



Stage 03: Assessment Report

P235: Aligning BSC requirements with the calculation of reconciliation interest performed by the Funds Administration Agent

What stage is this document in the process?

01 Initial Written Assessment

02 Definition Procedure

▶ 03 Assessment Procedure

04 Report Phase

P235 will align the Balancing and Settlement Code drafting for calculating the interest on Reconciliation Charges with the calculation methodology undertaken by the Funds Administration Agent systems. This methodology has been used by the FAA since NETA Go-Live, and mirrors that used under the Pool.



The Modification Group unanimously recommends:
Approval of the Alternative Modification with a retrospective Implementation Date of NETA Go-Live



Impact of approving P235: **Low**
P235 will align the Code with the calculation which the Funds Administration Agent already uses



Impact of rejecting P235: **High**
Rejection could result in system and process changes for the Funds Administration Agent and for BSC Parties

155/06

P235
Assessment Report

7 May 2009

Version 1.0

Page 1 of 7

© ELEXON Limited 2009

Contents

1	Why Change?	3
2	Solution	4
3	Case for Change	5
4	Costs and Impacts	6
5	Group's Recommendations	7
6	Further Information	7

Attachment A: Part 2 - Detailed Assessment

Attachment B: Proposed Modification Draft Legal Text

Attachment C: Alternative Modification Draft Legal Text

About This Document:

This document is an Assessment Report, which ELEXON will present to the Panel on 14 May 2009 on behalf of the P235 Modification Group. The Panel will consider the Group's recommendations, and will agree an initial view on whether or not this change should be made. The Panel will then seek industry comments on its initial view through a further consultation.

There are 2 parts to this document. This is Part 1. It outlines the solution, impacts, costs, benefits and implementation approach for this change. It also includes the Group's full recommendations to the Panel on the final page.

Part 2 in Attachment A explains how the Group's discussions led it to its chosen solution and the recommendations in this report. It also includes a summary of the industry responses received to the Group's consultation.

You can download copies of the full industry consultation responses [here](#).

Attachments B and C contain the Group's agreed legal text.



Any questions?

Contact:

Kathryn Coffin



kathryn.coffin@elexon.co.uk



020 7380 4030

155/06

P235

Assessment Report

7 May 2009

Version 1.0

Page 2 of 7

© ELEXON Limited 2009



What are Reconciliation Charges?

The adjustments made to a Party's Trading Charges following a Reconciliation Run.

These adjustments are intended to make it as if the Metered Volumes determined at that Reconciliation Run had been submitted at the Initial Settlement Run.

Why has P235 been raised?

ELEXON has recently identified that the Balancing and Settlement Code ('the Code') requirements for calculating the interest on Reconciliation Charges are inconsistent with those undertaken by the Funds Administration Agent (FAA) systems. ELEXON notified the industry of the inconsistencies on 3 April 2009 in ELEXON Circular [01715](#).

Having analysed the effects of the differences between the FAA systems methodology and the Code requirements, ELEXON has concluded that the FAA interest methodology is the more appropriate calculation.

Following a recommendation by ELEXON, the Panel raised P235 on 9 April 2009 to align the Code requirements with the methodology used by the FAA systems and thereby remove the inconsistencies.

What inconsistencies are identified by P235?

The FAA systems have used the same method of interest calculations since NETA Go-Live, and mirror the methodology used under the Pool arrangements.¹ The Code requirements are detailed in **Section N6.4.2(b)**, and have remained unchanged in this respect since the Code was first drafted.

The FAA interest calculations differ from the Code requirements in four ways.

Area of inconsistency	FAA methodology	Code drafting
Start of interest calculation period	Interest calculation period extends all the way back to the Payment Date for the Initial Settlement Run	Interest is only calculated back to the Payment Date of the previous Reconciliation Run
Base Rate used in interest calculation	Calculates interest on a daily basis, using the Base Rate applicable to each day in the calculation period	Implies the use of a single Base Rate for each day in the calculation period
Accumulation of interest over the calculation period	Calculates interest on a compound basis (where the amount on which interest is calculated for each day in the period includes the accumulated interest levied on previous days)	Implies the use of simple interest (where the amount on which interest is charged remains the same for each day in the calculation period)
End of interest calculation period	Interest calculation period <u>excludes</u> the Payment Date for the current Reconciliation Run	Interest calculation period <u>includes</u> the Payment Date for the current Reconciliation Run

Section 2 in Part 2 of this document explains the effect of the inconsistencies in more detail, and includes an illustration of their materiality for Parties' Trading Charges.

155/06

P235

Assessment Report

7 May 2009

Version 1.0

Page 3 of 7

© ELEXON Limited 2009

¹ The New Electricity Trading Arrangements (NETA) replaced the previous Electricity Pool arrangements in 2001.



What is a Trading Dispute?

A mechanism for investigating a potential error in the data, processes or rules used for Settlement and (if appropriate) for recalculating impacted Trading Charges.

P235 will amend Section N6.4 of the Code to align it with the FAA methodology.

The Group has developed two solutions: a Proposed Modification and an Alternative Modification.

How are the Proposed and Alternative Modifications different?

The two solutions differ only in their implementation approaches.

The **Proposed Modification** would be implemented on a **prospective Calendar Day** basis, 2 Working Days after Authority approval.

This means that the Code would be aligned with the FAA interest calculation methodology for all Reconciliation Runs occurring on or after the Implementation Date. Parties would be able to raise Trading Disputes against the interest calculations for eligible historic Reconciliation Runs if they wished, as these would have been calculated in a manner which was inconsistent with the Code.

The **Alternative Modification** would be implemented **retrospectively** back to NETA Go-Live on 27 March 2001.

Under this approach it would be as if the inconsistencies between the FAA interest calculation and the Code had never occurred. If approved, Parties could not raise Trading Disputes against any interest calculations (past or future).

The Group has also considered but discounted:

- A prospective Settlement Day implementation for the Proposed Modification, under which the inconsistencies would only be removed for Reconciliation Runs for Settlement Days occurring on or after the Implementation Date.
- A different Alternative Modification which would retrospectively remove the inconsistencies from 9 April 2009 (the day that the Panel raised P235).

Section 4 in Part 2 of this document explains why the Group believes that these approaches would be less appropriate.



What are the Group's views?

The Group believes that both the Proposed and Alternative Modifications are better than the Code drafting, but that the Alternative Modification is best overall

Why will P235 be better than the existing Code drafting?

ELEXON, the Panel and the Modification Group agree that the interest calculation method used by the FAA is preferable to the Code requirements.

The Group unanimously believes that both the Proposed and Alternative Modifications better facilitate competition and thereby the achievement of **Applicable BSC Objective (c)**.²

This is because both solutions:

- Better reflect the principle behind the BSC's Reconciliation process (i.e. that Reconciliation Charges should adjust BSC Parties' payments as if the 'correct' monies had been exchanged on the Payment Date of the Initial Settlement Run) and the time value of money to Parties;
- Give a fairer and/or more accurate result for Parties than the existing Code drafting; and
- Avoid costs to Parties in changing their systems and processes to align with the Code.

The Group also unanimously agrees that both the Proposed and Alternative Modifications better facilitate the achievement of efficiency and thereby **Applicable BSC Objective (d)**.³

This is because they both:

- Reduce confusion;
- Promote clarity and transparency; and
- Avoid costs to align the FAA systems with the Code.

All industry respondents to the Group's consultation agree that both solutions better facilitate the achievement of the Applicable BSC Objectives when compared with the existing Code drafting.

You can find a more detailed explanation of these views in Part 2 of this document.

ELEXON has not identified any evidence that the BSC rules for calculating Reconciliation interest were intended to be different from the Pooling and Settlement Agreement. This suggests that the Code wording represents a drafting error and that the FAA calculation was the intended methodology for NETA.

155/06

P235

Assessment Report

7 May 2009

Version 1.0

Page 5 of 7

© ELEXON Limited 2009

² Applicable BSC Objective (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'.

³ Applicable BSC Objective (d) 'Promoting efficiency in the implementation and administration of the balancing and settlement arrangements'.

Why is the Group recommending a retrospective change?

The Group unanimously agrees that the Alternative Modification will better facilitate the achievement of Applicable BSC Objectives (c) and (d) when compared with the Proposed Modification.

This is because the Group notes that any Trading Dispute against interest calculations could, if upheld, change and redistribute Parties' past cash flows.

The Group believes that this poses a risk to Parties, as it:

- Creates uncertainty for Parties (with a negative effect on competition);
- Results in a less fair/accurate (and therefore anti-competitive) calculation of Parties' interest charged and/or received; and
- Has resource implications for ELEXON (reducing its efficiency in administering the BSC arrangements) and for Parties (who would have to reprocess invoices).

The Group believes that a retrospective implementation back to Go-Live is therefore appropriate and desirable in this specific case, because it gives absolute clarity and certainty that the methodology used since NETA was the intended and correct calculation.

The Group notes that the Alternative Modification is not a typical retrospective change, since it normalises the status quo and actually prevents alterations to Parties' historic cash flows.

These views are unanimously supported by respondents to the Group's consultation.

Sections 4 and 5 in Part 2 of this document provide a more detailed explanation of the Group's views.

4 Costs and Impacts

Will P235 impact any systems and processes?

No, as approval of P235 will align the Code with the calculation method which the FAA already uses. The only costs will be **3 man days** of ELEXON effort (equating to £660) to update the Code and the FAA Service Description, which is based on the Code drafting.

However, rejection of P235 could result in costs to the FAA and Parties to align systems and processes with the Code. Section 3 in Part 2 gives further details.

5 Group's Recommendations



The P235 Modification Group invites the Panel to:

- AGREE an initial recommendation that Proposed Modification P235 **should not** be made;
- AGREE an initial recommendation that Alternative Modification P235 **should** be made;
- AGREE an initial **prospective Calendar Day** Implementation Date for Proposed Modification P235 of 2 Working Days after an Authority decision;
- AGREE an initial **retrospective** Implementation Date for Alternative Modification P235 of 27 March 2001 (NETA Go-Live);
- AGREE the draft legal text for Proposed Modification P235;
- AGREE the draft legal text for Alternative Modification P235;
- AGREE that Modification Proposal P235 be submitted to the Report Phase; and
- AGREE that ELEXON will issue a P235 draft Modification Report for consultation and will present the results to the Panel at its meeting on 11 June 2009.

Recommendation

The Group unanimously recommends approval of the Alternative Modification, with a retrospective Implementation Date of NETA Go-Live

6 Further Information

You can find more information in:

Attachment A: Part 2 - Detailed Assessment

See this attachment for full details of:

- The Group's discussions of the areas set by the Panel in its Terms of Reference;
- The differences between the Code drafting and the FAA methodology (with worked examples and information on the materiality to Parties);
- The impacts, costs and implications of approving or rejecting P235;
- The effects and appropriateness of different potential implementation approaches;
- The Group's views against the Applicable BSC Objectives (including its consideration of the industry responses to its consultation); and
- The Group's membership.

You can download the full industry consultation responses from ELEXON's website [here](#).

Attachment B: Proposed Modification Draft Legal Text

Attachment C: Alternative Modification Draft Legal Text

See these attachments for copies of the Group's draft legal text.

155/06

P235

Assessment Report

7 May 2009

Version 1.0

Page 7 of 7

© ELEXON Limited 2009