out in section 6.

Legal text

The proposed redlined changes to the BSC to deliver P362 Proposed and Alternative Modifications can be found in Attachments A and B respectively.

Please note that the draft legal text for the Alternative solution is identical to the draft legal text for the Proposed solution, except for the provisions relating to H10.1.1 (Alternative text allows Ofgem to grant TC a BSC Derogation) and H10.2.1 (Alternative allows TC to apply for a BSC Sandbox Application).

A summary of the Workgroups discussions and actions in response to the first and second Assessment Consultation views on the legal text can be found in section six below.

Self-Governance

The Workgroup unanimously believes that this Modification does not meet the Self-Governance Criteria due to it having a material impact on competition and the Code's governance and modification procedures (Self-Governance criteria (a) (ii) and (iv) respectively).

This is on the basis that making the change will impact the Code's governance and modification procedures, through the introduction of a derogation mechanism for BSC obligations. BSC Derogations will also impact competition, as it aims to enable the trialling of innovative ideas and for more companies to offer alternative solutions to consumers. The Workgroup also noted that it has an indirect impact on consumers (a)(i), as any costs will ultimately be paid for by consumers.

Responses to the Assessment Consultations

| Do you agree that P362 does not meet the Self-Governance Criteria and so should not be progressed as a Self-Governance Modification? | | | | |
|--|-----|----|--------------------|-------|
| | Yes | No | Neutral/No Comment | Other |
| First Consultation | 9 | 0 | 0 | 0 |
| Second Consultation | 7 | 0 | 0 | 0 |

All respondents to the first and second Assessment Consultation agreed that P362 should not be progressed as a Self-Governance Modification. The reasons given broadly aligned with the Workgroup.

Are there any (other) alternative solutions?

The Workgroup discussed a number of variations of the proposed solution, including in response to the first Assessment consultation. These discussions are detailed in section six below.



What are the Self-Governance criteria?

A proposal that, if implemented:

- a) is unlikely to have a material effect on:
 - i. existing or future electricity consumers; and
 - ii. competition in the generation, distribution, or supply of electricity or any commercial activities connected with the generation, distribution, or supply of electricity; and
 - iii. the operation of the national electricity transmission system; and
 - iv. matters relating to sustainable development, safety or security of supply, or the management of market or network emergencies; and
 - v. the Code's governance procedures or modification procedures; and
- b) is unlikely to discriminate between different classes of Parties

4 Impacts & Costs

Estimated central implementation costs of P362

The implementation costs of P362 are approximately £6,000 to make the required changes detailed below. These costs primarily relate to the delivery of products needed by ELEXON to operate the sandbox service.

Indicative industry costs of P362

No material impacts or costs have been identified for industry participants to implement P362 from the first or second Assessment Consultation. This is in line with ELEXON's expectations. Rather it will enable parties to apply for BSC derogations, should they wish to.

Responses to the Assessment Consultations

| Will the implementation of P362 impact your organisation? | | | | |
|---|-----|----|--------------------|-------|
| | Yes | No | Neutral/No Comment | Other |
| First Consultation | 3 | 5 | 0 | 1 |
| Second Consultation | 1 | 6 | 0 | 0 |

Three respondents to the first Assessment Consultation said they would be impacted. Of which, only one indicated an implementation effort to implement a process to respond to derogation consultations. The other two did not indicate an implementation effort but identified indirect impacts should they wish to engage with the BSC sandbox process. The remaining five respondents to the first Assessment Consultation indicated that they would not be impacted.

One respondent to the second Assessment Consultation reported that they would need to adapt their processes to respond to BSC Sandbox applications. All other respondents confirmed they would not have any direct implementation impacts.

| Will your organisation incur any costs in implementing P362? | | | | |
|--|-----|----|--------------------|-------|
| | Yes | No | Neutral/No Comment | Other |
| First Consultation | 0 | 9 | 0 | 0 |
| Second Consultation | 0 | 7 | 0 | 0 |

All respondents to the first and second Assessment Consultation indicated that they would not incur costs in implementing P362.

These responses are in line with the impacts identified below.

P362 impacts

| Impact on BSC Parties and Party Agents | |
|--|--|
| Party/Party Agent | Impact |
| Parties and Agents | No implementation impacts identified. This Modification will allow Parties and Agents to participate in the sandbox process. |

| Impact on Transmission Company | |
|--|--|
| <p>The TC will not be permitted to apply for BSC derogations in the Proposed Modification, but will be permitted in the Alternative Modification. The TC confirmed in its impact assessment that if the Proposed Modification is approved, it will need to adapt its processes to provide views on applications in the future, and in the event the Alternative Proposal is approved, it will additionally need to adapt its processes to consider the submission of applications.</p> | |

| Impact on BSCCo | |
|-----------------|--|
| Area of ELEXON | Impact |
| ELEXON | <p>Implement the P362 legal text and CSDs. Implement products to operate the sandbox service:</p> <ul style="list-style-type: none">• Produce a suite of templates, such as impact and risk assessment templates.• Deliver local working instructions.• Produce guidance for applicants on the sandbox process.• Produce a sandbox webpage to provide an overview and support for applicants. <p>For the avoidance of doubt, ELEXON will not be permitted to apply for BSC derogations.</p> |

| Impact on BSC Systems and process | |
|-----------------------------------|---|
| BSC System/Process | Impact |
| All | No implementation impacts. However, the Modification Proposal will allow participants to suggest ideas that could impact BSC systems and processes. These impacts would be considered as part of the sandbox process on a case by case basis, and applications could be rejected on the basis of these impacts. |

| Impact on BSC Agent/service provider contractual arrangements | |
|---|--|
| BSC Agent/service provider contract | Impact |
| All | No implementation impacts. However, the Modification Proposal will allow participants to suggest ideas that could impact BSC Agents. These impacts would be considered as part of the sandbox process on a case by case basis, and applications could be rejected on the basis of these impacts. |

| Impact on Code | |
|----------------|---|
| CSD | Impact |
| Section B | Update to expand the role and function of the BSC Panel to include consideration of sandbox applications. |
| Section H | Update to include the sandbox provisions. |
| Section X | Update to include new defined terms. |

| Impact on Code Subsidiary Documents | |
|-------------------------------------|--------|
| CSD | Impact |
| None | - |

| Impact on other Configurable Items | |
|------------------------------------|--|
| Configurable Item | Impact |
| New – BSC Sandbox Procedure | A new BSC subsidiary document providing further detail on the BSC sandbox process and requirements. This will be added to the Baseline Statement and subject to the Change Proposal (CP) process – see Attachment D. |
| Guidance notes | New guidance notes to provide support for sandbox applicants. |

| Impact on Core Industry Documents and other documents | |
|---|--|
| Document | Impact |
| Ancillary Services Agreements | No direct impacts, although we understand that some codes may require changes to facilitate their own sandbox service. |
| Connection and Use of System Code | |
| Data Transfer Services Agreement | |
| Distribution Code | |
| Distribution Connection and Use of System Agreement | |

Impact on Core Industry Documents and other documents

| Document | Impact |
|---|--------|
| Grid Code | |
| Master Registration Agreement | |
| Supplemental Agreements | |
| System Operator-Transmission Owner Code | |
| Transmission Licence | |
| Use of Interconnector Agreement | |

Impact on a Significant Code Review (SCR) or other significant industry change projects

P362 has been exempted from existing SCRs by Ofgem.

Impact on Consumers

No implementation impacts identified.

Impact on Environment

No implementation impacts identified.

Recommended Implementation Date

The Workgroup and the Panel recommends an Implementation Date for P362 of:

- **Five Working Days after the Authority's decision.**

As this is a document only change, the Workgroup believe it is important to put in place the BSC sandbox service as soon as reasonably practicable. ELEXON will not receive applications directly from applicants. Rather, Ofgem will control the application rounds and when to pass applications onto ELEXON.

Responses to the Assessment Consultations

| Do you agree with the Workgroup's recommended implementation approach? | | | | |
|--|-----|----|--------------------|-------|
| | Yes | No | Neutral/No Comment | Other |
| First Consultation | 9 | 0 | 0 | 0 |
| Second Consultation | 7 | 0 | 0 | 0 |

All respondents to the first and second Assessment consultation agreed with the proposed implementation approach. All respondents, except one, reported that they did not require a lead time to implement. One respondent indicated that they require a one month lead time to communicate the change internally. The Workgroup noted that the same respondent had not indicated any impact or costs for implementing P362. They believed this to be excessive for internal communications and so kept the recommended implementation approach the same.

Cross-code working

The Workgroup highlighted that many innovative products or services would likely have cross-code impacts. Whilst some projects may only impact one code, they believed these would be the minority of cases. The Workgroup believed that the BSC sandbox would add the most value to industry if other codes had a sandbox service too. Ideally there would be a way to co-ordinate these sandboxes across the different electricity and gas codes, with a single point of entry for applicants. Many members believed Ofgem should be leading and co-ordinating applications across industry. The Workgroup views were consistent with those of the BSC Panel when the Initial Written Assessment was presented at the [November Panel meeting](#). The Workgroup were therefore pleased when Ofgem agreed to fulfil this role.

Ofgem are continuing to hold cross-code meetings to agree and put in place the cross-code arrangements. A member suggested that a cross-code group or the Code Administration Code of Practice (CACoP) group would be well placed to facilitate sandbox applications across-codes.

The role of Ofgem

It was not until after the first P362 Workgroup meeting (held on 13 December 2017) that Ofgem agreed to co-ordinate the sandbox user journey. Ofgem held a meeting with Code Administrators in January 2018 to seek support for industry sandboxes. Code Administrators agreed in principle to work with Ofgem on implementing industry sandboxes. Ofgem agreed to:

- Develop a single point of access, removing the need to apply to multiple codes;
- Operate a sifting process ahead of applications being forwarded to relevant parties; and
- Co-ordinate the feedback process for valid applications.

Existing Ofgem derogation powers

Some members believed that Ofgem should be raising BSC Modifications, using powers gained from [P351 'Align the BSC with changes to the SCR requirements'](#), to address any barriers in the market that it is aware of.

The Workgroup explored whether existing Ofgem powers would forgo the need for a BSC sandbox. [Electricity supply licence condition](#) 11.3 provides the Authority with the power to relieve a licensee of obligations (in whole or in part) under the BSC (and Master Registration Agreement (MRA), Distribution Connection and Use of System Agreement (DCUSA), Connection and Use of System Code (CUSC)). Similarly, [electricity generation licence conditions](#) 5.2 and 6.2 provide the Authority with the power to relieve a licensee of obligation in respect of parts of the Grid Code and Distribution Codes respectively.

For **licensees**, Ofgem could treat derogations against codes on a case by case basis after careful consideration of the evidence provided by the supplier or third parties. These powers can only apply to licensees, and therefore do not extend a solution to parties who are not required to be licensed (e.g. Party Agents, licence exempt generators and

Suppliers). Additionally one member believed that a BSC sandbox would ensure that the experts of the BSC, ELEXON and the Panel, were involved in the decision making process.

The Workgroup therefore agreed that it was still necessary to proceed with a process described in the BSC.

P362 Ofgem derogation powers

The Workgroup discussed whether Ofgem can remove conditions from recommended derogations, and agree to derogations which the BSC Panel has recommended be rejected. The Workgroup agreed that the BSC Panel is best placed to consider the risks and impacts with regards to Settlement but also acknowledged that Ofgem's ability to co-ordinate between Codes is diminished if they cannot make amendments for incompatible conditions. Additionally, Ofgem are able to make value judgements not obliged to the BSC Panel (e.g. benefit to consumers).

Three options were considered by the Workgroup:

1. Include provisions in the cross-code process for Ofgem to consult with Panel(s) when conditions are incompatible or subject to differing value judgement;
2. Include send-back provisions in BSC legal text to enable Ofgem to request Panel remove/alter conditions; or
3. Include provisions in the BSC removing the effect of any Ofgem decision to remove or alter a condition of derogation, or approving a recommendation to reject.

The Workgroup rejected option three as it would devalue the decision making role of Ofgem and could jeopardise coordination with other sandboxes. Legally the BSC cannot directly empower or restrict Ofgem, as it is not a Party. Moreover, the Workgroup supported Ofgem's role as a decision maker, but believed any reasons for the decision should be transparent. The Modification process has been used as a basis for the derogation process and option three would be inconsistent with this approach.

Under the Modification process, Ofgem cannot amend a solution. Where Ofgem want an amendment to the solution, they must send the Modification back to the Panel (as per [Section F2.7A](#)). A member believed the derogation process should follow a similar approach. If the Panel have set conditions to alleviate particular concerns or risks, any changes to these conditions could change the Panel's view. Where Ofgem wish to amend the conditions, the Panel should therefore re-evaluate the derogation and make a new set of recommendations to Ofgem.

A member did not believe this approach would reduce the ability of Ofgem to co-ordinate with other sandboxes. Rather it ensures the basis for any recommendations and decisions are robust and will stand up to judicial review. In addition, it was important for transparency and for industry to understand the basis on which decisions are made. The decision does not have to agree with the Panel, but they should have to consult the Panel on any changes to the conditions.

Ofgem commented that they fully support a collaborative approach with Code Administrators. They agreed they would need to evaluate the Panel's concerns and conditions and could not disregard them, but could disagree with them.

A member wondered if Ofgem sitting on the Panel could negate the need for option two and support option one instead. However, another Workgroup member highlighted that Ofgem does not vote at the Panel and would not be able to fetter its discretion or offer binding decisions at the Panel. The member commented that Ofgem attends the Panel to provide an important link back to decision makers at Ofgem by reporting back on the Panel discussions and providing appropriate updates to the Panel. In addition, the Ofgem representative would likely need to seek expertise from colleagues.

A member was concerned that the back and forth nature of option two may add time to the derogation process. The Workgroup considered hard coding a fixed response time for the Panel re-evaluating derogations. Where a fixed approach is taken, it may result in more 'no' decisions, as there may not have been time to sufficiently consider the derogation.

The Workgroup agreed instead to adopt a similar approach taken for Urgent Modifications. The Panel Chairman will decide whether an ad-hoc Panel meeting is required, having regard for the circumstances and request of the applicant.

The Workgroup agreed to progress with option two as the conditions set could have been fundamental to the Panel's recommendation. One member believed sending derogations back should be the exception and could be further reduced by building robust cross-code processes. The Workgroup believed option two gave the right balance between transparency, protection for Parties and supporting innovators. They agreed that Ofgem have the final decision.

Responses to the first Assessment Consultation

| Do you agree with the send back provisions? | | | |
|---|----|--------------------|-------|
| Yes | No | Neutral/No Comment | Other |
| 9 | 0 | 0 | 0 |

The Workgroup noted that all nine respondents agreed with the send back provisions.

The Workgroup discussed whether the wording of the send back provision in the draft legal text was too specific. The drafting in H10.3 allows Ofgem to direct the Panel where it is unable to form an opinion in relation to a Sandbox Report. Concern was raised that the condition to send back when 'unable to form an opinion' may be too narrow. There may be circumstances where Ofgem are able to form a view but still require further information.

The Workgroup noted that the current wording is based on the Modification Send Back provisions (Section F2.7A) and that this had not experienced any issues in practice. A member also commented that the Panel would be very unlikely to question or refuse an Ofgem request for further information. The Workgroup supported the view that requiring further information should be taken to mean that a view has not been formed.

The BSC Sandbox Process

The Workgroup believed that a key success criterion for P362 would be that the sandbox process is quicker and less burdensome than the Modifications process to enable ideas to be tested and brought to market.

Strong concerns were initially raised about the appropriateness of BSC Parties funding the sandbox service. The concerns focussed on ELEXON spending Parties' money to progress non-Parties applications and on funding research and development of other Parties. There was a concern that the nature of trialling innovative ideas is that most of them will fail, so why should Parties money be used to fund something that does not work. These concerns were alleviated by clarifying the intention of P362 and in the design of P362, as elaborated on below.

Contrary views were also expressed by the Workgroup. Successful trials should result in BSC Modifications that will remove barriers and bring opportunities to all Parties. ELEXON believed any support provided prior to the applicant becoming a Party was comparable to the [market entry service](#). ELEXON already provides guidance to potential Parties looking to enter the market, including some that have applied to Ofgem's sandbox.

ELEXON expects to resource the sandbox service using existing resource. Successful applicants will need to accede to the Code (if they are not already a Party) and so should be entitled to the normal BSC services at that point. The Workgroup believed it to be important for ELEXON to be transparent about how it was funding the sandbox service. One Workgroup member did not believe it appropriate for ELEXON to be ramping up resources to operate the sandbox service. ELEXON agreed to provide details of sandbox service in its annual BSCCo Business Plan.

ELEXON confirmed that the sandbox is not appropriate for trialling unproven technology, large scale products or services that would be better facilitated via a Modification, or products or services that would not provide any benefits to the wider industry. The application should demonstrate how it will provide benefits to the wider industry and if it cannot, it should be rejected. Any applications posing significant risk to Settlement should be rejected. The scale of the derogation should be constrained to mitigate risk to Settlement and kept at a level needed to test the idea but not to scale it. The Workgroup acknowledged that successful applicants would get a first mover advantage, but should not be making significant commercial gains as a result.

The derogation should apply only to pre-competitive products and services that would not be cost-effective to trial otherwise. Whilst the BSC change process allows for different options and solutions to be considered, it does not allow for these different options to be tested in the live market environment. The sandbox service will provide real life data and evidence to support decision making and is inherently more powerful than a paper based assessment. It was suggested that a halfway house, between paper based and real market testing, would be for a virtual test environment to be available to Parties. ELEXON agreed this could bring many benefits, and should be re-considered following the planned architectural changes to BSC central systems. ELEXON also noted that there is always a difference between a test environment and a live environment.

The Workgroup noted that it would be helpful if there were an example project for how a derogation might be applied. The solution was developed without consideration of any specific derogation that might be requested by an applicant.

Charges to applicants and Derogated Parties

Application fee

There was some concern raised around the volume of additional work the sandbox service may require from ELEXON. The Workgroup agreed that the solution should allow for the Panel to set an application fee. This would deter speculative applications. ELEXON

confirmed that the fee could not be a BSC Section D Charge as these charges applied only to BSC Parties. As non-Parties can apply to the sandbox, Section D charging was not appropriate. The fee would defray BSC Costs for Parties.

The Workgroup noted that they would expect the fee to be set at zero initially and only increased if the volume of work exceeded that expressed in the ELEXON business plan. Innovators within the Workgroup were content with this approach, on the basis that the fee would be fixed and known upfront so that it could be factored into business plans and costs.

The Workgroup also discussed removing the fee, given that Ofgem would act as the 'gate keeper' for applications, which should result in fewer applications reaching ELEXON. However, they agreed to keep the fee, as it would enable ELEXON to recover some costs if the volume of work became more significant and built flexibility into the solution. ELEXON agreed with the Workgroup that the fee should be published and easy to find on the BSC Website.

Additional fees

The Workgroup agreed that ELEXON should be able to charge a Derogated Party additional fees associated with the administration of the derogation, if applicable. The charges should be agreed as part of the application process, so that it is clear to the Party what they will be expected to pay and when. For example, if the derogation requires ELEXON to operate a workaround, the Workgroup believed it reasonable for the Derogated Party to pay for this. Furthermore, they agreed any extensions to the Trial or Transition Period could result in an extension to recovery of these costs also.

The Derogation Period

The Workgroup felt strongly that derogation should be for a limited period of time and should not be subject to continuous extensions as is the case for Metering Dispensations. The purpose of the sandbox derogation is to test and trial products or services. It is not intended to put in place a permanent arrangement that would give individual Parties special benefits and exemptions to rules that everyone else is expected to adhere to.

The maximum Derogation Period

The Workgroup discussed the maximum period needed to trial the product or service ('the Derogation Period'). Many members shared the view that most products or services should get the data they need within six to 12 months to prove the concept. One member highlighted that if the project involved trialling solar technology you may need two summer seasons of data. The Workgroup therefore agreed that no more than **two years** should be needed to trial the product or service.

Transition vs. Derogation Period

A member suggested that it would be unreasonable for a Derogated Party to be required to exit the sandbox if they were trying to put in place permanent arrangements via a BSC Modification or if the Modification is delayed. If a Party is forced to exit, they may lose financial backing and no longer be able to operate. A member therefore suggested that a

'transition period', in addition to the Derogation Period, should be created to allow the Party time to put in place the enduring arrangements.

The Workgroup considered allowing the transition period to be open until the Modification was implemented, rejected or withdrawn, at which time the Derogation Period would be triggered, if needed. However, many members felt uneasy about this prospect as it could result in prolonged derogations. It may even be in the Derogated Party's interest to drag the Modification process out. The Workgroup identified the following solution requirements for this area:

- Parties should be incentivised to raise Modifications in a timely manner;
- Parties should not be given an unfair advantage from having an extended derogation;
- An extension should not increase the risk to Settlement or Parties; and
- Extensions should not be able to be continually extended.

The Workgroup believed so long as the transition period did not allow the Party to extend its scope or scale of operation, and the risk and impact to Settlement and Parties remained acceptable, then it was reasonable to allow the transition period to be extended to allow for Modifications to be put in place. Any payment of costs agreed as part of the application, may be continued to cover the extension.

A member suggested that three years should be plenty of time to trial the product or service and put in place a Modification. The Workgroup agreed a **three year** maximum for both the trial and transition period would meet the solution requirements listed above. The three year period should be subject to a Modification being raised (and not implemented, rejected or withdrawn) during the Derogation Period. A member commented that if more than three years was required to test an innovative product and service and put new arrangements in place, then the sandbox process is probably not the appropriate mechanism. A **Derogation Period** is the trial and transition period together.

The Workgroup also believed the maximum trial and Derogation Period should be placed in the BSC and not a CSD. Given the critical nature of this aspect, the Workgroup agreed to seek industry views on this proposal.

Minimum Derogation Period

The Workgroup wondered whether there should be a minimum Derogation Period to avoid frivolous or gaming behaviour, such as seeking a derogation to get an advantage from not having to comply with the normal rules. However, the Workgroup were satisfied that this would likely be identified and rejected as part of the process and could be dealt with if it happened.

Conditional start dates

The Workgroup discussed when derogation should start. They agreed that the Panel should be able to set a conditional start date, for example the derogation must start between 'x' and 'y', for a period of 'z' months. One member commented that contingency should be built into the plans by applicants. Another member suggested that a date could be agreed in principle and finalised in a meeting.

Extensions

The Workgroup considered the circumstances that might justify an extension to a Derogation Period, such as illness or significant technical failures (e.g. fire). One member suggested that allowing for extensions sent the wrong message, but accepted there may be a need for it. If a new barrier emerged, the Workgroup believed this should require a new derogation and this was not a valid reason to request an extension. A new barrier requires a new derogation. The Workgroup agreed that extensions could be sought for the Derogation Period, up to the maximum two years, and for the transition period, up to the maximum 3 years. Ofgem could direct these extensions, or preferably, the Derogated Party would request the extension, providing justification, and the Panel would make a recommendation to Ofgem whether to extend the derogation or not.

Responses to the first Assessment Consultation

| Do you agree with the Workgroup's proposal for a maximum two year trial period and a maximum three year derogation period if an associated | | | |
|--|----|--------------------|-------|
| Yes | No | Neutral/No Comment | Other |
| 8 | 1 | 0 | 0 |

The Workgroup noted that in response to this question, eight respondents to the consultation agreed and one disagreed.

The Workgroup discussed the one respondent who disagreed and who wanted a two year Derogation Period. The Workgroup believed the current approach was fairer as some projects may require two seasons of the same type (e.g. two summers) to trial the product or service. The Workgroup therefore decided to not to change the Derogation Period. More generally, respondents put forward views for and against changing the Derogation Period. These views echoed discussions previously held and considered by the Workgroup.

Criteria

The Workgroup believed that adopting Ofgem's eligibility criteria would be sensible. However, this was determined to be redundant after Ofgem agreed to act as the point of entry, on the assumption they would only pass on applications to ELEXON that met their eligibility criteria, which are:

1. **Innovation:** The proposition must be ground-breaking or significantly different to what is currently in the market. It could include either technological or business model innovation.
2. **Consumer benefit:** It should be clear how the proposition would benefit consumers. This could be, for example, because it would lead to direct benefits such as lower energy bills or better customer service, or indirect benefits such as increased competition in the market.
3. **Background research:** You should have researched the concept and be able to show that you have attempted to find out about the regulatory implications.
4. **Need for support:** The Innovation Link provides information on the regulation in the energy sector. It does not provide business advice on the commercial viability of a project. You should be able to tell us why you need Link support. For

example, what it is that you wish to understand from a regulatory perspective or how you think Link support would benefit you.

The Workgroup were quick to agree that all applications would need to demonstrate that they better facilitate the Applicable BSC Objectives as these are the basis on which changes to the BSC are made.

Some members, more familiar with the Panel, believed the Panel's assessment of applications should be similar to Modifications. The Panel would need to take a balanced view, including short and long term impacts, which may differ, and be able to defer its decision if they require further information to inform its decision. The Workgroup concluded that the Panel should have broad discretion to make its decisions on a case by case basis.

The Workgroup discussed the extent to which compliance with other codes and licences should impact the Panel's decision. ELEXON's legal counsel confirmed that the Panel could only make recommendations for BSC derogations. It is not the role of ELEXON or the Panel to consider compliance with anything other than the BSC. However, the Workgroup believed that if ELEXON or the Panel were aware that consideration of other codes and licences was required this should be flagged in the Panel report to Ofgem. ELEXON agreed with this approach.

The Workgroup considered requiring the applicant to provide a self-declaration of compliance statement signed by a director. However, this was rejected once Ofgem agreed to act as the 'gate keeper' for applications, noting that the responsibility to ensure compliance lies wholly with the applicant.

Consider totality

The Workgroup believed that, in order to protect the integrity of Settlement, the Panel should consider the totality of derogations. For example, the risk posed by one application that impacts 1000 MSIDs may be acceptable, but the risk posed by a second application with an additional 1000 MSIDs may not be acceptable.

The Workgroup noted that Ofgem would need to carefully consider how it would handle applications to ensure it treated them fairly. For example, is a simple first in first out the right approach, or would a 'currency pool' of risk be more appropriate?

Subsidiary document

The Workgroup were of the view that a subsidiary document would be required to detail further eligibility criteria and considerations. This approach was seen to offer a more efficient way to maintain the provisions, rather than including the text in the BSC. However, the Workgroup believed associated procedures did not need to be under change control, but instead could be published on the BSC Website, if needed. ELEXON noted this was less likely now Ofgem were leading the process.

The Workgroup believed that key parts of the subsidiary document should be available as part of the Assessment Procedure Consultation to provide comfort to Parties on how the process would work. Attachment D contains the draft subsidiary document.

Responses to the first Assessment Consultation

| Do you agree with the content of Attachment D, with specific consideration of the application approach, eligibility criteria and monitoring approach | | | |
|--|----|--------------------|-------|
| Yes | No | Neutral/No Comment | Other |
| 8 | 0 | 0 | 1 |

As part of the Assessment Procedure Consultation, respondents were asked whether they agreed with the draft subsidiary document. Eight respondents agreed and one commented they had not reviewed the document.

Risks

One Workgroup member commented that the purpose of the BSC is to ensure volumes and funds are allocated and settled accurately, equitably and efficiently. Any derogation that allows participants to side step this principal or undermines it should not be acceptable.

Another Workgroup member was concerned that there was a risk that new BSC Parties with limited experience are more likely to mismanage their trading positions, resulting in them going bust and abandoning customers. Any financial defaults will have to be paid for by BSC Parties.

One member suggested that applicants should provide some working capital to cover any costs incurred in the event of failure or issues. However, this was seen to be overly complex. Furthermore, Parties requirements to lodge Credit Cover for Trading Charges should not be derogated.

Any risks should relate to the derogation and not to the technology. Only projects with sufficiently mature (field ready, not lab ready) technology and products should be allowed to participate.

The Workgroup agreed that constraining the scope of the application in terms of time and scale will help reduce the risk and impact. The applicant and ELEXON should be required to conduct risk assessments for each application and present the findings to the Panel and Ofgem.

Impacts

Derogations should not adversely impact Parties or Settlement. The Workgroup agreed that ELEXON must conduct an impact assessment, supported by the applicant. There may be impacts or operating models that ELEXON is not aware of in the industry. There may also be cases where the industry is already trialling the idea in compliance with the Code, which ELEXON is not aware of. These can only be identified by asking industry. This will help ensure the idea is truly innovative.

The Workgroup therefore agreed that ELEXON must consult industry. The consultation will increase the chances of identifying all likely impacts and better inform the Panel and Ofgem in its decision making.

The Workgroup discussed how long the consultation should be for. They recognised that different organisations will require different timescales. They did not believe any more

than 15 Working Days should be needed, but thought less than 10 Working Days may not be enough.

The Workgroup believed it important for ELEXON to conduct its own impact assessment. This will form the basis for the industry consultation. The Workgroup and ELEXON believed transparency was an important design principle to ensure trust in the process. It was agreed that all consultation responses will be published, save for any redactions for confidential information. The impact assessment responses and ELEXON's action in regard to any response will be included in the report to the Panel and Ofgem to maintain the history of the impacts identified. This approach is similar to that taken for BSC Modifications.

Who should be able to participate?

One Workgroup member believed the need for a sandbox was exacerbated because non-parties were not able to raise Modifications without Ofgem designation. ELEXON pointed out that the sandbox service was designed for testing pre-competitive and innovative products or services that met a given set of criteria. It is not appropriate to compare the Modification and sandbox services. Moreover, non-Parties would be able to apply to Ofgem for derogation. If derogated they could raise a consequential Modification to address the barrier being faced.

Only Parties can be derogated – you cannot be derogated against a code you are not a party to. Therefore, if a non-Party applies to enter the sandbox, they would need to accede to the Code before the derogation became effective. It was noted that the derogation could include provisions related to Market Entry and Qualification. For example, if they needed to accede as a Supplier, but did not need to carry out the majority of the Supplier functions, they could seek derogation for those areas too.

The Workgroup agreed with ELEXON that BSCCo should not be able to apply for derogation. The Workgroup also believe the TC² should not be permitted to apply for derogation. The Workgroup initially believed it would be inappropriate for these organisations to seek derogation from rules that they are bound to administer. In response to the first Assessment Consultation the Workgroup reviewed these restrictions. These discussions are captured in the alternative solution discussions below, and an alternative solution was proposed to enable the TC to apply for derogation.

The Workgroup agreed that multiple Parties can be linked with derogation. For example, two Parties may be in a partnership, with both providing different functions that require derogation. Both Parties could therefore be derogated.

What can be subject to BSC derogation?

The Workgroup agreed that the following should not be eligible for derogation:

- The Electricity Market Reform (EMR) provisions protected in BSC Section F1.1.9;
- The European Union law provisions; and
- The sandbox provisions.

² This includes National Grid as Electricity System Operator, but excludes its Interconnector businesses.

The Workgroup was concerned that any provisions related to requirements that have originated from outside the BSC, such as EMR legislation and European Network Codes that have a higher legal standing, should be protected. In addition, the Secretary of State has powers of veto for the EMR provisions. The Workgroup was concerned that unless the EMR provisions were protected, there was a risk these powers of veto may be evoked, increasing the risk that P362 is rejected. The EU law provisions in the P362 draft legal text have been drafted so as to work following Brexit.

ELEXON clarified that the existing provisions around indemnity and the ability to claim damages and other liabilities against the Panel and ELEXON would apply. Any support provided by ELEXON could not be considered legal advice. However, ELEXON would play the 'critical friend' role with applicants and Derogated Parties.

The Workgroup discussed how a Derogated Party's responsibility for reconciliations should be treated. The Workgroup believe that there are certain areas and principles of the BSC that cannot be derogated in practice, such as the requirements to register Metering Systems or pay Settlement and trading charges.

The Workgroup believed that Settlement Reconciliations would be one such area. One member suggested that a Derogated Party could arrange for responsibility for reconciliations to be passed to another Party or for sufficient credit cover to be lodged to cover any shortfalls following a subsequent reconciliation.

The Workgroup believed it would be important to include some guidance for applicants on what would likely be unacceptable risk to Settlement. They noted that as applications are progressed, knowledge of the areas less and more likely to be derogated would be learnt. Attachment D contains some areas that ELEXON initially believes would likely result in unacceptable risks to Settlement.

Transition Plan

The Workgroup agreed that the Party should request a Derogation Period as part of its application. This plan must detail how they will exit the sandbox and return to its previous state. The plan will automatically be applied at the end of the Trial Period, unless the derogated period has been extended, either for exceptional circumstances or for allowing a Modification to be put into place. The Party may also choose to exit early. The Panel (or Ofgem) may also trigger the plan. For example, if the derogation has an unexpected material impact on Settlement, the derogation may be withdrawn.

Panel Role

The Workgroup discussed how the Panel voting should work. They considered the existing voting rules in BSC Section B, the voting rules used for Modifications or requiring a unanimous decision.

The current derogation provisions in the BSC, such as for Metering Dispensations, require a unanimous decision. These decisions are made by the ISG and Supplier Volume Allocation Group (SVG), where all decisions are required to be made by a unanimous vote of members. The only other unanimous voting in the BSC is required for Fast Track Self-Governance Modification Proposals considered by the Panel. All other Panel decisions (including Modifications), and those of the Performance Assurance Board (PAB) and Trading Disputes Committee (TDC) are made by simple majority voting.

The Workgroup believed that a unanimous decision would have been more appropriate if the Panel were the decision maker. Conversely, if they are making a recommendation, or there is a route for appeal, a simple majority would be better suited.

The Workgroup supported Ofgem being the decision maker, as this was seen to be the most efficient way for cross-code decisions to be made. The Workgroup discussed alternatives to Panel making recommendations to Ofgem, such as the Panel deciding, with the Party having a right to appeal to Ofgem. Any self-governance type concepts were seen to be adding unnecessary complexity.

Given that the Panel are making recommendations to Ofgem and are not deciding whether to derogate, the Workgroup believed that unanimous voting would be too restrictive and decided to adopt the general voting provisions in BSC Section B. The Workgroup did not believe the Modification voting provisions added any value; rather they were overly restrictive (requiring meetings to be held in person) and therefore should not be adopted.

Reporting and monitoring

The Workgroup believed that applicants would require support from ELEXON and Ofgem to understand the type and level of detail required to be reported on. The Workgroup reiterated the importance of transparency and reporting meaningful information that would be of benefit for other Parties, without exposing commercially sensitive or intellectual property information. A member commented that innovators are often keen to share their experiences and learn from one another and this should be the ethos for the reporting and monitoring of BSC derogations.

A Workgroup member believed that the project outcomes should be known and defined up front. Key milestones should be identified and these could form the basis to report against. Other areas the Workgroup expected to be reported against were any impacts on Settlement and key learnings. The Workgroup agreed that the Derogated Party should be required to report back to ELEXON, who would publish the update, save for any redactions for confidentiality reasons. In practice the Party may only need to report once, to Ofgem, and copy the relevant codes in.

The Workgroup also agreed that ELEXON should report to the Panel periodically on the sandbox service, in a lessons learned report. This should also be published and may lead to changes to the process.

New Party Role

A Workgroup member wondered if a new Party role would help make the process more efficient, such as a 'sandbox role'. ELEXON noted that they are aware Ofgem is considering moving the market away from roles and towards functions. One benefit of the new role would be to allow Parties to enter and exit more quickly. However, the Workgroup believed that the derogation process should inform what a new role or function may need to look like and would be best addressed in a subsequent Modification.

Further considerations

A member brought to the attention of the Workgroup a set of legal questions that a CUSC Panel Member had raised. The Workgroup noted that the key take away for P362 was that any BSC derogations would be to avoid creating distortions or impacting other schemes

and laws, such as EU State Aid. The Panel would need to keep in mind these areas when considering whether to recommend derogation or not.

Appendix 4 contains the questions and Ofgem's response to these.

BSC Legal Text

Responses to the first Assessment Consultation

| Do you agree with the Workgroup that the draft legal text in Attachment A delivers the intention of P362? | | | |
|---|----|--------------------|-------|
| Yes | No | Neutral/No Comment | Other |
| 8 | 0 | 0 | 1 |

Eight of the respondents to the first Assessment Consultation agreed that the draft legal text for the original proposed solution delivers the intention of P362. The ninth respondent believed the legal text broadly achieved the intentions set out in the first Assessment Consultation report, but had several comments, which are discussed further below.

Appeals Process

A respondent suggested that there should be an appeals process, similar to the Modifications Procedures. Under the Modifications process a Party may challenge an Authority decision either via Judicial Review or appealing the decision under the Energy Act. The existing provisions in the Energy Act were not written with the BSC Sandbox process in mind and so a legislative change may be required to extend to the scope to cover BSC Derogations.

The Workgroup did not believe that creating a new codified appeals process for BSC Derogations was worthwhile or necessary. The Workgroup however, did note that Ofgem are leading the sandbox process and deciding whether to approve or reject Applications. They therefore believed an appeals process was something that Ofgem should carefully consider.

Sandbox definition

A respondent suggested that the term Sandbox does not convey useful meaning, and could overlap with the use of the term by Ofgem. He suggested that the term 'BSC Derogation Applications' and 'BSC Derogations' would suffice and would be more meaningful. The Workgroup emphasised that this overlap was deliberate as they wanted to be clear that the BSC Sandbox Process links to the Ofgem sandbox process. It was also noted that the most important thing was that the term was clearly defined, which it is.

Should distributors be able to apply for BSC Derogation?

A respondent also suggested that distribution companies' ability to apply for BSC Derogations should also be limited. The rationale given was this would prevent companies creating changes to the codes they administer. He was concerned that as some distribution companies are also Code Administrators, as well as being BSC Parties, they

should not be permitted to trial new products or services, as it was not their money to spend. The Workgroup believed that as distributors are BSC Parties, with specific functions, which do not include code administration, there was not an issue with distributors applying for BSC Derogations. Moreover, distributors may be able to bring benefits to industry by trialling innovative products or services.

Other minor legal text changes

The Workgroup also agreed to make the changes captured at the start of section 3 above. The Workgroup believed these changes, suggested by respondents, whilst not strictly necessary, would clarify and tighten the existing solution.

The Workgroup believed a withdrawal provision would add clarity to the process. Where an Applicant wanted to withdraw its Application, any Application Fees should still be paid.

The original drafting of H10.2.2 allowed BSCCo and the Panel to not take any steps at all for Applications. The intent of this provision was to allow ELEXON and the Panel to control the amount of time and effort spent on the Sandbox process, protecting Parties from excessive costs in this area. However, the Workgroup agreed with a respondent that BSCCo and the Panel should be required to deal with Applications in some way, rather than not being obliged to take any steps at all (as per H10.2.2). The Panel would maintain its ability to prioritise Applications, if necessary, which would maintain the original intent of this provision.

The Workgroup also considered and dismissed the following suggestions:

- The Workgroup did not believe it appropriate for the Panel to explicitly be required to consider cross-code issues and impacts (suggested update to H10.2.4). ELEXON confirmed it would include any identified cross-code impacts in the Sandbox Report, as is the case for Modifications. The Workgroup did not believe it appropriate to oblige the Panel to consider impacts on other codes as its remit was the BSC. The Workgroup noted that cross-code impacts was a key role for Ofgem as the industry sandbox co-ordinator;
- It was suggested that BSCCo should inform the Applicant of any send back as soon as it becomes aware (suggested update to H10.3.2). The Workgroup believed this was a role for Ofgem, as they are the primary point of contact for the Applicant and will make any send back decisions. ELEXON confirmed it was likely to do this in practice anyway;
- It was suggested that there was overlap between H10.3.4 and H10.3.6. ELEXON and the Workgroup were content that there was no overlap; and
- H10.7.3 – it was suggested that Ofgem should always be informed where a BSC Derogation may no longer meet the Eligibility Criteria, and not just where Panel considers that a BSC Derogation no longer meets the Eligibility Criteria. The Workgroup dismissed this suggestion as Ofgem sit on the Panel and so will always be informed of these instances.

Responses to the second Assessment Consultation

Do you agree with the Workgroup that the draft legal text in Attachment A and B delivers the intention of P362 Proposed and Alternative solution respectively?

| Yes | No | Neutral/No Comment | Other |
|-----|----|--------------------|-------|
| 7 | 0 | 0 | 0 |

All respondents to the second Assessment Consultation agreed that the draft legal text delivers the intention of P362 Proposed and Alternative Modifications. There were no suggestions to amend the legal text.

Alternative Solutions proposed by respondents to the first Assessment Procedure Consultation

Do you agree with the Workgroup that there are no other potential Alternative Modifications within the scope of P362 which would better

| Yes | No | Neutral/No Comment | Other |
|-----|----|--------------------|-------|
| 6 | 2 | 0 | 1 |

Two respondents to the first Assessment Consultation believed there were alternative solutions that should be considered. One respondent who marked their response as 'other', also proposed an alternative solution. The remaining six respondents did not identify any alternatives.

One respondent suggested that Applications could be assessed by an industry workgroup, but acknowledged that this would require more time and effort from ELEXON and industry and may not be aligned with the intent of the Sandbox process. The Workgroup agreed that this approach was not in the spirit of an agile process designed to support innovation.

One respondent suggested that the option to extend the derogation through the Transition Period could be removed. The Workgroup did not believe this would be fair to the Derogated Party, as they may not be able to raise a Modification until sufficient data had been collected from the trial, which may not occur until near the end of the trial.

Should the TC and BSCCo be able to apply for BSC Derogation?

A respondent to the first Assessment Procedure consultation believed a solution in which the TC could be granted BSC Derogations would better facilitate Applicable BSC Objective (c), competition, as compared to a solution where they could not. The respondent put forward two arguments:

1. There is a risk that a BSC Sandbox Application may require a consequential derogation by the TC; and
2. Exclusions of the TC might be an unnecessary barrier to innovation.

As such, the respondent argued that the proposed solution was overly restrictive and that there were already appropriate controls in place, such as the TC being unable to vote on the merits of the Application at Panel or make decisions on Applications. The TC is being

asked to do more by industry and so it should not be restricted from trialling ideas that could provide benefits to the wider industry.

The same arguments were put forward by the respondent in relation to BSCCo. However, ELEXON and the Workgroup felt strongly that it would be inappropriate for BSCCo to seek BSC Derogations, as the entity responsible for the implementation of the BSC. It was suggested that BSCCo would be very unlikely to need a consequential derogation. If a Derogated Party was derogated from certain BSC obligations, ELEXON would not be in breach of the BSC by giving effect to that derogation.

The Workgroup voted on the proposal to allow the TC to apply for and be granted a BSC Derogation:

- Four members believed the alternative solution would better facilitate Applicable BSC Objective (c), compared to the original solution, as it could allow the TC to trial or facilitate innovative products or services which could improve competition.
- Three members believed the original proposal was better than the alternative as it was inappropriate for the TC, which is responsible for establishing the BSC under its Transmission Licence condition, to seek BSC Derogations. One member noted that following the planned separation between the Electricity System Operator and the Electricity Transmission Owner, his view may change.

The Workgroup therefore formally raised an Alternative Modification, as the **majority** believed it was better than the Proposed Modification.

The Workgroup noted that Ofgem would need to be particularly cautious in considering Applications from monopolies, such as the TC.

Responses to the second Assessment Consultation

| Do you agree with the Workgroup that there are no other potential Alternative Modifications within the scope of P362 which would better | | | |
|---|----|--------------------|-------|
| Yes | No | Neutral/No Comment | Other |
| 6 | 1 | 0 | 0 |

No new suggestions were put forward in response to the second Assessment Consultation. One respondent suggested, as they did in the first Assessment Consultation, that the option to extend the Derogation Period beyond two years could be removed.

Further comments from respondents to the Assessment Procedure Consultations

| Do you have any further comments on P362? | | |
|---|-----|----|
| | Yes | No |
| First Consultation | 3 | 6 |
| Second Consultation | 3 | 4 |

First Assessment Consultation

Three respondents provided further comments in the first Assessment Consultation. The remaining six respondents did not provide any further comments.

A respondent believed further obligations should be included to require ELEXON to report on its costs of operating the sandbox service. The Workgroup agreed, as this is something they understood ELEXON would be doing anyway. They also agreed to require the 'lessons learnt' report (see H10.8.1) at least annually.

A number of further comments were made by respondents, which have been clarified with the respondents and the Workgroup and did not require any further actions.

Second Assessment Consultation

Three respondents provided further comments to the second Assessment Consultation. One suggested that without actual examples of derogations, P362 is a best guess and may need to evolve over time. However, they noted that the protections for BSC Parties seem robust.

One respondent believed it important for Applicants to clearly define the success criteria for the derogation, as well as the minimum scope, for consideration by the Panel. This should include the benefits to other industry participants and how it will remove barriers and bring opportunities to all BSC Parties. The Workgroup noted Ofgem's eligibility criteria would cover these last two items and that the criteria detailed in the new BSC subsidiary document (see Attachment D), together with the ability for the Panel to set conditions for BSC Derogations should provide the Panel with the sufficient tools to manage Applications.

Lastly, one respondent had reservations about the Alternative Proposal, until the Electricity System Operator and the Electricity Transmission Owner separation activity has completed, which is currently scheduled for 1 April 2019. The Workgroup was unsure how the separation would alleviate any concerns around the appropriateness of the TC to get BSC Derogations, as the obligation to establish a BSCCo will be transferred from one legal entity to a new legal entity. The Workgroup agreed this did not have any bearing on the P362 deliberations.

The separation would mean that National Grid Electricity Transmission Limited (NGET) will maintain the Transmission Owner role, whilst the ESO role will be transferred to National Grid Electricity System Operator (NGESO). As such, NGET Electricity Transmission Owner will be that same as any other Electricity Transmission Owner in respect of the BSC. The Workgroup noted that Electricity Transmission Owners are not a Party to the BSC.

Workgroup discussions on respondent's views against the Applicable BSC Objectives

Does the Alternative Modification better facilitate Applicable BSC Objective (b)?

A respondent to the second Assessment Consultation commented that they were not convinced that allowing the TC to apply for Derogations will allow for a more efficient operation of the electricity Transmission System, as there is no evidence to support this claim. One Workgroup member stated that, in principle, they could see how Objective (b) could possibly be facilitated, but did not believe there would be direct benefits and it would depend on a case by case basis for each application (second order effect) and

hence remained neutral. The Workgroup member who supported Objective (b) clarified that they foresaw examples, which could for example, reduce the cost of balancing via new balancing products and could therefore facilitate Applicable BSC Objective (b). They wanted to 'leave the door' open for these opportunities. A third work group member stated that they did not believe Applicable BSC Objective (b) was facilitated and so should – in their view – remain neutral.

Should monopolies be able to apply for BSC Derogations?

Two respondents to the second Assessment Consultation raised concerns around monopolies, such as the TC, raising BSC Derogations. One respondent commented that "Ofgem would need to be particularly cautious in considering Applications from monopoly companies, this is to ensure a level-playing field for all market participants." A member commented that you cannot create BSC legal text requiring Ofgem to be cautious, although they agreed with the comment. Another respondent believed that applications from the TC must have greater transparency.

The Workgroup discussed whether the TC should be required to disclose all information. The legal text allows for information, at the request of the Derogated Party, to be redacted from the reports required to be provided by a Derogated Party. The reporting requirements will be detailed in the Sandbox Report (see Section H10.7.2 in the draft legal text). ELEXON reminded the Workgroup that information would not be withheld from BSCCo and can be anonymised, if needed.

One view given was that the TC and Distribution companies should not be permitted to redact information, save for general law provision, such as data protection laws. They should be required to publish all information as required by the Sandbox Report that they are legally allowed to. As these companies are using public money and have a monopoly status, any Derogation must be for the benefit of all and should not withhold information that gives individual companies a competitive advantage. The rules around transparency for the [Network Innovation Competition](#) / [Network Innovation Allowance](#) and [Low Carbon Networks Fund](#) were highlighted for comparison.

A contrasting view was that requiring transparency on all cases may increase costs, if the data is costly to collect and report, and could act as a barrier to seeking a Derogation. This could be seen as an unnecessary barrier. Further the existing criteria and the ability for the Panel to set conditions was seen to be robust and sufficient in setting reporting requirements.

The Workgroup voted on whether to amend the legal text in Section H10.7.2 to exempt the TC and Distribution companies from being able to request information is redacted. The majority rejected this proposal.

The Workgroup agreed that the new subsidiary document, 'the BSC Sandbox Procedure', should be updated to make clear that the BSC Sandbox Application Report will be published on BSCCo's website. Redactions will only be made in exceptional circumstances, in accordance with the Code or another legal requirement.

7 Workgroup's Conclusions

The Workgroup provided its views on both the P362 Proposed and Alternative Modifications against the Applicable BSC Objectives. The **majority** of the Workgroup believes that P362 **Alternative** Modification would overall better facilitate the Applicable BSC Objectives compared with both the existing baseline and Proposed Modification and so should be approved.

This is in relation to BSC Objective (c) and (d), as the majority of the Workgroup believes that allowing the TC to be granted BSC Derogations will be better for competition as it is less restrictive than the Proposed Modification and so has a greater chance of enabling more innovative products and service to be trialled. Furthermore, by negating the need for future Modifications to enable small scale product tests with no material impact on the rest of the industry, ELEXON and industry resource can be focussed elsewhere and the trials should lead to more efficient Modifications.

One member also believed that Applicable BSC Objective (b) was better facilitated under the Alternative but not the Proposed as the innovative products or services that the TC could trial could lead to the implementation of products or services that result in a more efficient operation of the electricity transmission system. The member recognised that this was a potential to better facilitate Applicable BSC Objective (b) rather than an immediate benefit.

However, those members who believed the Proposed was better than the Alternative believed that it was not appropriate, given the governance arrangements, for the TC to get BSC Derogations. One member believed this was detrimental against Applicable BSC Objective (c) as the conflicts of interest had the potential to harm competition by giving unfair advantages to any companies working with the TC's trial. Another member did not believe allowing the TC to be granted BSC Derogation would improve competition as they did not believe it would be necessary.

P362 was raised by the Panel (in accordance with Section F2.1.1(d)(i)), who appointed a BSCCo representative as the Proposer's representative. In this circumstance, the Proposer's representative is not allowed to vote (see Section F2.4.5C). We have captured the Proposer's views against the Applicable BSC Objectives, but these views are not counted.

Applicable BSC Objective (b)

The Proposer and the **majority** of the Workgroup are **neutral** against Applicable BSC Objective (b). The minority of the Workgroup believes that P362 Alternative Modification would better facilitate Applicable BSC Objective (b) as it allows for the TC to trial new ways of doing things that could lead to the implementation of products or services that allow for a more efficient operation of the electricity transmission system.

Applicable BSC Objective (c)

The **Proposer** and the **majority** of the Workgroup **agree** that P362 **would** better facilitate Applicable BSC Objective (c) as it will enable the trialling of innovative ideas and for more companies to offer alternative solutions to consumers, and therefore increase competition.

By enabling innovative businesses to test their new products and ways of working, P362 makes it possible to introduce more disruptions to the existing ways of doing business. Greater numbers of firms offering greater numbers of alternative solutions will provide consumers with more choice as a result of an increased competitive market.

The industry is rapidly changing and P362 will help to foster an environment to support this rapid change. By sharing lessons learned, the whole industry can benefit. P362 will encourage new ideas to be brought forward and encourage innovators to enter a market which is perceived to be slow and difficult to enter.

The **minority** of Workgroup members were **neutral** against Applicable BSC Objective (c) for the **Proposed** Modification as they believed any benefits to competition were balanced out by penalising Parties who have invested time and money in complying with the existing BSC rules. One member commented that it is difficult to say until examples come forward. The **minority** of members believed P362 was **detrimental** against Applicable BSC Objective (c) for the **Alternative** Modification as they were of the view that any benefits were outweighed by the potential negative impact on competition introduced by allowing the TC to trial services or products which may not benefit all participants.

Whilst innovation should be supported, some members felt uncomfortable 'letting people off the hook'. Some members also commented that there is a rule book for a reason and there will be inherent risks from deviating from those rules. However, they believed that appropriate checks and balances had been put in place to mitigate these risks, particularly with Ofgem acting as the 'gatekeeper' and the send back provisions.

Applicable BSC Objective (d)

The **Proposer** and the **majority** of Workgroup members **agree** that P362 **would** better facilitate Applicable BSC Objective (d) as negating the need for future Modifications to enable small scale product tests with no material impact on the rest of the industry, ELEXON and industry resource can be focussed elsewhere. Additionally, if enduring Modifications should become necessary following a successful trial, more information about the solution and any impacts will be known in advance, facilitating a more efficient Modification process.

Innovators will see the sandbox process as less intimidating than a Modifications process and will welcome the support that comes with the process. A member was pleased that the sandbox process has been brought forward as a Modification to give Parties an opportunity to assess and contribute towards it.

The **minority** of the Workgroup were **neutral** against Applicable BSC Objective (d) as they believed that any efficiency gained was balanced out by the costs of administering the sandbox service. Please note that in the first Assessment Consultation the majority of the Workgroup were neutral against Objective (d), however this is now the minority view of the Workgroup.

Applicable BSC Objectives (a), (e), (f) and (g)

At this stage, the **Proposer** and all **Workgroup** members believe that P362 is **neutral** against Applicable BSC Objectives (a), (e), (f) and (g).

| Does P362 better facilitate the Applicable BSC Objectives? | | |
|--|---|--|
| Obj | Proposed Modification | Alternative Modification ³ |
| (a) | <ul style="list-style-type: none"> • Neutral – unanimous – no impact | <ul style="list-style-type: none"> • Neutral – unanimous – no impact |
| (b) | <ul style="list-style-type: none"> • Neutral – unanimous – no impact | <ul style="list-style-type: none"> • Neutral – Proposer⁴ and majority – no impact • Yes – minority - implementation of products or services may allow for a more efficient operation of the electricity transmission system |
| (c) | <ul style="list-style-type: none"> • Yes – Proposer and majority - will enable the trialling of innovative ideas and for more companies to offer alternative solutions to consumers, and therefore increase competition • Neutral – minority - any benefits to competition were balanced out by penalising Parties who have invested time and money in complying with the existing BSC rule | <ul style="list-style-type: none"> • Yes – Proposer and majority – as per proposed. Majority believe Alternative better facilitates competition as less restrictive compared to Proposed. • No – minority – Conflict of interest will adversely impact competition |
| (d) | <ul style="list-style-type: none"> • Yes – Proposer and majority - improves efficiency of Mods process and removes the need for future Modifications to enable small scale product tests with no material impact on the rest of the industry • Neutral – minority - any efficiency gained was balanced out by the costs of administering the sandbox service | <ul style="list-style-type: none"> • Yes – Proposer and Majority – as per Proposed • No – Minority – increased risk from TC participation outweighs efficiency gains from Mods process |
| (e) | <ul style="list-style-type: none"> • Neutral – unanimous – no impact | <ul style="list-style-type: none"> • Neutral – unanimous – no impact |
| (f) | <ul style="list-style-type: none"> • Neutral – unanimous – no impact | <ul style="list-style-type: none"> • Neutral – unanimous – no impact |
| (g) | <ul style="list-style-type: none"> • Neutral – unanimous – no impact | <ul style="list-style-type: none"> • Neutral – unanimous – no impact |

³ Shows the different views expressed by the other Workgroup members – not all members necessarily agree with all of these views.

⁴ As the Proposer was a representative of BSCCo, he was not able to vote as per Section F2.4.5C, but we have captured his views.

Assessment Consultation respondents' views against the Applicable BSC Objectives

First Assessment Consultation

| Do you agree with the Workgroup's initial unanimous view that P362 does better facilitate the Applicable BSC Objectives than the current baseline, and | | | |
|--|----|--------------------|-------|
| Yes | No | Neutral/No Comment | Other |
| 8 | 0 | 0 | 1 |

Eight respondents to the first Assessment Consultation agreed with the Workgroup's initial view that P362 does better facilitate the Applicable BSC Objectives than the current baseline and so should be approved. The views provided were broadly in line with those provided by the Workgroup. Not all of the nine respondents expressed a clear view on specific Objectives, but of those who did:

- 6 believed that P362 better facilitates Applicable BSC Objective (c);
- 1 identified detrimental impacts against Applicable BSC Objective (c);
- 1 was neutral against Applicable BSC Objective (d); and
- 1 identified detrimental impacts against Applicable BSC Objective (d).

Workgroup members considered all responses before deciding on their views as captured above.

Second Assessment Consultation

| Do you agree with the Workgroup's initial majority view that the P362 Proposed solution does better facilitate the Applicable BSC Objectives compared with the current baseline? | | | |
|--|----|--------------------|-------|
| Yes | No | Neutral/No Comment | Other |
| 7 | 0 | 0 | 0 |

All respondents to the second Assessment Consultation agreed with the majority of the Workgroup that the Proposed Modification does better facilitate the Applicable BSC Objectives. The views given aligned with those of the Workgroup. Not all of the respondents expressed a clear view on specific Applicable BSC Objectives, but of those who did:

- Objective (c) - 4 support; and
- Objective (d) - 1 support and 2 neutral.



Do you agree with the Workgroup's initial majority view that the P362 Alternative solution does better facilitate the Applicable BSC Objectives compared with the current baseline?

| Yes | No | Neutral/No Comment | Other |
|-----|----|--------------------|-------|
| 7 | 0 | 0 | 0 |

All respondents to the second Assessment Consultation agreed with the majority of the Workgroup that the Alternative Modification does better facilitate the Applicable BSC Objectives. The views given aligned with those of the Workgroup. Not all of the respondents expressed a clear view on specific Objectives, but of those who did:

- Objective (b) – 1 neutral as insufficient evidence of benefits that could be realised by industry parties and consumers if TC can be granted BSC Derogations
- Objective (c) - 4 support; and
- Objective (d) - 1 support, 2 neutral and 1 detrimental as any T C Derogation more likely to impact all parties so Modification route is preferred.

Do you agree with the Workgroup's initial majority view that the P362 Alternative solution does better facilitate the Applicable BSC Objectives compared with the P362 Proposed solution and so should be approved??

| Yes | No | Neutral/No Comment | Other |
|-----|----|--------------------|-------|
| 5 | 2 | 0 | 0 |

What are the Applicable BSC Objectives?

(a) The efficient discharge by the Transmission Company of the obligations imposed upon it by the Transmission Licence

(b) The efficient, economic and co-ordinated operation of the National Electricity 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 of the balancing and settlement arrangements

(e) Compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency [for the Co-operation of Energy Regulators]

(f) Implementing and administering the arrangements for the operation of contracts for difference and arrangements that facilitate the operation of a capacity market pursuant to EMR legislation

(g) Compliance with the Transmission Losses Principle

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8 Panel's Initial Discussions

Panel Discussion on P362

At its meeting on 14 June 2018, the BSC Panel was invited to provide its initial views on the P362 Proposed and Alternative Modifications, outlined in the P362 Assessment Report.

The Panel agreed with a member who commented that they were pleased with how P362 had developed and moved on from where it had started.

'Sandbox Modifications'

A Panel Member queried whether Modifications raised as a result of a BSC Derogation would be treated differently to 'standard' Modifications. ELEXON clarified that P362 was not amending the Modification Procedures and therefore 'sandbox Modifications' would be treated the same as any other Modification. It is hoped that 'sandbox Modifications' will be more efficient to progress as they will be informed by evidence and data collected from the trialling of the innovative service or product.

Application Fee

The Panel wondered how many applications they could expect to see and whether an application fee would need to be set. ELEXON said they currently expected the volumes to be relatively low (less than ten) and for the new service to be absorbed into business as usual. This was on the basis that Ofgem had received 37 expressions of interest for their second window of the regulatory sandbox, of which eight are now being considered for a regulatory sandbox. Many of the 37 did not require a regulatory sandbox. Further, Ofgem will act as an initial filter for applications. ELEXON are required to report an estimate of the costs incurred in operating the sandbox service in the annual lessons learnt report.

The Panel discussed when and how the application fee should be set. There was a general consensus that the fee should be cost reflective rather than an arbitrary barrier to entry. ELEXON agreed to consider this if and when a fee was believed to be appropriate. The Panel agreed that the fee should be set only if large volumes of applications were being received and it therefore became necessary. It was noted that Ofgem do not charge a fee for its sandbox.

Sandbox Procedure

A Panel Member asked that the subsidiary document be reviewed to make it clear that you need to become a BSC Party in order for the BSC Derogation to become effective, as this was not currently prominent enough. Further, they asked for the wording on page 11 to be reviewed to make clear that the Panel may be mindful of imminent BSC changes but that they must still consider changes and sandbox applications against the current baseline, and that applicants would not be expected to consider such things.

Market Entry

The Panel discussed how the market entry process would work for applicants who were not BSC Parties. ELEXON confirmed that you cannot be derogated from the BSC if you are not a Party to it. An applicant could seek derogation from the market entry and Qualification provisions that did not apply to its functions and operation needed for the trialling of its service or product. A Panel Member believed these applicants would probably find it easier to simply buy a 'Supplier in a box'. Another member commented that these applicants could also seek services from other companies to fulfil functions that required specialist knowledge or capability.

Alternative Modification

The TC representative re-confirmed their commitment to supporting and facilitating innovation. He believed it was challenging to try to second guess what types of applications you could receive under the sandbox process, but that it was important not to overly restrict who could participate. It was more important to ensure suitable controls were in place. He believed suitable controls were in place to allow the TC to participate in the BSC Sandbox, as the Panel did not contain any TC voting members, and Ofgem made the final decisions.

ELEXON also confirmed that Distributors could apply for and be granted BSC Derogations under both the Proposed and Alternative solutions.

Panel's initial views against the Applicable BSC Objectives

Proposed vs current baseline

The Panel **unanimously** agreed that the P362 Proposed Modification **better** facilitated Applicable BSC Objectives (c) and (d), for the reasons given by the Workgroup.

Alternative vs current baseline

The Panel **unanimously** agreed that the P362 Alternative Modification **better** facilitated Applicable BSC Objectives (c) and (d), for the reasons given by the Workgroup.

Proposed vs Alternative

The Panel **unanimously** agreed that the P362 **Alternative** Modification is **better** than the P362 Proposed Modification and therefore initially recommends that the P362 **Alternative** Modification should be **approved** and that the P362 **Proposed** Modification should be **rejected**. The reasons align with those of the Workgroup.

Panel's views on draft legal text

The Panel **unanimously** agreed that the draft redlined changes to the BSC for the P362 Proposed and Alternative Modifications in Attachments A and B deliver the intention of P362.

Panel's views on the proposed Implementation Date

The Panel **unanimously agreed** with the Workgroup's recommended Implementation Date for the P362 Proposed and Alternative Modifications as detailed in Section 5.

Panel's views on Self-Governance

The Panel **unanimously agreed** with the Workgroup that P362 **does not** meet the Self-Governance Criteria as there is a material impact on competition and the Code's governance and modification procedures and so should not be progressed as a Self-Governance Modification.

9 Report Phase Consultation Responses

This section summarises the responses to the Panel's Report Phase Consultation on its initial recommendations. You can find the full responses in Attachment I.

| Summary of P362 Report Phase Consultation Responses | | | | |
|--|-----|----|---------------------------|-------|
| Question | Yes | No | Neutral/ No Comment | Other |
| Do you agree with the Panel's initial unanimous view that the P362 Proposed Modification better facilitates the applicable BSC Objectives than the current baseline? | 7 | 0 | 0 | 0 |
| Do you agree with the Panel's initial unanimous view that the P362 Alternative Modification better facilitates the Applicable BSC Objectives than the current baseline? | 7 | 0 | 0 | 0 |
| Do you agree with the Panel's initial unanimous view that the P362 Alternative Modification better facilitates the Applicable BSC Objectives than the P362 Proposed Modification and should therefore be approved? | 5 | 2 | 0 | 0 |
| Do you agree with the Panel's initial unanimous view that the redlined changes to the BSC deliver the intention of the P362 Proposed and Alternative solutions? | 7 | 0 | 0 | 0 |
| Do you agree that the subsidiary document in Attachment D delivers the intent of P362? | 7 | 0 | 0 | 0 |
| Do you agree with the Panel's initial unanimous recommended Implementation Date? | 7 | 0 | 0 | 0 |
| Do you agree with the Panel's initial unanimous view that P362 should not be treated as a Self-Governance Modification? | 7 | 0 | 0 | 0 |
| Do you have any further comments on P362? | 4 | 3 | N/A | N/A |

Do you agree with the Panel's initial unanimous view that the P362 Proposed Modification better facilitates the Applicable BSC Objectives than the current baseline?

Respondents were unified in their belief that the Proposed Modification better facilitates the applicable BSC Objectives. Each of the four respondents who provided further commentary noted their belief that the modification will better promote competition than the current baseline. The same respondents expressed their neutrality over whether the modification will facilitate BSC Objective (d), with one pointing out that, though the Modification has the potential to promote efficiency, any such gains are offset by the likelihood of increasing costs and workload.

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Do you agree with the Panel's initial unanimous view that the P362 Alternative Modification better facilitates the Applicable BSC Objectives than the current baseline?

Responses were uniformly positive, with seven out of seven replies in the affirmative. No new arguments were put forward.

Do you agree with the Panel's initial unanimous view that the P362 Alternative Modification better facilitates the Applicable BSC Objectives than the P362 Proposed Modification and should therefore be approved?

While a majority of respondents agreed with the Panel's unanimous view, two replied negatively and expressed a preference for the original Modification. Both of these respondents identified an adverse impact on BSC Objective (d) within their rationales, noting the risk to efficiency of handling of Balancing and Settlement arrangements should the Transmission Company have BSC Derogations, a concern that was echoed by four out of the six consultees.

In relation to BSC Objective (b) one respondent remained unconvinced that allowing the Transmission Company or any Network Owner to apply for derogations would allow for greater efficiency.

One respondent stated their preference for the original Modification proposal but conceded that both it and the Alternative would better facilitate the BSC Objectives and, as such, they would not object to either proposal's approval by the Authority.

One consultee expressed their belief that it would be unfair to exclude the Transmission Company from a route to innovation while other monopolies are free to take advantage of the process made possible by this Modification.

Do you agree with the Panel's initial unanimous view that the redlined changes to the BSC deliver the intention of the P362 Proposed and Alternative solutions?

All consultees believed that the redlined changes to the BSC deliver the intention of the P362 Proposed and Alternative solutions.

Do you agree that the subsidiary document in Attachment D delivers the intent of P362?

All consultees indicated that the subsidiary document delivers the intent behind the Modification. One respondent noted that the document will require a small adjustment to reflect the Alternative solution, while another respondent stated their belief that it should be made clear that several parts of the BSC, including requirements to pay settlement and trading charges alongside the lodging of credit cover, cannot be derogated from. ELEXON notes that Attachment E is the draft subsidiary document for the Alternative Proposal and that section five of the document details a list of requirements that would likely result in a derogation request being rejected.

Do you agree with the Panel's initial unanimous recommended Implementation Date?

All consultees found no issue with the recommended Implementation Date of five working days following the Authority's decision.

Do you agree with the Panel's initial unanimous view that P362 should not be treated as a Self-Governance Modification?

Three consultees expanded on their agreement with the Panel's view, noting that the Modification does not meet the Self-Governance Criteria. No new arguments were put forward.

Do you have any further comments on P362?

Four respondents wished to offer further commentary on the topic. It was observed that the process would evolve over time as a necessity with early applications carefully reviewed to facilitate changes to the subsidiary document and legal text.

One response highlighted the potential benefit of applicants clearly defining success criteria and a minimum scope when presenting their application. One consultee stated their support of innovation within the energy market and argued that this Modification will further that aim.

Finally, one respondent called on Ofgem to approve and implement the Modification as soon as possible and emphasised the benefit to customers that the Modification would unlock upon implementation.

Panel's final discussions on P362

At its meeting on 12 July 2018, the BSC Panel was invited to provide its final views on the P362 Proposed and Alternative Modifications.

Derogation Period

A Panel member questioned the minimum Derogation Period, suggesting that 2 years went beyond the idea of a proof of concept, further stating their view that the sandbox is rightly intended to trial innovative services and products rather than testing economic viability.

Another Panel member pointed out that, due to the unpredictable nature of what applications the sandbox would receive, a minimum Derogation Period of 2 years felt suitable on the basis of facilitating contingency and flexibility, as for example trials may not work first time.

ELEXON added that the Panel can set conditions on Derogations, such as the scope (e.g. number of Metering Systems in the trial) to mitigate risks and on timescales. Further, the Applicant is required to submit the shortest period necessary to test the proposal and must justify this request. ELEXON will assess and work with the Applicant on the appropriate Derogation Period before presenting it to the Panel. The Panel can recommend rejection of the proposal to Ofgem on the basis of the Derogation Period. These points helped to alleviate the Panel Member's concern.

Proposed vs Alternative

The representative from National Grid stated that the Transmission Company desired to be flexible and agile in their response to innovative ideas and that the recommendation of the Alternative Modification would help to facilitate this, echoing feedback from the Report Phase Consultation responses.

A Panel member pointed out that, as the Transmission Company, National Grid are well-versed in the Modification process and wondered if this would be a more appropriate route for them. One Panel member noted that National Grid would be one of the most likely parties to make use of the sandbox process upon the Modification's implementation.

Another Panel member further added that it would be unwise to exclude National Grid from a route to innovation given the unpredictable nature of innovative ideas.

Panel's final views

The Panel's final views and arguments remained unchanged from their initial views. The Panel unanimously:

- **AGREED** that the P362 Proposed Modification:
 - **DOES** better facilitate Applicable BSC Objective (c);
 - **DOES** better facilitate Applicable BSC Objective (d); and
- **AGREED** that the P362 Alternative Modification:

- **DOES** better facilitate Applicable BSC Objective (c);
 - **DOES** better facilitate Applicable BSC Objective (d); and
- **AGREED** that the P362 **Alternative** Modification is **better** than the P362 Proposed Modification;
- **AGREED** that the P362 **Alternative** Modification should be **approved** and that the P362 **Proposed** Modification should be **rejected**;
- **APPROVED** an Implementation Date for the Proposed and Alternative Modification of:
 - 5 Working Days following the Authority's approval;
- **AGREED** that P362 should **not** be treated as a Self-Governance Modification;
- **APPROVED** the draft legal text and Code Subsidiary Document for the Proposed Modification;
- **APPROVED** the draft legal text and Code Subsidiary Document for the Alternative Modification; and
- **APPROVED** the P362 Modification Report.

11 Recommendations

The BSC Panel recommends to the Authority:

- That the P362 Proposed Modification should be **rejected** and that the P362 Alternative Modification should be **approved**;
- An Implementation Date for the P362 Proposed or Alternative Modification of:
 - 5 Working Days following the Authority's approval;
- The BSC legal text and CSD for the P362 Proposed Modification and Alternative Solution.

Workgroup's Terms of Reference

Specific areas set by the BSC Panel in the P362 Terms of Reference

- a) What conditions, principles or criteria should the Panel consider when determining whether to grant derogation?
 - i. What checks and balances are needed?
 - ii. What decision making power should the Panel be granted and what should the voting mechanism be e.g. simple majority, unanimous or recommendation to Ofgem?
 - iii. How will the solution assess the impact on other Codes and schemes such as CFDs?
- b) What should the scope of derogations and conditions in the BSC be?
- c) Who should be able to participate in the electricity market sandbox?
- d) What process, if any, should applicants go through prior to formally requesting derogation?
 - i. How often should ELEXON run its sandbox process?
- e) How should the solution ensure the processes and derogated projects are transparent to industry?
 - i. How often should any reporting be and where should it be published?
- f) How should the risk to Settlement, the BSC and other industry participants of derogated projects be managed and mitigated?
 - i. Should the BSC Auditor provide a view on the risk to Settlement?
- g) What role should ELEXON have in supporting derogation requests?
 - i. How can the costs of running a BSC sandbox be fair and consistent to BSC Parties?
 - ii. What is the legal status of any support provided by ELEXON?
 - iii. What is the legal status of any derogation provided by the BSC Panel?
- h) How should the transitional process from tested/proved derogated projects to a new permanent baseline be handled?
 - i. How should useful Modifications identified as a result of sandbox projects be progressed?
- i) How can the P362 solution accommodate other electricity industry sandboxes, for example to avoid duplication and provide a common process?
 - i. What cross-code impacts are there?
- j) What changes are needed to BSC documents, systems and processes to support P362 and what are the related costs and lead times?
- k) Are there any Alternative Modifications?
- l) Should P362 be progressed as a Self-Governance Modification?
- m) Does P362 better facilitate the Applicable BSC Objectives than the current baseline?

Assessment Procedure timetable

| P362 Assessment Timetable | |
|---|--------------------------------|
| Event | Date |
| Panel submits P362 to Assessment Procedure | 9 Nov 17 |
| Workgroup Meeting 1 | 13 Dec 17 |
| Workgroup Meeting 2 | 24 Jan 18 |
| Workgroup Meeting 3 | 26 Feb 18 |
| Workgroup Meeting 4 | 7 Mar 18 |
| First Assessment Procedure Consultation and Industry Impact Assessment | 21 Mar 18 to 12 Apr 18 (15WDs) |
| Workgroup Meeting 5 | 23 Apr 18 |
| Second Assessment Procedure Consultation and Industry Impact Assessment | 8 May 18 to 21 Jun 18 (10WDs) |
| Workgroup Meeting 6 | 30 May 18 |
| Panel considers Workgroup's Assessment Report | 14 Jun 18 |

Workgroup membership and attendance

| P354 Workgroup Attendance | | | | | | | |
|---------------------------|--|----------|----------|----------|---------|----------|----------|
| Name | Organisation | 13/12/17 | 24/01/18 | 26/02/18 | 7/03/18 | 23/04/18 | 30/05/18 |
| Members | | | | | | | |
| Claire Kerr | ELEXON (<i>Chair</i>) | ✓ | ✓ | ✓ | ✓ | ✗ | ✓ |
| Jemma Williams | ELEXON (<i>Chair</i>) | ✗ | ✗ | ✗ | ✗ | ✓ | ✗ |
| Lawrence Jones | ELEXON (<i>Lead Analyst</i>) | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Andy Colley | SSE | ✓ | ✓ | ✓ | ✓ | ☎ | ☎ |
| Derek Weaving | Centrica | ✓ | ✓ | ☎ | ☎ | ✓ | ✗ |
| Kenneth Skou | NEAS Energy | ✗ | ✓ | ✓ | ✗ | ✗ | ☎ |
| Chris Smith | Kingscote Enterprises | ✓ | ✓ | ☎ | ☎ | ✓ | ☎ |
| Pam Liu | Inventev Technology Limited | ✓ | ✓ | ✓ | ☎ | ✓ | ☎ |
| Aaron Dickinson | Utiligroup | ✓ | ✓ | ✗ | ✗ | ✗ | ✗ |
| Lisa Waters | Waters Wye Associates | ✓ | ✓ | ✓ | ☎ | ✓ | ☎ |
| Richard Vernon | Npower Group PLC | ✓ | ✓ | ✓ | ☎ | ✓ | ✗ |
| Dan Bentham | EDF Energy | ✓ | ✓ | ✗ | ✗ | ✗ | ☎ |
| Michael Oxenham | National Grid | ✓ | ✓ | ☎ | ☎ | ✓ | ☎ |
| Attendees | | | | | | | |
| Peter Frampton | P362 (<i>Proposer Representative</i>) & ELEXON (<i>Design Authority</i>) | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| David Stephens | ELEXON (<i>Lead Lawyer</i>) | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Scott Laczay | Ofgem | ✓ | ✓ | ✓ | ☎ | ✓ | ☎ |
| Karsten Mandrup Nielsen | NEAS Energy | ✗ | ✓ | ✗ | ✗ | ✗ | ✗ |
| Derek Walker | Inventev Technology Limited | ✓ | ☎ | ✓ | ☎ | ✓ | ☎ |
| Jamie McRorie | Ofgem | ✗ | ✗ | ☎ | ☎ | ✗ | ✗ |

Appendix 2: Glossary & References

Acronyms

Acronyms used in this document are listed in the table below.

| Acronyms | |
|----------|---|
| Acronym | Definition |
| BEIS | Department for Business, Energy & Industrial Strategy |
| BM | Balancing Mechanism |
| BSC | Balancing and Settlement Code |
| BSCCo | Balancing and Settlement Code Company |
| CACoP | Code Administrators Code of Practice |
| CFD | Contracts for Difference |
| CoP | Code of Practice |
| CP | Change Proposal |
| CSD | Code Subsidiary Document |
| CUSC | Connection and Use of System Code |
| DCC | Data Communications Company |
| DCUSA | Distribution Connection and Use of System Agreement |
| EMR | Electricity market Reform |
| EU | European Union |
| FCA | Financial Conduct Authority |
| GB | Great Britain |
| GCRP | Grid Code Review Panel |
| GEMA | Gas and Electricity Markets Authority |
| GSP | Grid Supply Point |
| HVDC | High Voltage Direct Current |
| ISG | Imbalance Settlement Group |
| MRA | Master Registration Agreement |
| MSID | Metering System Identifier |
| NETS | National Electricity Transmission System |
| NGET | National Grid Electricity Transmission plc |
| NRA | National Regulatory Authority |
| PAB | Performance Assurance Board |
| RfG | Requirements for Generators |
| SCR | Significant Code Review |
| SVG | Supplier Volume Allocation Group |
| TDC | Trading Disputes Company |

| Acronyms | |
|----------|---|
| Acronym | Definition |
| TFEU | Treaty on the Functioning of the European Union |
| UK | United Kingdom |

External links

A summary of all hyperlinks used in this document are listed in the table below.

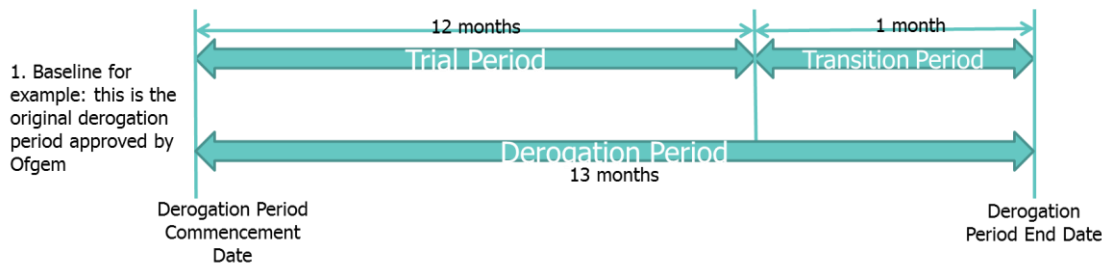
All external documents and URL links listed are correct as of the date of this document.

| External Links | | |
|----------------|---|---|
| Page(s) | Description | URL |
| 6 | Panel Paper 271/04 on proposal for BSC sandbox | https://www.elexon.co.uk/meeting/bsc-panel-270/ |
| 6 | Ofgem Innovation Link | https://www.ofgem.gov.uk/about-us/how-we-engage/innovation-link |
| 6 | Ofgem regulatory sandbox | https://www.ofgem.gov.uk/publications-and-updates/update-regulatory-sandbox |
| 6 | Ofgem sandbox application round | https://www.ofgem.gov.uk/publications-and-updates/regulatory-sandbox-2-calling-expressions-interest |
| 7 | BSC Section L | https://www.elexon.co.uk/bsc-and-codes/balancing-settlement-code/bsc-sections/ |
| 7 | Code of Practice | https://www.elexon.co.uk/bsc-and-codes/bsc-related-documents/codes-of-practice/ |
| 8 | P362 page on the ELEXON website | https://www.elexon.co.uk/mod-proposal/p362/ |
| 18 | November Panel meeting | https://www.elexon.co.uk/meeting/bsc-panel-271/ |
| 18 | P351 'Align the BSC with changes to the SCR requirements' | https://www.elexon.co.uk/mod-proposal/p351/ |
| 18 | Electricity supply licence conditions | https://www.ofgem.gov.uk/licences-codes-and-standards/licences/licence-conditions |
| 18 | Electricity generation licence conditions | https://www.ofgem.gov.uk/licences-codes-and-standards/licences/licence-conditions |
| 20 | Section F2.7A | https://www.elexon.co.uk/bsc-and-codes/balancing-settlement-code/bsc-sections/ |
| 21 | Market entry service | https://www.elexon.co.uk/reference/market-entry/ |

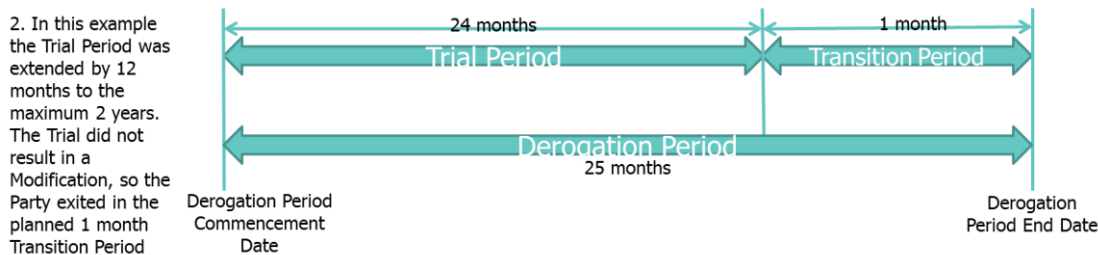
| External Links | | |
|----------------|--|---|
| Page(s) | Description | URL |
| 36 | Electricity Network Innovation Competition | https://www.ofgem.gov.uk/network-regulation-riio-model/current-network-price-controls-riio-1/network-innovation/electricity-network-innovation-competition |
| 36 | Electricity Network Innovation Allowance | https://www.ofgem.gov.uk/network-regulation-riio-model/network-innovation/electricity-network-innovation-allowance |
| 36 | Low Carbon Networks Fund | https://www.ofgem.gov.uk/electricity/distribution-networks/network-innovation/low-carbon-networks-fund |
| 54 | State Aid | https://www.gov.uk/guidance/state-aid |
| 55 | State Aid manuals | https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/607691/bis-15-148-state-aid-manual-update.pdf |
| 55 | European Commission's factsheet | http://ec.europa.eu/competition/publications/factsheets/antitrust_procedures_102_en.pdf |

Appendix 3: P362 Derogation Period examples

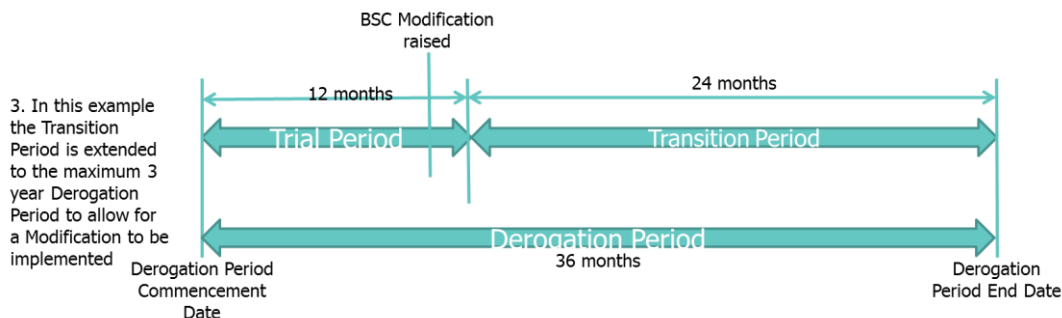
Approved Derogation Period example 1



Approved Derogation Period example 2



Approved Derogation Period example 3



Appendix 4: Further legal considerations

At the December 2017 CUSC Panel meeting a member asked the Ofgem representative whether a number of items had been considered by Ofgem for their sandbox, namely:

1. State Aid;
2. Competition law; and
3. Affect on cross border trade; [and EU derogation process].

The member took an action to write to the Ofgem representative on these items. An extract of this email is below:

1. State Aid

In respect of State Aid, I was thinking in terms of where “State aid is any advantage granted by public authorities through state resources on a selective basis to any organizations that could potentially distort competition and trade in the European Union (EU).” [emphasis added] as defined via the UK Government website.

<https://www.gov.uk/guidance/state-aid>

Further clarification can also be found in the ‘State Aid Manual’ published by BEIS:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/607691/bis-15-148-state-aid-manual-update.pdf

It sets out at paragraph 1.10 (and further details in Annex A) the four tests that should be applied.

Would you or your colleagues be able to confirm if: (a) the Ofgem sandbox arrangements have already been explicitly assessed in terms of State Aid; (b) that the those four test in Annex A of the BEIS document have been performed in this case by Ofgem; and (c) that as a result Ofgem have certified that the sandbox arrangements are not ‘State Aid’?

I was wondering if what is being proposed, in terms of the ‘sandbox’, could amount to a conferring of an advantage, on a selective basis, to some organisations (by, for example, them avoiding the need to comply with some Code obligations that similar organisations have to comply with) might be considered to fall within the definition of ‘state aid’?

If this was the case then there could, it seems, be an ability for parties adversely affected by such aid to seek recompense etc., under EU and national law - presumably from the public authority concerned?

In regard to the definition of ‘public authority’ I recall engaging with your colleagues (plus National Grid and others) about ten years ago on whether Code Administrator(s) / NGET, by virtue of the functions they perform (namely the legal / mandatory nature and the role of Ofgem in their work) display the characteristics, in law, of a ‘public authority’ or not. I attach a paper from the Ministry of Justice from around that time that may be helpful in that regard. Suggestions at that time were that a case could be made that Code Administrators could be considered as a ‘public authority’.

2. Competition Law

In respect of competition law, I was thinking in terms of the distorting (and discriminatory) effect on competition that could arise where a company is applying to some parties mandatory obligations whilst not applying those same mandatory obligations to other parties where both sets of parties are identical.

I'm not certain that the respective approval of this by a Panel (or indeed GEMA?) can overwrite the need for the Code Administrator (such as ELEXON or NGET) to comply with competition law generally, and Article 102 (TFEU) specifically.

One of the potential competition law concerns might include the possibility of 'an abuse of a dominate position' arising. Further information on this can be found by reference to the European Commission's factsheet –

http://ec.europa.eu/competition/publications/factsheets/antitrust_procedures_102_en.pdf

See, for example , the statement on page 1 of the factsheet about 'What is an Abuse':

"To be in a dominant position is not in itself illegal. A dominant company is entitled to compete on the merits as any other company. However, a dominant company has a special responsibility to ensure that its conduct does not distort competition. Examples of behaviour that may amount to an abuse include requiring that buyers purchase all units of a particular product only from the dominant company (exclusive purchasing); setting prices at a loss-making level (predation); refusing to supply input indispensable for competition in an ancillary market; charging excessive prices."

In this context I note the statement on page 2 of the factsheet which maybe relevant:-

"Victims' claims for damages: Any citizen or business which suffers harm as a result of a breach of the EU competition rules should be entitled to claim compensation from the party who caused it. This means that the victims of competition law infringements can bring an action for damages before the national courts."

In this regard, if such a situation occurred, then it would seem that the party who caused it could be NGET for the CUSC and Grid Code (plus ELEXON for the BSC).

3. Affect on Cross Border trade

In respect of trade (noted under (1) above) on the face of it there is the potential risk, with the sandbox approach, that in offering a difference in approach to certain parties (be they generators, demand side response providers or demand) than other parties (who are the same type of undertakings) that this could have an affect on cross border trade; both with other Member States but also within the (UK) Member State (GB / Northern Ireland).

As I'm sure you appreciate, there are overarching requirements to ensure that there is no affect on cross border trade under EU law. This is helpfully summarised in a Commission Guideline, which can be found at:

<http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=LEGISSUM:l26113&from=EN>

In terms of the national codes (such as the CUSC, BSC, Grid Code, Distribution Code etc.,) and the need not to affect cross border trade; this legal obligation is, for example, set out in Regulation 714/2009 (the 'Third Package') at Article 8(7) in the following terms:

"The network codes shall be developed for cross-border network issues and market integration issues and shall be without prejudice to the Member States' right to establish national network codes which do not affect cross-border trade."
[emphasis added]

In addition to the three points I mentioned at the December Panel meeting I've also thought of another relevant item, namely in terms of the compatibility with the EU Network Codes / Guidelines.

4. EU derogation process

I notice that ELEXON prepared some slides for the December GCRP (see attached). There are a number of references to 'derogations' in those slides, such as at Slides 3 and 5 (I've emphasised the text below):

"Regulatory sandboxes typically offer advice on innovative business models to help understand the frameworks within which they must operate, and derogations to specific aspects of the rules that could be deemed overly burdensome"

"The sandbox is not a thing or a place or a system – it is conceptual, a set of processes to facilitate the provision of advice or obtaining a derogation "

"Providing derogations requires a Modification to add provisions to the BSC"

"Subject to the approval of the workgroup, the derogations will be the responsibility of the BSC Panel, and ELEXON will support applications to derogation if necessary"

However, the CUSC deals (at a very high level) with two principle items, namely (i) the contractual arrangements for the connection etc., to the GB transmission system (NETS) and (ii) the 'connection' and 'use of system' charging arrangements for the GB transmission system (NETS).

Given the introduction of the new RfG Guideline connection regime from 18th May 2018 onwards (plus DCC and HVDC to follow) I cannot see how, for example, either the CUSC Panel (or the GCRP for that matter) can provide, legally, any derogation(s) for new connecting parties (or for existing parties who substantially modify) in terms of the RfG (of DCC or HVDC) requirements as this can only be granted by the NRA (Ofgem in the case of GB) and this power cannot be delegated (by the NRA) - in the sandbox case to either the CUSC or Grid Code Panel(s).

Furthermore, in terms of supporting innovation, the RfG was specifically drafted to take that into account. As you may be aware, the RfG included a specific 'carve out' which permitted emerging (generator) technology providers to apply to the NRA to be allowed to sell their equipment based on the 'status quo' (pre RfG) connection conditions. Ofgem consulted on their approach, for GB, to dealing with emerging technology applications etc., in the autumn of last year. Therefore, it seems to me that the CUSC Panel would not be able to offer relief from the harmonised connection rules for new entrants via a sandbox approach.

As an aside, with respect to the Balancing Guideline, a similar derogation arrangement (as those for the three connection related Guidelines) is set out (in Article 62) which would, it seems, preclude the BSC Panel likewise being able to issue derogations to obligations arising from that Guideline. In this context, I know that my colleague Andy Colley (who I've copied into the email) is involved with the P362 BSC Workgroup which is considering

this and he may also be interested in your answers to the questions I've posed in this email.

Finally, in regard to this fourth item, I'll not dwell on the charging aspects of CUSC (as set out in the two methodologies contained in Section 14) as I assume; given Ofgem's duties under Article 37 (1) (a) and (6) (a) of Directive 2009/72; that any 'sandbox' type change(s) to charges to be paid could only be implemented by a CUSC Modification being raised in each case (rather than either the CUSC Panel or the Code Administrator or NGET directly themselves dis-applying the part(s) of Section 14 to certain parties) and being approved by Ofgem accordingly.

I'm sure that all these four items (and others) will have been considered in depth already by Ofgem prior to its sandbox initiative being presented and therefore the questions I'm asking can be quickly answered and my concerns allayed.

Ofgem Response

The below is an extract of Ofgem's response to the points raised by the CUSC panel member:

1. State aid

Under European Union rules it is illegal for EU countries to give financial help to some companies and not others in a way which would distort fair competition. This help is called "state aid", and the rules barring it are enforced by the European Commission and national courts. State aid is governed by the Treaty on the Functioning of the European Union (TFEU). Article 107(1) of TFEU states that "any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market".

This expression is often broken down into a four step test to help work out if an action will be "state aid". The CUSC Panel member email refers to government guidance which reiterates the four-part test. For State aid to exist, all four parts of the following test must be satisfied:

1. aid is granted by the transfer of state resources;
2. to a certain undertaking;
3. thereby creating a selective advantage; and
4. the transfer of resources distorts or has the potential to distort competition and trade between EU countries.

In the present circumstances the sandbox proposals would appear to fail the first of these four tests. To qualify as State aid the transfer in question must involve 'State resources'. This includes resources controlled by central and all local governments together with public or private bodies which use state resources. However, private funds do not normally constitute "state resources"; there must be a direct or indirect transfer of State resources for Art. 107 TFEU to apply. This general principle is obviously applicable to any derogation the BSC code may entail. Should that derogation result in a benefit to an undertaking that would not entail advantage of state resources; to the extent there is any relief from regulatory burden whatsoever the funds which underpin the Balancing Mechanism are generated by ELEXON's customers, namely BSC Parties which are either Electricity

Generation or Supply Licence holders. For the first test to be satisfied there must also be a “transfer of resources”. This can be positive, such as a grant or negative, such as a tax rebate or loan at less than market rates of interest. In either case the transfer improves the beneficiary’s net financial position and has an impact on the state balance sheet. However, on the face of the facts the proposed sandbox neither positively distributes State resources nor does it imply that the State will forego resources that it would otherwise have benefitted from. The State bears no budgetary burden by reason of the Sandbox proposals and so the first limb of the four part test is not satisfied.

However, the position in respect of any additional government-based incentives will need to be considered on a case by case basis. The BSC includes provisions dealing with additional funds in the market which come directly from Government and which have been cleared by the EU Commission to ensure they are State aid compliant. For example, Capacity Market funds are “state resources” but are lawful (and not State aid) because they have been approved by the EU Commission. Should any application for a derogation have an appreciable impact on such pre-existing State aid clearance then each will need to be carefully considered on a case by case basis to determine if it would be compatible.

However, we understand that the Sandbox would contemplate temporary relief from an obligation of the BSC which, while relieving the undertaking in question of a burden, does not relate in any difference to the net financial position for the State and so does not, in principle, involve State aid. For the avoidance of doubt, having determined that that Regulatory Sandbox does not satisfy the first of the four parts of the test for the presence of State aid it is not necessary to consider the remaining elements of the test.

2. Competition Law

The CUSC Panel member email refers to Article 102 which relates to the abuse of a dominant market position. Both UK and EU competition law prohibit businesses with significant market power unfairly exploiting their strong market positions. To be in a position of dominance, a business must have the ability to act independently of its customers, competitors and consumers. Establishing if a company is dominant requires a complex assessment of a number of elements. However “dominance” means, generally, that a party has a dominant trading position in relation to a particular market. i.e that it is in a trading position of economic strength which enables it to prevent effective competition being maintained on the relevant market by affording it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers. Given the composition of the Panel, the balance that it seeks to achieve and Ofgem’s ultimate oversight it does not appear that any one party would be in a position to exert its dominance through the derogations process (any more than it would in the normal conduct of the BSC).

3. Distortion of trade - Effect on cross border trade

It is unclear what the CUSC Panel member email is asserting under this heading. The guidelines which are referred and linked to in the email set out “guidelines on the effect on trade”, but this is in respect of the application of that concept to breaches of competition law under Article 101 or 102 of the TFEU. In order to establish a breach of competition law under either Articles 101 (anti –competitive agreement) or 102 (dominance) it is necessary to have regard to whether the behaviour in question has an effect on cross- border trade. However if there is no anti-competitive agreement or abuse of dominant position there is no contravention which would have an appreciable effect on international trade. For the sake of completeness it is our view that there is little, if any, risk that the Ofgem sandbox or proposed P362 would appreciably affect intra-community trade. The UK market will remain open to that intra –community trade and the derogations process will be available

to those participating in the market. The derogations in question are understood to be short term and for specific purposes that will have no impact on cross –border trade or discriminate between EU operators.

4. EU Derogation Process

During our call it became apparent that there were 2 aspects of concern expressed under this heading:

Firstly, there was a concern that any derogation might seek to exempt one or more parties from requirements that were binding as a result of, for example, EU law. Derogations could not be permitted in circumstances where that would be outside the Panel's or Ofgem's authority. There will indeed be limitations to the extent of what a Sandbox can achieve. As observed it may not be within the gift of ELEXON or CUSC or even Ofgem to issue derogations from any particular requirement, particularly if these are set by EU law or primary legislation. The example given in the email of "RfG Guideline connection regime from 18th May 2018" seems to be a reference, for example, to the implementation arrangements in place for EU Commission Regulation 2016/631 establishing network code on the requirement for grid connection of generators. Any derogation to the requirements of that EU regulation would need to be carefully considered and may well be outside what a derogation process can achieve. It is anticipated that, to the extent it would be possible to do so, parties would explore alternatives on order to make sure a derogation (if granted) still enabled compliance with the EU regulation or equivalent which was at stake.

Secondly, during the meeting, we touched on whether a code, in this case the BSC, could operate a derogation process without Ofgem (the Authority) becoming involved and/or ultimately approving of any particular derogation. From a policy perspective I do not think that Ofgem would welcome enabling an industry panel to permit derogations without a degree of control from Ofgem. From a legal perspective my preliminary thoughts are that to permit such an approach may be unlawful on the basis that it would fetter the Authority's discretion and/or purport to delegate the Authority's functions to a 3rd party. The Authority is given statutory authority to issue and modify the transmission licence. The licence itself obligates to licence holder to create the code and tightly controls the circumstance within which those codes may be modified, with the Authority ultimately approving modifications in each case. Whilst a derogation may be time-limited, for a set period of time and directed for the benefit of one or more parties it nevertheless would modify the effect of the code for that party for the duration of the derogation. There is an argument therefore that a "derogation" is a type of modification, the delegation of which to 3rd party would be to delegate an important part of the Authority's functions. We think that from a policy and legal perspective it is important that the Authority retains ultimate direction over the derogations process. We have since seen a draft of p362, which would appear to recognise these principles at 10.1.1 which would give the Authority ultimate control over derogations.

To conclude, the CUSC panel member's email sets out several relevant considerations which will need to be borne in mind when the Panel, and the Authority, considers any derogation. However these legal considerations need not, in principle, imply that a "sandbox" approach to the BSC is impermissible. Such derogations will be considered on a case by case basis, not just to ensure that the relevant policy considerations are taken into consideration but to ensure that the derogation does not contravene the relevant legal considerations.