



78/009

INTERIM REPORT for Modification Proposal P157 Replacement of current Supplier Charges rules

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RECOMMENDATIONS

The VASMG invites the Panel to;

- **NOTE** the contents of this Interim Report;
- **CONFIRM** the decision to seek an extension to the Assessment Procedure and request an interim report; and
- **AGREE** that the VASMG will complete the Assessment Procedure such that an Assessment Report will be prepared and submitted to the Panel meeting of 12 August 2004.

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¹ The current version of the Balancing and Settlement Code (the 'Code') can be found at www.elexon.co.uk/ta/bsc/el_docs/bsc_code.html



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SUMMARY OF IMPACTED PARTIES AND DOCUMENTS

As far as the VASMG has been able to assess the following Parties/documents have been identified as being potentially impacted by Modification Proposal P157.

Parties	Sections of the BSC	Code Subsidiary Documents
Suppliers <input checked="" type="checkbox"/>	A <input type="checkbox"/>	BSC Procedures <input checked="" type="checkbox"/>
Generators <input checked="" type="checkbox"/>	B <input type="checkbox"/>	Codes of Practice <input type="checkbox"/>
Licence Exemptable Generators <input checked="" type="checkbox"/>	C <input type="checkbox"/>	BSC Service Descriptions <input type="checkbox"/>
Transmission Company <input type="checkbox"/>	D <input type="checkbox"/>	Service Lines <input type="checkbox"/>
Interconnector <input checked="" type="checkbox"/>	E <input type="checkbox"/>	Data Catalogues <input type="checkbox"/>
Distribution System Operators <input type="checkbox"/>	F <input type="checkbox"/>	Communication Requirements Documents <input type="checkbox"/>
Party Agents		
Data Acquirers <input type="checkbox"/>	G <input type="checkbox"/>	Reporting Catalogue <input type="checkbox"/>
Data Collectors <input type="checkbox"/>	H <input type="checkbox"/>	MIDS <input type="checkbox"/>
Meter Operator Agents <input type="checkbox"/>	J <input checked="" type="checkbox"/>	Core Industry Documents
ECVNA <input type="checkbox"/>	K <input type="checkbox"/>	Grid Code <input type="checkbox"/>
MVRNA <input type="checkbox"/>	L <input type="checkbox"/>	Supplemental Agreements <input type="checkbox"/>
BSC Agents		
SAA <input type="checkbox"/>	M <input type="checkbox"/>	Ancillary Services Agreements <input type="checkbox"/>
FAA <input type="checkbox"/>	N <input type="checkbox"/>	Master Registration Agreement <input type="checkbox"/>
BMRA <input type="checkbox"/>	O <input type="checkbox"/>	Data Transfer Services Agreement <input type="checkbox"/>
ECVAA <input type="checkbox"/>	P <input type="checkbox"/>	British Grid Systems Agreement <input type="checkbox"/>
CDCA <input type="checkbox"/>	Q <input type="checkbox"/>	Use of Interconnector Agreement <input type="checkbox"/>
TAA <input type="checkbox"/>	R <input type="checkbox"/>	Settlement Agreement for Scotland <input type="checkbox"/>
CRA <input type="checkbox"/>	S <input checked="" type="checkbox"/>	Distribution Codes <input type="checkbox"/>
Teleswitch Agent <input type="checkbox"/>	T <input type="checkbox"/>	Distribution Use of System Agreements <input type="checkbox"/>
SVAA <input type="checkbox"/>	U <input type="checkbox"/>	Distribution Connection Agreements <input type="checkbox"/>
BSC Auditor <input type="checkbox"/>	V <input type="checkbox"/>	BSCCo
Profile Administrator <input type="checkbox"/>	W <input type="checkbox"/>	Internal Working Procedures ² <input checked="" type="checkbox"/>
Certification Agent <input type="checkbox"/>	X <input type="checkbox"/>	Other Documents
MIDP <input type="checkbox"/>		Transmission Licence <input type="checkbox"/>
TLFA <input type="checkbox"/>		
Other Agents		
SMRA <input type="checkbox"/>		
Data Transmission Provider <input type="checkbox"/>		

X = Identified in Report for last Procedure

N = Newly identified in this Report

² the PARMs system is a BSCCo run system and is impacted by P157.

1 DESCRIPTION OF PROPOSED MODIFICATION

1.1 Modification Proposal

Modification Proposal P157 'Replacement of current Supplier Charges rules', (P157), was raised on 5 January 2004 by EDF Energy. P157 proposes to replace the current Supplier Charges rules in Annex S-1 of the Code with a robust set of rules that adhere to the proposed criteria for a technique that would provide corrective measures suggested by the Volume Allocation Standing Modification Group (VASMG) during its work on Issue 6 (Supplier Charges).

The Proposer believes that a clear and readily understood set of rules should assist with the drive to improve the quality of data entering Settlement. The latest BSC Audit has been qualified and it is the Proposer's view that a major contributory factor to this was the level of poor data quality in Supplier Volume Allocation especially within the Non Half Hourly (NHH) sector. Supplier Charges are intended to be a corrective technique but the recent work of the VASMG on Issue 6 has raised serious concerns over the appropriateness of the current rules and their effectiveness as a corrective technique.

The Proposer considered that P157 better facilitated the achievement of Applicable BSC Objectives (c) and (d). The achievement of Applicable BSC Objective (d) - promoting efficiency in the implementation and administration of the balancing and Settlement arrangements, would be achieved by P157 since the quality of data entering Settlement will be improved through the introduction of a Supplier Charges mechanism that is easily understood and that provides incentives on Parties. The Proposer further argued that any mechanism that is effective in improving data quality should also better facilitate the achievement of Applicable Objective (c) – promoting effective competition in the generation and supply of electricity, and promoting such competition in the sale and purchase of electricity.

The Initial Written Assessment (IWA) was presented to the Panel at its meeting on the 15 January 2004. The Proposer raised Modification Proposal P157 so that the more detailed work required to implement a replacement to the current Supplier Charges rules could be undertaken and a solution could be decided upon, since no solution was recommended by the Modification Proposal. For this reason a 2 month Definition Procedure was recommended.

The Definition Report was presented to the Panel at its meeting on 11 March 2004. The Panel recommended that P157 be assessed fully during a three month Assessment Procedure. During the initial stage of the Assessment Procedure, the Group issued one consultation document to industry detailing its initial conclusions regarding the Proposed Modification and suggested alternatives. At its meeting on 13 May 2004, the Panel requested that the VASMG present an Interim Report at the next Panel meeting to enable the Panel to choose to seek provisional thinking from the Authority if necessary.

1.2 Proposed Modification

The VASMG developed the Proposed Modification for P157 in the following form:

There will be Supplier Charges on Serials SP01, SP02, SP04, SP08a, b and c. The former three will be charged on a £ per day basis and the latter three on a £ per MWh basis. The charges will be capped such that no Supplier shall pay more than 1%*Credit Assessment Price of its Supplier Take in any GSP Group. The funds collected will be used in the following manner. 10% will be circulated to all Trading Parties based on their Main Funding Shares. The remaining 90% will be redistributed in one of the following two methods (the former has been consulted upon the latter not):

- On a GSP Group basis to NHH Suppliers who have performed above average on SP08a for the GSP Group on a market share basis – this will be called the "average performance" option;

- Following a [12³] month period, a Supplier's performance is compared to its performance [12] months earlier (when the charge was accrued). If there has been an improvement the charge associated with that improvement is recouped by the Supplier. The remaining funds will be forfeited and redistributed to all Parties based on their Main Funding Share (as with the initial 10%) – this will be called the "bond rebate" option.

The Group have not currently agreed which of these options will form part of the Proposed Modification.

In addition there will be a facility for the Performance Assurance Board (PAB) to select particular Serials or market issues such that Suppliers' performances with reference to these issues are compared in named peer group comparison (pgc) tables that are published on the BSC Website. There will be rules outlined in the relevant Balancing and Settlement Code Procedures (BSCP) that will dictate how and when these pgc tables can be published.

³ This period can be amended as is considered appropriate

2 ISSUES RAISED BY THE PROPOSED MODIFICATION AND ASSESSMENT AGAINST THE APPLICABLE BSC OBJECTIVES

2.1 Supplier Charges

2.1.1 Serials

The VASMG considered Supplier Charges and concluded that they should be aimed at maintaining accuracy and timeliness of Settlement over a long period of time. The Group considered the Serials that the P99 Supplier Charges were applied to and discussed what changes if any P157 would make.

SP01 and SP02

There is currently a charge associated with these Serials which look at the timeliness of Performance Assurance Reporting and Monitoring System (PARMS) data provision. The Group considered that it was important to incentivise Suppliers to provide data in a timely manner; therefore they agreed that these Serials should have Supplier Charges attached.

SP04

This Serial is concerned with the timely installation of mandatory Half Hourly (HH) metering. The Group felt that it was important that Suppliers install HH metering for all sites/Premises⁴ over 100KW, therefore this Serial was also deemed by the Group to be appropriate for Supplier Charges.

SP08a, b and c

This Serial is concerned with the provision of accurate data based on AAs/Actuals into Settlements. Under SP08a, the Group felt that Suppliers ought to be charged if they fail to provide Annualised Advances (AAs) for 97% of Non Half Hourly (NHH) meters at Final Reconciliation (RF). SP08b is a charge applied to Suppliers who fail to provide actuals for 99% of HH meters above 100kW at the First Reconciliation Run (R1) –this Serial is for compulsory HH metering (MIST⁵). Finally SP08c is a charge applied to Suppliers who fail to provide actuals for 99% of HH meters below 100kW at RF – this Serial is for non compulsory HH metering (MOST⁶). The Group considered SP08a, b and c and deemed them appropriate to have Supplier Charges attached under P157.

Please note: Charges should continue to be applied to importing meters only on the basis that estimations of export are either zero or profiled using strict techniques.

2.1.2 Genuine pre-estimate of loss calculation

The Group considered the legal opinion regarding the requirement to set the charges that are applied to the Serials such that they are reflective of the genuine pre-estimate of loss. Any type of Supplier Charges regime that has a correlation between degree of under-performance and amount charged is a liquidated damage - no matter how simple or complex that correlation. A liquidated damage that is set prior to the charge being incurred must be a genuine pre-estimate of the loss caused as a result of under-performance.

With this in mind the Group went on to discuss potential components of a genuine pre-estimate of loss, considering the previous discussions that established this under the Pooling and Settlement Agreement (as part of the 1998 Programme) for the current Supplier Charges.

⁴ This will change if P124 is approved by the Authority but will not affect the Supplier Charges under P157.

⁵ MIST = Metering Inside Settlement Timescales

⁶ MOST = Metering Outside Settlement Timescales

Two members of the Group offered contrary legal opinions to that provided by BSCCo's lawyer. These opinions were considered and addressed by BSCCo. These opinions were reiterated in the consultation responses on central incremental costs and redistribution.

	Possibilities for inclusion
SP08 a, b and c	<ul style="list-style-type: none"> • <u>Value of volume of energy that is assumed to be uncertain</u> • <u>Cost of uncertainty</u> • <u>Cost of special meter read</u> • <u>Cost of Post Final Settlement Run</u> • <u>Central Incremental Costs</u> • <u>In-house Supplier costs to correct bad data</u>
SP04	<ul style="list-style-type: none"> • <u>Approximate price £y for procuring a CoP5 HH Metering system to represent the value of risk over x months. Hence a pre-estimate of loss of £y/x per month (to recover cost of installing appropriate systems)</u> • <u>Charge for uncertainty between HH and NHH metering (i.e. use of profiles)</u>
SP01 and SP02	<ul style="list-style-type: none"> • <u>Administration costs</u>

2.1.2.1 Methodology that the Group disagreed with and discarded

Cost of special meter read:

This was the addition of the cost of a special meter read to the genuine pre-estimate of loss. Initially the VASMG thought that this was an appropriate measure as it would incentivise people to read meters and is the cost that a Supplier had avoided and which resulted in an estimated value being entered into Settlement. However on reflection the Group considered that including this would not fit with a theory of genuine pre-estimate of loss, as it did not reflect the loss other Parties suffered but rather the opportunity cost to the Supplier itself.

Cost of Post Final Settlement Run

The Group considered whether this was appropriate for inclusion under SP08. It was thought that if used in association with the value of the volume of energy that is assumed to be uncertain, this might be double counting. However it was pointed out that the calculation of the value of the volume of energy that is assumed to be uncertain looks at the financial charge that having too many Estimated Annual Consumptions (EAC) has exposed others to via altered GSP Group Correction Factor (GCF) etc whereas the former assumes that if you have too many EACs at RF you are more likely to raise a Dispute to correct and thus require a Post Final Settlement Run. The Group however discounted this idea since the calculations would be inaccurate as Post Final Settlement Runs are not used to correct EACs alone.

In-house Supplier costs to correct bad data

The theory behind including this is that having incorrect data would lead to a NHH Supplier not reaching the 97% target at RF. If this data is not corrected and a customer changes Supplier, the Supplier will pass on this problem to the new Supplier. Thus Suppliers that do not reach the 97% target may fail due partly to having received incorrect data. This data is not then corrected due to the

cost of correction. Charging Suppliers this cost of correction would encourage them to correct in house data and hence not pass the problems on to the next Supplier.

The VASMG initially considered that this was a separate issue that was not appropriate for inclusion in the genuine pre-estimate of loss. In addition, the VASMG concluded that a realistic number to include in the genuine pre-estimate of loss could not be reached, since it felt that any numbers quoted by Suppliers (if at all) would be widely variable. These variable numbers are, in fact, realistic since it depends what errors there are in the data and how easy they are to correct. Following the consultation the VASMG discussed inclusion of this element again. See section 6.2.1 for details of this discussion

Approximate price £y for procuring a CoP5 HH Metering System to represent the value of risk over x months. This resulted in a pre-estimate of loss of £y/x per month (to recover cost of installing appropriate systems).

The Group did not think that taking into account the price of installation of HH Metering and communications system was appropriate for calculating the genuine pre-estimate of loss for SP04. The Group gave the same rationale for this as for rejection of the cost of a special meter read, above. It believed that this does not estimate the loss caused to counterparties as a consequence of underperformance, rather it is an opportunity cost to the Supplier itself.

2.1.2.2 Methods to be included or to consult on:

Value of volume of energy that is assumed to be uncertain – SP08:

The Group considered this to be an important component of the genuine pre-estimate of loss calculation for all SP08 Serials

This methodology assumes:

- The change in the overall volume between Initial Settlement Run (SF) and RF is caused by replacing estimates with actuals;
- The change in the overall volume therefore gives a measure of how much inaccuracy was in the SF estimates;
- The % volume change over the time period (SF-DF) was compared with the corresponding % change in estimates to get the average % volume change for % of estimate change;
- The level of inaccuracy in the estimates remaining at RF is comparable to that in the estimates replaced between SF and DF.

The calculations were performed separately for HH and NHH data for a sample of Suppliers in all GSP Groups over a two separate two month periods, May/June and October/November 2001. The calculations worked out the change in percentage estimates between SF and DF and the corresponding change in volume that these estimates were assumed to have caused. The average change in volume that a 1% change in the % of estimates brings about was calculated. The loss that this will cause other Suppliers in Settlement is calculated by applying a price to this volume. This price is termed the imbalance differential and was calculated as the average of the difference between System Sell Price (SSP) and Market Price, and System Buy Price (SBP) and Market Price, over a year from 11 March 2003 to 10 March 2004 inclusive. This value is used as it is assumed that a Party will have contracted its energy at the Market Price and the inaccuracy of another Supplier's estimation will push a Supplier longer or shorter and hence the difference between its imbalance charges and its contracted charges is used.

Examples of the £/MWh value calculated and the methodology are contained in Appendix 1 of this document.

Cost of uncertainty – SP08

The Group were inclined to view this as having minimal impact and were not certain it ought to be included in the genuine pre-estimate of loss calculation. However the Group decided it would consult industry as to its view of the size of this uncertainty and whether there was a suitable method of calculating it.

Several methods were discussed to try to cost in to the genuine pre-estimate of loss the fact that not reaching targets set at the relevant Settlement Runs makes Parties uncertain as regards the accuracy of Settlement and Parties try to offset this risk in some way. The Group discussed the two aspects of uncertainty that Parties would have to consider and which of these could be catered for in this aspect of the genuine pre-estimate of loss. There is the uncertainty in the GSP GCF⁷ as well as the uncertainty in imbalance payments. The former is considered small and insignificant in this context and the latter is dependent on SSP and SBP and therefore difficult to predict. The Group also discussed the Settlement Uncertainty Model (SUM) that originated from the difficulties that Financial Directors of companies (in this case Host Suppliers pre-1998) had trying to enter a prudent figure for Reconciliation Charges in their annual accounts. This uncertainty is not applicable to HH and also not necessarily appropriate for a genuine pre-estimate of loss calculation since it is accounting for variations in Reconciliation Charges rather than the uncertainty that data entered into Settlement (even after RF) is accurate.

The following methods were considered as ways to calculate the cost of this type of uncertainty to Suppliers:

- A) The Settlement timetable has been set such that there are target percentages that a Supplier ought to have settled on actual data at each Settlement Run. E.g. target AAs at SF = 3%, R1 = 17%, R2 = 43%, R3 = 78%, RF= 97%. This was the methodology used by the 1998 Programme.

It is assumed that the industry by accepting these levels and runs, also accepted that this would imply a certain accuracy of Settlement. (This assumes that Settlement is 100% accurate if all data entered is actual data). In other words, the industry has effectively set a price on certainty by deciding the number of Settlement Runs and the target percentages of actuals at each Run. However, it was considered that this price might not necessarily be cost reflective.

It is then assumed that if a Supplier does not reach the target percentages set, that Supplier is increasing the uncertainty of other Suppliers in relation to the accuracy of Settlement and since the industry has effectively set a price on certainty those who decrease it by a certain amount can be charged correspondingly.

See Appendix 2a of this document for further details regarding this methodology.

- B) The Group also considered the additional uncertainty that would be associated with Settlement in the case of nobody sending any actual data in. Some members of the Group suggested that there was little or no uncertainty currently but acknowledged that there might be uncertainty if performance levels across the industry were to drop considerably. The calculation that was considered looked at how to approximate the uncertainty in Settlement that would result from a large performance decrease. This methodology requires approximating the extent to which an EAC or estimate would be

⁷ The main causes of error in the GSPGCF are, Line loss factors, Profile errors, Data errors NHH and HH, Estimates HH and EACs NHH. The Group were considering uncertainty caused by the latter two.

more inaccurate were performance to drop (the assumption is a linear degradation in the quality of estimation however this is not necessarily the case). It also requires an assumption to be made as to the likelihood of performance dropping to such a level. No suggestion was given for this although it was thought that this would be very unlikely.

See Appendix 2b of this document for further details regarding this methodology.

- C) The Group further considered information regarding Suppliers' Internal Pricing Teams and how they cost uncertainty into their price calculations. All members agreed that the price contains some acknowledgement of the quality of consumption data of customers. However it was considered highly unlikely that any estimate of this would be submitted by Parties since it is highly commercially sensitive information.

See Appendix 2c of this document for further details regarding this methodology.

Central Incremental Costs – SP08

The Group considered the different aspects of the Performance Assurance Framework (PAF) costs and whether there would be any incremental costs due to Supplier under-performance. BSCCo presented a methodology that could be included which took into account the costs of PAF and BSCCo staff as well as additional effort spent on performance issues including the cost of Operational Support Managers (OSM). The former costs would not necessarily be avoided if performance on SP08 were to improve since other industry performance issues or areas of non-compliance might arise. Savings suggested are also based on the assumption that the relevant Standards are attained through the implementation of systems and processes that operate in compliance with the procedures outlined in the Code and do not lead to the subsequent creation of settlement error. The latter (including OSM) costs are value added services to aid participants in relation to performance issues, these costs would also not necessarily be saved but time spent by staff on performance issues would be used on their day to day work. BSCCo maintained that it was difficult to segment the cost into base costs and incremental costs and were the VASMG to use this as part of the genuine pre-estimate it would have to use either the total amount or an estimate of what would be incremental e.g. 15%. Some members of the Group were concerned that there were potential legal problems with including this as part of the genuine pre-estimate of loss. Two members of the Group offered such legal opinions and these were considered and addressed by BSCCo. The legal opinion provided by BSCCo was that the most important concept to note is simply that the charges levied must be a pre-estimate of the actual loss and that where it can be shown that a component of actual loss is an increment in the costs of administering the PAF in any way, then it is not only reasonable but necessary to consider this in formulating a genuine pre-estimate.

The Group considered that it was likely that a portion of the central costs was an increment necessary to deal with poor Supplier performance and that a reasonable percentage was 15%. This value was then divided by the amount of NHH or HH energy in a year (depending on whether it will be used for SP08a, b or c) to get a £/MWh value to add on. The Group consulted on this in its consultation to industry and the results of this and the conclusions reached are described below in Sections 7.1.2 and 7.2.1.

See Appendix 3 below for further details regarding this methodology.

Charge for uncertainty between HH and NHH metering (i.e. use of profiles) – SP04

The Group considered this methodology and agreed it was suitable.

The Group supported a methodology that would charge for the uncertainty between HH meter reads and the approximated data produced from profiles for NHH meter reads. In the event that a Supplier failed to install a HH meter at a 100kW site, the site would be traded on a profile and the error in the

allocated profile would feed into the GSP GCF reducing the accuracy of the bills of all the NHH Suppliers in that GSP Group. It was noted that profiling was designed for <100kW demand and errors would be introduced when applied to above 100kW Premises.

The analysis done was to take some examples of HH actual customer data and see what consumption would have been applied if they had used profiles. The difference or error was multiplied by the imbalance differential (average difference between SSP and market price, and SBP and market price) to get the cost of the error for the length of time of the data. This cost was divided by the number of days the data spanned, to get a cost per day value.

See Appendix 4 below for further details regarding this methodology.

Administration costs – SP01 and SP02

The Group considered this methodology and agreed it was suitable.

The current charge of SP01 and SP02 is £25 per day, per GSP Group which was based on the administration cost incurred if reports are provided late. Some of the VASMG believed that if the charges are removed, the non delivery of reports could become a problem and the escalation of a Party in the Performance Assurance Board (PAB) process is too draconian a measure for this Serial. Overall the Group believed that Parties should be incentivised to deliver reports that are accurate and timely, although some considered that the incentive should not be financial. In addition the charges on SP01 and SP02 seem to have worked in the past, in that a Party perhaps new to the industry may be late in one month and incur the charges but then will generally not repeat this.

It was agreed that administration costs were probably the only thing that was applicable for inclusion in the genuine pre-estimate calculation. The Group understood that under P99 charges to SP01 and SP02 were applied per GSP Group, per missing report, per day. The Group felt that this charge did not reflect a genuine pre-estimate of loss since administration costs of chasing up missing reports would not vary by GSP Group and by number of missing reports only by day. It thus considered that the charge ought to be applied per day. It used a cost of £400 per man day and assumed a 5% per day charge - £20 per day for SP01 and £20 per day for SP02.

(See Appendix 5 for a summary of the components of a genuine pre-estimate of loss for the Serials. This Appendix also contains a comparison with the current Supplier Charges.)

2.1.3 CAPS

There is a model and explanation located on the BSC Website in the P157 Modification area: http://www.elexon.co.uk/ta/modifications/mods_docs.html that can be used to look at the effect of caps on different Suppliers.

The Group discussed whether a cap on the amount of money to be paid in Supplier Charges was appropriate, given that the genuine pre-estimate of loss calculated for P157 was an accurate reflection of the loss caused by a Supplier's under-performance. The Group wanted to see how much a very small Party could be charged and whether the charge would be too much to bear if uncapped.

The Group were keen to retain the cap for a number of reasons:

- They felt it was unsuitable for commercial contracts to have limitless liabilities attached; and
- Although logically a cap may conflict with a genuine pre-estimate of loss, a lack of certainty in the effects of Supplier Charges makes a cap a good idea.

It is worth noting that SP08 is charged in proportion to size of Party i.e. the charges are in £/MWh.

SP01, SP02 and SP04 are however charged on a per day basis.

The Group considered the cap using a simplified model. Some scenarios are shown in Appendix 6a.

The Group decided to work out the cap value in a different way from how it is derived currently. Currently the monthly cap for each Supplier is its proportion of the GSP Group Takes' multiplied by the GSP Group monthly cap. The Group looked at how much a Supplier paid for its energy and then what the maximum amount it considered it would be able to cope with being charged by a Supplier Charge type scheme, taking into account the profit margin Suppliers make. The Group considered that 1% of the cost of the Suppliers market (NHH+HH) in a particular GSP Group was appropriate. This would be 1%*market share*price. It was suggested that a suitable price would be the Credit Assessment Price since this is derived from imbalance and market prices and is considered to represent the average cost of energy in the market as well as the fact that it is a fairly fixed number. Alternatively the weighted average Market Index Price over the period could be used. There was some concern about the choice of 1% - i.e. whether it was high enough and if so whether it would continue to be relevant – see analysis in Appendix 6b. The Group did however feel that 1% was significantly higher than the current cap and would therefore be applied less frequently whilst preventing limitless liability. There was a suggestion that this percentage could be reviewed from time to time by the PAB or the Panel to reflect ongoing changes in the market.

2.1.4 REDISTRIBUTION

There is a model and explanation located on the BSC Website in the P157 Modification area: http://www.elexon.co.uk/ta/modifications/mods_docs.html that can be used to look at redistribution.

90% of the funds received from Supplier Charges are currently redistributed back to Suppliers based on their market share within the relevant GSP Group. The other 10% is currently redistributed to all Trading Parties based on their Main Funding Share. Some members of the VASMG stated their view that the redistribution method ought not to be changed. Two reasons were given. That Supplier Charges genuine pre estimate of loss calculation was conceptually linked with the method of redistribution. It is reasonable to redistribute the funds in proportion to which Parties are damaged and it is inherent in the process of calculating the GSPGCF that Suppliers are "damaging" themselves. In addition, that it is not legally possible to extricate redistribution from the charge. See Section 7.2.5 below. The Group decided to look at the varying methods of redistribution, irrespective of whether it agreed that it should be changed. Several methods of redistribution were discussed by the VASMG:

- Net redistribution on performance alone - this methodology meant that Parties performing better would receive a greater share of the funds - this was discarded as it does not take into account market share of Suppliers.
- Net redistribution if a Supplier performed over the standard (proportional to market share) - this was discarded since a Supplier would only get money back if it was performing above the standard. If no Suppliers performed above the standard then no money would get redistributed. This could lead to windfall sums being received by Suppliers - in an extreme case a very small NHH Supplier with only 1 Metering System, that was reaching 97% AAs would receive all money for a GSP Group if no-one else performed well.
- Net nil own receipts – A Party would not receive any of its own money back. This money would either get redistributed to everyone else according to market share of the remainder or form a surplus. The former approach is problematic because small Suppliers may receive back very large sums of money whilst performing badly. The latter approach is problematic as the surplus would need to be used so as to ensure BSCCo accounts would net to zero.
- Net Redistribution to those performing over the average of the GSP Group based on market share – a Party would only get money back if its performance was above average. The funds would be divided between all those above average according to market share.

The VASMG decided that funds from all the Serials would be collected per GSP Group. The sum should be redistributed based on Supplier's NHH performance in the relevant GSP Group. The theory behind this is that any errors as a result of underperformance would feed into the GSP-GCF reducing the accuracy of the bills of all the NHH Suppliers in that GSP Group and not the HH Suppliers.

The latter "Net Redistribution to those performing over the average of the GSP Group based on market share" was deemed to be the best option and is termed "average performance" option throughout this paper. It is described in detail below in Section 7.2.5.

The VASMG considered how this option worked in the simplified model provided to them and compared it to the other options for redistribution that had been modelled. The Group agreed that this option accomplished two things. It encourages above average performance and thus would gradually work to encourage Parties to move above the average, hence increasing the average. Additionally it would also encourage eventual movement towards the target of 97%. The Group felt that this solution meant that revising the value of 97%, as a level below which Suppliers would be charged, did not need to be considered as the solution encourages an increase in the average performance and does not just target 97%.

2.1.5 90/10 rule

The Group considered why the rule for taking 10% of the funds received through Supplier Charges and distributing it to all Trading Parties exists. The reason one member of the Group remembered as accounting for this rule was as follows:

- 10% = to compensate against the increase in the level of central costs (Trading Disputes), which is split across all Trading Parties.
- 90% = to compensate against the NHH error from GCF

The Group decided that the theory behind giving all Trading Parties a portion of the costs was valid and although it considered the number to be fairly arbitrary, since there was a request to include 'deeper' costs the Group would leave this as it stands.

2.1.6 FORCE MAJEURE

The Group considered whether it required a further force majeure provision to that already extant in Annex S-1 of the Code. The Group referred to discussions under Modification Proposal P115 "Disapplication of Supplier Charges Under Certain Circumstances" (P115). The VASMG concurred with the views put forward by the P115 Modification Group that there is a link between Section S and Annex S-1 and hence a link between the obligations laid down in Section S2 and the Supplier Charges regime in Annex S-1 which describes how the Supplier carries out those obligations. Supplier Force Majeure can be applied to the provisions dealing with Supplier Liquidated Damages. Further provision was considered unnecessary by the Group since each force majeure occasion would by its nature be an unpredictable event therefore specifying anything would be difficult. The Group decided that this should be considered on a case by case basis and should be left to the discretion of the PAB/Panel.

2.2 Peer Group Comparison (pgc)

The Group then considered pgc tables and discussed what should be reported via this method. The Group decided that it was appropriate for the pgc tables to be used to tackle so called "hot" issues such as the audit issues highlighted by the BSC Auditor.

The Group discussed the following issues:

- What should be published;

- Where it should be published;
- What safeguards to put in place to ensure accurate data was published.

The Group considered which Serials and Audit Issues would be incentivised via publishing performance publicly in pgc tables. The group concluded that rather than choosing one or more issues for pgc, P157 should be used to introduce the provision within the Code to allow PAB to use pgc for issues it felt would be beneficial as part of the PAB escalation process. (See Appendix 7 below).

The VASMG also considered whether pgc should be named or unnamed. It was clarified that unnamed pgc already occurs and a Code change is not required to change the performance areas that pgc covers, hence under P157 only named pgc would be considered.

It was questioned whether pgc would be an incentive. One member suggested that the very fact that no one in the industry wants named, public pgc to be introduced is an indication of its likelihood to work since Suppliers seem to fear its effects. One member suggested that the fact that the press can have access to the pgc tables and may use the data to write articles and draw conclusions regarding particular Suppliers would provide an incentive. It was also suggested that PAB escalation is a painful process to go through and suggested that the Group should not underestimate the PAB escalation process as an incentive. It was pointed out that escalation to PAB is a strong "last resort" measure and incentive techniques that would encourage improved performance would be preferable. Pgc tables that name Suppliers will sharpen up the PAB process and thus aid the PAB in improving performance. One member believed that pgc would be a low cost tool and will not make performance any worse.

The VASMG also expressed a desire to have less rather than more pgc tables so that the usefulness of the tool is not diluted.

The VASMG considered that the following changes would be required:

Section J 1.4.2 of the Code will be amended such that for the avoidance of doubt pgc tables can be published publicly.

BSCP534 will also be amended such that when and where the pgc tables will be published is explained. The Group wished to cater for several risks via the content of BSCP534:

- 1) That the data is incorrect;
- 2) That Parties have no warning to improve before pgc published;
- 3) That Parties have no prior information telling them the standards to which pgc may be applied.

Wording could be inserted into BSCP534 and this would ensure that Parties were aware of the Standards they have to keep and the potential for pgc tables to be published on any of these Standards. The wording could appear thus:

"In addition to the pgc reports produced from the PARMS reports the PAB may also publish pgc on any performance matter affecting the industry, for the avoidance of doubt this includes all matters that the PAB are tasked with in accordance with Sections B-1, J, J-1, S-1 and any issues raising from the BSC Audit."

The pgc tables will be published on the BSC Website and will appear in the following format:

		GSP Group 1	GSP Group 2	GSP Group 3	etc
Party Name A	Supplier Id 1				
Party Name A	Supplier Id 2				

Party Name B	Supplier Id 1				
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The VASMG wished Party name to appear such that energywatch and other interested Parties could understand who the table was referring to, since Supplier Id is difficult for a non industry expert to work out.

The VAMSG also wished Parties to receive a copy of the data used to generate the information in the table (by email) xWD before publication with its name and position visible. It will thus have xWD to check and query the data. In addition, the Group also wished to include a proper appeals process. It was suggested that there is an appeals process already for PARMs data thus if this data is not queried then it can be assumed to be correct and hence used in a pgc table. If the data to be used is not PARMs data, then an appeals process is required. It is thought this could work similarly to the Query process for Supplier Charge reports contained in BSCP536.

The PAB will consider whether to use pgcs part of the escalation of a particular issue. The PAB shall notify industry via the Performance Assurance Administrator (PAA) y months in advance of a particular issue and data relating to it may be published in a pgc table of what data is to be used and the methodology for creating the pgc table. This notification period will not be for consultation but to allow industry to improve performance prior to publication of data

An example of a pgc table based on % AAs reached at RF for NHH and % Actuals reached at R1 for HH will be in an appendix to the BSCP534.

The VASMG also felt it appropriate to alter the PAB escalation table to include reference to pgc:

SEVERITY LEVELS TABLE

Under 'example activities' for Severity Level 4...'consider pgc'

Severity Level	Meaning	Example Issues	Example Activities
4	There is concern that without a change of approach or commitment, a severity 3 problem will not be resolved, or not be resolved within a reasonable timescale.	Energy settled on Actuals is unsatisfactory and the participant is not meeting pro-forma milestones to deliver improvements.	All activities for lower Severity Levels, <i>plus</i> Targeted Technical Assurance visit. Escalate to PAB. Feature in the Panel assurance report Consider publishing peer group comparison tables as described in section ???

2.3 Implementation Date

The Implementation Date recommended by the Group is a Calendar Day, July 2005 Implementation Date.

The advantages this has are as follows:

- Calendar Day implementation means that the old rules are stopped and the new ones started. There are thus no problems deciding how to combine the new rules with the old especially

regarding caps and redistribution which are calculated on a Parties overall position for any given month;

- Calendar Day implementation set for a future date means that Parties will know the rules in advance of the implementation. In this way the problem of lack of knowledge of obligations that would be associated with an earlier Calendar Day implementation (e.g. November 2004), is ameliorated;
- July 2005 Implementation Date allows pre P99 rules to be fully run off before P157 is introduced hence data used in P157 will be solely post P99 data; and
- Development can take place in the scheduled June 2005 Release, which will allow system and process changes to be made in the most efficient manner.

The other options available are below. Consideration was given to:

- How the new rules would interact with the old ones; and
- Development within a scheduled BSC Systems Release.

Date	Type of implementation	Pre P99	Post P99	P157	Comments
May 2004	Settlement Day	Run off	None	Staggered start	Retrospective What to do with caps and redistribution Code containing both rules?
May 2004	Calendar Day	No Run off	None	Start immediately	Retrospective Change 2 systems Not know on SD what obligations were
Nov 2004	Calendar Day	Short run off	Short start	Start immediately	Retrospective Change and integrate 2 systems Not know on SD what obligations were
Decision +	Settlement Day	Run off	Run off	Staggered start	3 systems 2 separate algorithms - messy What to do with caps and redistribution Code containing all rules?
Decision + i.e. Jul 2005	Calendar Day	Run off	14 month start	Start 14 months after P99	Retrospective but with warning to Parties from decision to implementation New P157 integrated with P99 system

					Simple change Development within SVA Jun 05 release
Two tier Decision + x Cut off old	Calendar Day	No Run off	Short start		Retrospective No run off needed
Jul 2005 Implement new	Calendar Day			new	Warning to Parties from decision to implementation Gap where no charges Development within SVA Jun 05 release

2.4 Assessment of how the Proposed Modification will better facilitate the Applicable BSC Objectives

The Group considered its initial opinion as to whether P157 better facilitated the achievement of the Applicable BSC Objectives.

The majority of the Group initially felt that P157 better facilitated the achievement of Applicable BSC Objectives (c) and (d) for the following reasons:

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;

Applicable BSC Objective d) - promoting efficiency in the implementation and administration of the balancing and Settlement arrangements.

The Group felt that if P157 improved performance and hence data quality in the industry then P157 would better facilitate the achievement of the Applicable BSC Objectives. This is because by improving data quality:

- The disincentive for a new Party to enter the market is reduced since there is less uncertainty in the market (c);
- Less time and money would be spent improving poor performance and dealing with data quality issues and Parties would thus save money and this would increase competition (c);
- The efficiency of BSCCo would be increased as less time would be spent improving poor performance and dealing with data quality issues (d);

The Group noted that these were its initial views and may be amended / revisited following receipt of the BSC Agent Impact Assessment if it felt that the costs outweighed the perceived or potential benefits.

2.5 Modification Group's cost benefit analysis of Proposed Modification

The costs for implementing P157 are still being finalised and hence no cost benefit analysis has been performed by the Group.

2.6 Alternative Modification

The Group considered potential alternatives within P157. Two alternatives were suggested.

One was to have a Supplier Charges module only i.e. omitting the pgc aspect of P157. This is due to doubts from some members of the Group as to whether pgc will be an effective form of incentive.

The other is setting the charges in the Supplier Charge module to zero. Those who considered this to be an appropriate alternative to consider did so because in their opinions the requirement to charge people a genuine pre-estimate of loss and not penal charges meant that the spirit of P157 – improving data quality – could never be fulfilled. This was considered to be especially the case by those who believe that conceptually and/or legally, redistribution of the funds received can not be changed from the current methodology i.e. it is tied to the genuine pre-estimate of loss.

The Group has not come to a final decision regarding whether either of these should form the Alternative Modification for P157.

2.7 Governance and regulatory framework assessment

During the assessment of the Proposed and Alternative Modification, the VASMG considered the wider implications of P157 in the context of the statutory, regulatory and contractual framework within which the Code sits, as is required by the Code (Annex F-1, paragraph 1(g)). The VASMG was of the opinion that, were P157 to be implemented, there would be no such wider implications.

3 COSTS

A full Impact Assessment is yet to be carried out.

The costs for progressing P157 through the Modification Procedures have been updated following the 2 month extension to the Assessment Procedure. The costs have increased from 80 man days to 105 man days. This is to reflect the additional analysis and modelling required during the next phase of P157.

4 RATIONALE FOR MODIFICATION GROUP'S RECOMMENDATIONS TO THE PANEL

The Group considered whether to suggest to the Panel specific questions regarding P157 and its progress that could be put to the Authority if provisional thinking were to be requested. The Group decided not to make any suggestions, although it acknowledged that the area of caps was a sensitive one.

5 IMPACT ON BSC SYSTEMS AND PARTIES

An assessment has been undertaken in respect of BSC Systems and Parties and the following areas have been identified as potentially being impacted by the Proposed Modification.

5.1 BSCCo

For the Supplier Charges aspect of P157 - there should not be any additional cost on BSCCo after the new system is implemented since the Supplier Charges rules will be amended but will run in a very similar way to currently. If the "bond rebate" redistribution method is used then there may be an impact on Supplier Charges billing.

If the PAB decide a certain issue is suitable for pgc tables to be published BSCCo will have to follow the new process in BSCP536 (annex 5 below). It will have to create and publish the pgc tables, provide Parties with prior warning of the data to be used and deal with queries and appeals.

5.2 BSC Systems

The Performance Assurance Reporting and Monitoring System (PARMS) will be amended in the Supplier Charges module. There will be no changes to the Serials and reporting aspect of the system but the charges, methodology for capping and the use of Supplier Charges funds will be amended.

System / Process	Potential Impact of Proposed/Alternative Modification
Reporting	PARMS system

5.3 Parties and Party Agents

The Supplier Charges rules will be amended such that Suppliers will be charged different amounts for the six Serials and will have new rules of redistribution and capping.

See Impact Assessments in annex 3.

6 IMPACT ON CODE AND DOCUMENTATION

6.1 Balancing and Settlement Code

Section J of the Code will be amended to allow, for the avoidance of doubt, named pgc tables to be published publicly. See annex 5.

Section S – specifically annex S-1 of the Code will be amended to incorporate the changes to Supplier Charges that will be introduced if P157 is approved by the Authority.

6.2 Code Subsidiary Documents

BSCP536 “Supplier Charges” will be amended to include provisions for pgc tables and instruction on when and how they will be used.

7 SUMMARY OF CONSULTATIONS

The sections referred to in the questions below are references to the consultation document issued to industry. See annex 4 for consultation responses in full. It should be noted that the “average performance” method of redistribution was consulted on in this consultation. The “bond rebate” method had not been discussed by the Group prior to the consultation being issued.

Consultation question	Respondent agrees	Respondent disagrees	No Opinion expressed
Do you believe Proposed Modification P157 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	5 (15) Qualified 2 (9)	2 (15) Qualified 1 (15)	1 (1)
<i>The questions below all refer to the genuine pre-estimate of loss calculation</i>			
Do you agree with the calculation of the value of volume of energy that is assumed to be uncertain as put forward in Section 2.1.2.2?	7 (26)	3 (28)	1 (1)
Do you consider that the cost of uncertainty as put forward in Section 2.1.2.2 should be included in the genuine pre-estimate of loss calculation? If so, are any of the methods suggested (A, B, C) relevant or can you state an alternative?	1 (9) Qualified 1 (15)	5 (20)	4 (11)
Do you agree that central incremental costs should be included in the genuine pre-estimate of loss calculation as put forward in Section	7 (26)	3 (28)	1 (1)

2.1.2.2? Please state rationale.			
Is the value of 15% put forward by the VASMG as a reasonable estimate for the increment in central costs appropriate? See Section 2.1.2.2 Please state rationale.	5 (22)	4 (31)	2 (2)
Do you agree with the method in which the genuine pre-estimate of loss for SP04 has been calculated? See Section 2.1.2.2 Please state rationale.	7 (26)	2 (25)	2 (4)
Do you agree with the method in which the genuine pre-estimate of loss for SP01 and SP02 have been calculated? See Section 2.1.2.2. Please state rationale.	6 (23) Qualified 1 (10)	3 (21)	1 (1)
<i>The questions below all refer to caps</i>			
Do you agree with the VASMG's decision to retain caps in Supplier Charges? See Section 2.1.3. Please state rationale.	8 (38)	Qualified 1 (15)	2 (2)
Do you agree with the new calculation that will be used to work out each Supplier's cap in the GSP Group i.e. 1% of Supplier Take in GSP Group * Credit Assessment Price? See Section 2.1.3. Please state rationale.	6 (31)	3 (22)	2 (2)
<i>The questions below all refer to redistribution</i>			
Do you agree with the suggested method of redistribution put forward by the VASMG? See Section 2.1.4. Please state rationale.	3 (11)	7 (43)	1 (1)
Do you agree with VASMG decision to leave the 90/10 rule as it is currently? See Section 2.1.4. Please state rationale.	7 (37)	3 (19)	1 (1)
Do you agree with the VASMG's decision to leave the current force majeure provisions in place? See Section 2.1.5.	9 (51)		2 (4)
Do you believe that Supplier Charges and the genuine pre-estimate of loss ought to be reviewed and if so how often? Please give rationale.	8 (42)	1 (9)	2 (4)
Do you agree with the VASMG's approach to peer group comparison – that it should be one of the tools available to the PAB to encourage good performance? See Section 2.2 Please state rationale.	4 (22)	5 (29)	2 (4)
Do you agree with the preferred P157 Implementation Date of Calendar Day July 2005 that is supported by the VASMG even though	7 (24)	1 (15)	1 (1)

<p>this is retrospective in nature?</p> <p>See Section 2.3</p> <p>Please give rationale.</p> <p>If you disagree please state preferred alternative and rationale.</p>	Qualified 2 (15)		
<p>Do you consider any of the alternatives suggested by the VASMG should be progressed?</p> <p>See Section 2.5</p> <p>Please state rationale.</p>	6 (39)	4 (15)	1 (1)
<p>Do you believe there are any alternative solutions that the Modification Group has not identified and that should be considered?</p> <p>Please give rationale</p>	6 (26)	3 (19)	2 (4)
<p>Does P157 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure?</p> <p>Please give rationale</p>	4 (30)	5 (23)	2 (2)

7.1 Modification Group's summary of the consultation responses

1 respondent made no comment throughout.

7.1.1 Applicable BSC Objectives

The majority of respondents agreed that P157 better facilitated the achievement of Applicable BSC Objectives c and d. Two respondents qualified their support.

- One claimed it would be acceptable, only as a package with exclusion of peer group comparison table; and
- Another claimed there was a need for further assessment in the area of redistribution.

Those who supported P157 did so for the following reasons:

- The current Supplier Charges are not proving to be effective as a corrective technique as performance is not improving in many areas. Immaterial/insignificant net charges are levied, and there is over-complexity and a lack of transparency of Suppliers' performance;
- P157 simplifies the number of charges to be applied;
- P157 should improve performance and hence data quality. This should reduce uncertainty within the market and less time and money should be spent on improving poor performance and consequently costs should be reduced;
- The recent qualified audit also indicates that Suppliers are not sufficiently incentivised to deliver expected data accuracy.

The minority of respondents did not believe that P157 better facilitates Applicable BSC Objectives (c) and (d).

Reasons given were that:

- The solutions proposed are not particularly clear or fair. Some of the Supplier Charges proposed are not a genuine pre-estimate of loss, and some elements of the 'genuine pre-estimate of loss'

appear logically unsound. Thus these aspects may be open to legal challenge, with a risk of losing this Performance Assurance technique and consequent risks to all market participants

- The redistribution method is unsuitable. One respondent believed that there is a clear link between the genuine pre-estimate of loss calculation and re-distribution, which is currently not met by P157. In addition, one respondent considered that restricting the payment of the 'compensation' to certain Parties appears to be discriminatory. One respondent believed that P157 did not give either clarity or incentives.
- There is no requirement for P157 now, since the industry is only now receiving invoices for the pre-P99 regime and therefore it is too early to judge what impact these charges will have on Suppliers' behaviour. In addition, P99 has only just been implemented so the industry are not yet able to judge what impact this will have on Supplier performance. Thus one respondent claims it has no standard against which to judge P157.

7.1.2 SP08 Genuine Pre-Estimate of Loss

Value of volume of energy assumed to be uncertain

The majority of respondents supported the calculation of the value of volume of energy that is assumed to be uncertain. The approach taken seems, according to one respondent, to be sensible in that it takes into account the variances between estimated and actual data between SF and DF and it is based on the assumption that the uncertainty in the Settlement bill is directly related to the change in the volume of estimated data versus actual data. There was however some surprise at the high level of this cost in the half hourly market. Further analysis was suggested and will be performed.

The minority of respondents did not support the calculation. Reasons given were that:

- It could depend significantly on the sample chosen (it may vary significantly by Profile Class/Standard Settlement Configuration (SSC) and GSP Group) as well as the behaviour of Suppliers in response to the change in the 'incentive'. In response to this concern the Group noted that the analysis used a sample of 8 Suppliers of differing sizes in all GSP Groups and was done at a Supplier level hence there ought to be no variation by Profile Class/SSC and GSP Group. In addition the Group agreed to carry out further analysis to increase the sample size;
- One respondent was concerned regarding SP08a that the value of the volume of energy assumed to be uncertain (£0.11/MWh) is half the incremental central costs (£0.21/MWh). In response to this concern the Group noted that central incremental costs are being reassessed by BSCCo – see Appendix 3;
- This respondent also expressed concern for SP08b/SP08c, the value of the volume of energy assumed to be uncertain (£4.43/MWh) seems very high. Again the respondent believes that more detailed analysis should be carried out. Additionally, this respondent stated that the value of uncertainty could not possibly be the same figure for both R1 and RF. There is a difference in magnitude of the impact to Settlements and on other Suppliers of the accuracy of Meter reads at R1 and RF that is not reflected in this figure. Parties contracting to accurate final outcomes will only be subject to cash flow variations in the interim Settlement Runs. Although it is desirable to have accurate actual data at SF, and an orderly progression to accurate Settlement at RF, inaccurate intermediate imbalance costs are not necessarily the cost suffered by other Parties. Therefore, Serial SP08b should be measured at RF, or its calculation should be based on the negative effect on cash flow.
- In addition, one respondent considered that data changes between SF and DF give an indication of estimations and errors at SF. However, it noted that the qualified audit suggests that even Supplier data in DF (Post-Final) runs are not meeting expected accuracy levels.

Cost of uncertainty

The minority of respondents agreed that this should be a part of the genuine pre-estimate of loss. One of these supported option A – (uncertainty at each Settlement Run) - and considered that one of the risks that a Supplier has to manage is the uncertainty in the final volume of energy that it will purchase for its customers. This respondent deemed the cost of uncertainty to be insignificant. The other respondent was unsure which option was most appropriate although it did have some sympathy with the thought process used for Option B – (uncertainty associated with no actual data entering Settlement). The majority of respondents thought it should not be included and 3 respondents did not express a definite opinion but made some comments.

- Several respondents believe that the cost of uncertainty is likely to be minimal and hence should not be included. One respondent noted that this was the opinion of the Group but said that the Group did agree that price contains some acknowledgement of the quality of consumption data of customers. This respondent considers that the cost of uncertainty should be included (even if it is found to be minimal) where there is a suitable method of calculating it. It would be interested to see whether any alternative methods are identified as part of this consultation;
- One respondent does not believe that any Party takes into account the cost of the uncertainty of Settlements being inaccurate;
- One respondent noted that none of the alternatives represent a clear and unambiguous methodology that can clearly justify the inclusion of this factor and would not be robust and unchallengeable.

Central Incremental Costs

The majority of respondents supported the inclusion of central incremental costs as part of the genuine pre-estimate of loss. Arguments in support of its inclusion were:

- Central effort required in the Performance Assurance Framework (PAF) would increase as Supplier performance deteriorates;
- All Suppliers have to meet the PAF costs and consequently those Suppliers who perform well are being subject to a genuine loss.

The minority of respondents did not support the inclusion of central incremental costs. Legal reasons were given and are detailed below:

- "The inclusion of central incremental costs is only right if they are caused as a direct result of Supplier underperformance. On this basis, we don't believe that the cost attributed to the OSM should be included – managing a Supplier's performance, and working to improve it, are already part of the OSM's responsibility, so we cannot see how an additional cost is incurred. The inclusion of additional costs incurred, perhaps due to special PAB meetings to discuss performance with a Supplier, could qualify, but in essence we expect that all of these costs would be covered within the annual BSCCo budget and so again should not be included. Our legal opinion supports this view on the basis that central incremental costs should not be included in the genuine pre-estimate of loss calculation, as they can in no way be credited as part of a Supplier's loss, and are purely consequential costs. The Modification Group had difficulty in measuring attributable central incremental costs, so again this would be open to challenge";
- One respondent consulted with its legal team and asked if a liquidated damage could include avoidable costs too, or must it be limited to a genuine pre-estimate of costs. They replied: This depends on how such a pre-estimate of loss is agreed to be calculated by the Parties. Under the current contract, avoidable losses such as the costs associated with the Board are not included.

Clause 1.3.1 states that the charges set out in the Menu of Supplier Charges represents a “genuine pre-estimate of the loss likely to be suffered by the Parties as a result of a failure by a Supplier to meet the applicable Performance Level and is reasonable in all the circumstances”, and further in clause 1.3.2 which states that “each of the Parties acknowledge that the charges in the Menu of Supplier Charges constitute the sole remedy of a Party in respect of any claim for damages arising from any failure by a Supplier to meet the applicable Performance Level or Serial”.

Given the above wording, it is clear that the intention between the Parties is not to include any losses other than those which result directly from the Supplier failing to meet the standards. To add in these extra costs of, for example, this Board would make the charges not limited to compensation, but penal too, as the Supplier which fails the most will contribute the most to the costs of this Board. Liquidated damages should be compensatory and not penal in nature, and it is for the claiming Party to prove that this is the case in the event of dispute.”

As regards the 15% - proportion of incremental central costs viewed as reasonable by the VASMG, The majority of respondents agreed with this amount (some of these expressed doubt of its source) and the minority of respondents considered that this was unjustified (one suggesting that an inflated figure of 50% seemed more appropriate). One respondent did not express an opinion. Comments included:

- It is difficult to assess this figure, and perhaps consideration should be given to consulting PAB as to what it deems reasonable. Having said that 15% does appear to be a ‘reasonable’ figure as clearly managing Suppliers poor performance will incur additional PAF costs;
- No exact calculation can be made but 15% feels intuitively of the right magnitude. Only BSCCo would be able to attempt such a calculation;
- We believe this is reasonable. There is no case to change away from the present assumption without an analysis of central costs by BSCCo. We do not think this to be necessary;
- The 15% weighting is arbitrary and cannot be justified - consequently it is difficult to comment on whether this is a reasonable estimate;
- It is not clear from the assessment report exactly which central costs have been identified as relating to the pursuit of SVA data accuracy. It is expected that costs would be considerably more than 15% of the PAF costs. If performance met original 1998 expectations, most of the PAF costs would be eliminated. In the absence of more information, 50% of PAF costs should be considered.

7.1.3 SP04 Genuine Pre-estimate of Loss

The majority of respondents agreed with the methodology suggested by the Group for calculating the SP04 genuine pre-estimate of loss. One reason given was that it seemed reasonable to charge for the uncertainty between HH Meter reads and the approximated data produced from profiles for NHH Meter reads. In addition this respondent believed that the price of installation of HH Metering and communications should be excluded (as is proposed), since this is not a loss caused to other Parties as a consequence of under performance used. Another stated that the proposed methodology was a suitable means of incentivising Suppliers to install a HH Meter at a 100KW site, thereby avoiding a site being traded on an inappropriate profile.

Several comments were made regarding the sample of data used for analysis. It was suggested that a larger sample could be used to validate this method, and that Customers across all Profile Classes 3 to 8 should be used. As a result the Group agreed to undertake further analysis across Profile Classes 5 and 7.

The minority of respondents did not support the methodology suggested:

- One respondent considered that the theory behind the calculation seemed to make sense i.e. comparing similar sized customers with or without HH Meters / profiles, but had the following concerns about the methodology which it felt would significantly compromise a genuine pre-estimate of loss for SP04:
 - the imbalance differential will change dependent on what period is used to calculate SSP and SBP;
 - this methodology would come unstuck for NHH sites with profiles where their consumption is away from the norm, for example, due to seasonal factors or, say, bakeries where the load differential is significantly different during the night and day.

The Group noted that the Customer data used was 365 day x 48 half hour matrix and the imbalance price applied was also 365 x 48 matrix, hence the change in imbalance differential by Period has been accounted for as has variation over the course of a year.

- Another respondent considered that using profiling data as the basis of these charges is not appropriate. Profiles in this context reflect at best the load shape of 100kW sites and are therefore unreflective of those sites significantly above 100kW. If load shapes are used for the basis of this charge it could be argued that there is already an incentive for Suppliers to install HH Metering at these sites. An alternative would be to weight the charge in line with the cost of installation i.e. to deter those Suppliers who deliberately trying to evade this cost⁸.

One respondent did not express an opinion. However, it commented that it seems rather harsh that a 99kW site/Metering System can operate permanently with a NHH Meter causing uncertainties with no charge, while a 101kW site with profiled values suffers charges. All NHH metering is estimated at a half-hour level, however, a site with HH metering has reduced uncertainty, and should expect to pay less towards the SVA arrangements, so the method suggested could be viewed as incentivising a Supplier to help itself.

7.1.4 SP01 and SP02

The majority of respondents agreed with the method proposed. Several had comments:

- One wanted to emphasise that failure to produce these reports under these Serials cannot be considered as a pre estimate of loss. However, there does need to be an incentive on Suppliers to produce these reports accurately and on time, and as the suggested charges to be applied seem reasonable, this seems preferable than the alternative, which is to escalate Parties to PAB;
- This is essentially an administration cost, and the methodology appears to reflect the actual work content;
- Qualified support was received from one respondent who commented that this seems a reasonable charge for the administrative costs caused by failure to comply with these Serials. However, it may be worth considering a change to the basis of charging (possibly with a smaller charge on a per Serial or per provider basis) to take account of the P99 data provision arrangements and overcome the problem that if one Agent fails to provide a report in a GSP Group there is then no incentive to ensure that any of the other reports are delivered;
- SP01 and 02 charging seems to have worked in the past;
- The method is clearer. The respondent accepts that an incentive on the timely delivery of reports is a good idea, however it doesn't want this to be the main focus of Supplier Charges, which should be accurate data.

⁸ The Group did not consider the cost of installation to be a genuine pre-estimate of loss and considered that the point of the charge was that profiles do not reflect sites above 100kW.

The minority of respondents considered this methodology was inappropriate:

- One respondent believes that PAB has the processes to manage under performance for these two Serials. It does however note that Liquidated Damages do incentivise performance in this area. These Serials are a measure of timeliness not accuracy;
- One respondent considered that although the existing charge did seem to have incentivised Suppliers to send in their reports promptly it did not believe such an administration charge was a genuine pre-estimate of loss since it is a consequential loss;
- One respondent disagreed with the changes made to the charging of SP01 and SP02 by the VASMG away from being on a per GSP Group basis. This respondent was of the opinion that since reports are required by GSP Group, and central effort to obtain them will be focussed by GSP Group, there is no reason to move away from charging by GSP Group and day. The charge needs to be large enough to avoid the situation where a large Supplier or a Supplier with a large error avoids or delays other charges by failing to submit PARMS data.

7.1.5 Caps

The majority of respondents agreed with the initial decision of the Group to retain caps. One respondent expressed concern as to why Ofgem were so clearly opposed to the retention of the cap.

Arguments given in favour of a cap were as follows:

- One respondent considered that although ideally there would be no caps, and the charges simply would reflect costs to other Parties, on the basis that the real costs to other Parties are very difficult to determine, and that the estimated costs may be determined pessimistically, it accepts a cap on charges as a compromise;
- Uncapped liabilities would act as a barrier to new entrants and therefore restrict competition.
- Backing off liability through renegotiation of the Agent contracts may prove a struggle and would certainly result in higher Agent fees for everyone, which would ultimately be passed on to the Customer;
- Removal of the cap could lead to limitless liabilities and therefore could exceed a genuine pre estimate of loss - if the cap was removed there would be a risk of straying into the areas of 'penalties'. In addition unlimited liability is unsuitable for commercial contracts;
- Caps need to be set to cover exceptional circumstances, not to be invoked on a regular basis;
- Since there has been limited analysis and discussion of the likely behaviour of the new Supplier Charges and re-distribution, caps are an essential safety mechanism.

One respondent gave a qualified negative response claiming that caps may not be required if the final set of Supplier Charges and the re-distribution method are consistent with a genuine pre-estimate of loss, reflect what liquidated damages are all about and are not at all penal. (This respondent supported retaining the existing re-distribution method).

One respondent gave no opinion but quoted its response to the Definition Consultation in which it supported the removal of caps so that Suppliers would be exposed to the full effect of the Supplier Charges. It also notes that Ofgem has expressed strong views on caps. In its decision letter on P115 Ofgem notes "the impact of caps in diminishing both the incentives and the status of Supplier charges as a genuine pre-estimate of loss". It also goes on to state that a 'level of error that would result in a Supplier exceeding its cap will not be reflected fully in the Supplier Charges, although other participants will have incurred a financial loss'. In considering whether caps should be retained the respondent believes that the Group should consider whether the removal of a cap would have an adverse effect on competition, in particular whether the removal of caps would increase barriers to entry and

consequently deter new entrants. If it can be established that the removal of caps would not have an adverse impact on competition then it would support removal of caps.

Additionally it notes that Ofgem will need to consider the impact of P157 on small businesses. It suggests that the Group considers how a revised cap or the removal of a cap would impact different Parties and in particular what impact it would have on smaller businesses.

The majority of respondents supported the VASMG revised method of calculating caps ($1\% \times \text{Supplier Take} \times \text{Credit Assessment Price}$). The following reasons were given:

- The figure seems reasonable when taking into account Ofgem concerns about applying a cap, in that 1% is higher than the current cap, and therefore it would be applied less often, whilst at the same time preventing the limitless liability which is a major concern. The application of a Credit Assessment Price seems reasonable in that it represents the average cost of energy as it is derived from imbalance and market prices;
- If a cap is retained the suggestion appears to be a reasonable approach and is reflective of a Supplier's dominance in any GSP Group;
- The value suggested represents a compromise, which should be subject to periodic review;
- Modelling indicates that that this level is suitable such that the cap is only triggered in exceptional circumstances. In addition using the Credit Assessment Price – an established Code value is useful.

The minority of respondents did not support the cap calculation suggested by the VASMG:

- One respondent considers 1% is too extreme a jump.
- Another respondent considers that the proposed cap is far too high. The fundamental rationale behind Supplier Charges is that (for NHH) 97% of the Meter reading should be actual by RF. The implication is that inaccuracies will arise due to the Meters for which actual reads are not available. It is not credible that the error that can arise in this remaining volume will get anywhere near 1% of a Supplier's total volume in a GSP Group. This respondent believes that the cap should be reflective of the likely outer bounds of the volume of inaccuracy. It therefore finds the proposed cap unacceptably high and want to see the cap reduced by a factor of 10;
- Another considers the 1% figure to have some of the desired properties but that it is essentially an arbitrary figure that would be unlikely to be able to withstand a legal challenge.

Allowing the PAB/Panel to change the level of the cap was also commented on:

- One respondent believes that the caps should only be changed via formal industry change and not at the discretion of PAB;
- Another considers that the provision that allows PAB/the Panel to change this level without going through the modification process also appears to conflict with the concept of a genuine pre-estimate of loss, and would therefore be open to legal challenge.

One respondent did not express an opinion, but commented that if caps are to be applied, the proposed methodology is an improvement on the existing method of determining the cap. It noted that there was some concern amongst the Group as to whether the percentage of Supplier Take was high enough. The revised limit is around three times higher than the current cap and it would appear from the model supplied that the likelihood of a cap being breached is much reduced. Given the concerns that Ofgem has raised previously concerning the retention of caps, the respondent suggested that the Group consider the merits of applying a higher percentage of Supplier Take.

7.1.6 Redistribution

The minority of respondents supported the suggested redistribution method:

- The suggested method of redistribution should yield an improved incentive on Suppliers, when compared with the present method;
- Net redistribution to those performing over the average of the GSP Group based on market share should be seen as an improvement on the current baseline. It should encourage Parties to perform above the average and hence increase the average.

However one of these respondents wanted to see the VASMG give more consideration to how it will work in practice. This is because in each of the GSP Groups, there will be a dominant Supplier (the original PES) and the next largest Supplier is likely to be the same brand across all GSP Groups. The Group therefore need to examine and be confident that the method for re-distribution of monies gives a fair balance of incentive versus reward between all Suppliers.

The majority of respondents did not support the redistribution method. Several reasons were given:

- One respondent sought legal advice on the collection and redistribution of Supplier Charges (genuine pre estimate of loss). The response from its legal team was as follows;

“These are linked under the current Annex S-1. The Performance Assurance Board (the “Board”) collects the charges and distributes them in a 90:10 ratio between the qualifying Suppliers and qualifying Trading Parties respectively. The collection and redistribution of charges should be linked as it provides a clear connection between the charges collected and the Parties which receive compensation as a direct result of a failure by a Supplier in meeting the applicable Performance Level. To remove the link weakens the compensatory requirement of liquidated damages and as a result the charges could be argued to be penal in nature.”

This respondent did however consider that if the redistribution method could be legally amended the suggested method was suitable since it provides an incentive both to be above average and to improve to the standard of 97%;

- Whilst the concept of redistributing funds to only those Suppliers who are on or above the average target would appear to act as a good incentive to drive up performance, this could lead to anomalies between large and small Suppliers. In particular on those Suppliers that were formally the host PES in a GSP Group, as it is these Suppliers which in essence will set the target average, thereby potentially skewing the results for the other Suppliers within a GSP Group. This will not produce the simplicity or the incentives outlined as an objective of the Modification Proposal. It does not meet the BSC objectives of promoting competition or increasing efficiency. As a result, further work needs to be done by VASMG in this area;
- Collecting on one basis and redistributing on another may cause anomalies in a number of instances and may provide an opportunity for gaming. For example, a company operating under more than one Supplier ID could transfer “problem” MPANs from one ID to the other in order to recover a proportion of the overall Supplier Charges incurred and thus ensure the funds back are maximised to the company as a whole. This could be significant if other Suppliers are below the target 97% and there is a large pot of Supplier Charges;
- In principle, ‘good’ performers are those which are suffering ‘damages’ and should be recipients of a share of the amounts collected from ‘poor’ performers. However, there are some concerns that referencing ‘good’ and ‘poor’ performance to an average performance in the GSP Group could create artificial step differences in charge redistribution. The level of performance should be taken into consideration more precisely, for example in a combination of total GSP volume (or share) and performance relative to average;

- Redistribution forms a key part of the Supplier Charges regime, and implementing a method that means some Suppliers will not receive damages due to them is fundamentally wrong. Any Supplier that is underperforming is obviously damaging other Parties, but it is damaging itself within the calculation of GSP GCF. This Supplier is also being affected by the underperformance of other Suppliers, and should be compensated for this regardless of its own performance. The redistribution method therefore should ensure that all Suppliers are compensated correctly on the basis of the genuine pre-estimate of loss incurred;
- The proposed method is flawed as it rewards Suppliers who are still performing below the target level of performance (currently 97%);
- The method outlined (which would compensate some Parties but not others for the impact of a Supplier's non-performance) is discriminatory and undermines the concept of liquidated damages.

7.1.7 90/10 Rule

The majority of respondents agreed with the initial decision of the Group, to leave the 90/10 rule as it is currently:

- There is not sufficient justification for adjusting the 90:10 rule at present, particularly as the 10% is to compensate the increase in central costs which is split across all Trading Parties not just Suppliers;
- As all Trading Parties are contributing to central administration costs it seems reasonable to take out a nominal 10% to compensate all Parties, 10% feels intuitively the right magnitude;

However, one respondent who supports the view of the Group believes that the 90/10 rule does have the potential to be contentious if it is not based on consideration of what proportion of under performance impacts other Suppliers through the GSP GCF and what proportion impacts all Trading Parties through an increase in central costs.

The minority of respondents considered that the rule ought to be changed:

- One suspects that the true full costs of the arrangements required to monitor, investigate and rectify SVA Supplier performance deficiencies is not being fully reflected on the Parties responsible. An increased share of the amounts collected should be apportioned to all Trading Parties to rectify this situation. In the absence of more information on costs, this respondent suggests 25% should be allocated to all Trading Parties, as a compromise;
- One prefers an 80/20 split on the basis that it would be a greater incentive on the NHH market to perform and it would mitigate against the increased liquidated damage in the HH market;
- One is unclear why this rule is in place. This respondent stated that the Group were unable to clearly justify its existence, and therefore this element should be removed.

7.1.8 Force majeure

All respondents who commented supported the VASMG's decision to leave the current force majeure provisions in place:

- It is good practice to have these and they are an essential part of any reasonable arrangement;
- The existing force majeure clauses within the Code adequately cover events that could impact on the performance of a Supplier;
- Force majeure is by its nature, unpredictable therefore trying to specify anything would be difficult;

- The Authority's decision on P115 states that 'the effectiveness of the incentives to try to resolve the underlying issues that cause underperformance would be eroded if a process was in place to disapply Supplier Charges'. Further force majeure provisions are not required. It may be appropriate to review them however if there is any evidence to suggest that they are being subject to abuse.

7.1.9 Reviewing Supplier Charges

The majority of respondents considered that reviewing Supplier Charges and the genuine pre-estimate of loss was a good idea. Various timings were suggested ranging from annual reviews to every three years or when there was a material change in the market. Reasons given were:

- It does seem appropriate to periodically review Supplier Charges and the genuine pre-estimate of loss but this should be balanced against providing Suppliers a degree of certainty over what charges will be applied. It may be appropriate to undertake a review every 2-3 years unless an exceptional event suggests that an earlier review would be appropriate;
- As the Settlements process takes 14 months from SF to RF, clearly it will take time to assess the effectiveness of the new Supplier Charges. A review every two years seems to be the right balance between accuracy and effort;
- Reviews should take place as regularly as required, probably annually, to ensure accuracy and currency and also to avoid complacency amongst participants. P157 has highlighted crucial issues surrounding performance and Supplier Charges;
- Supplier Charges should be reviewed when market forces dictate and on the basis of what the Customer requires. If performance is not being readily achieved it should be reviewed regardless of any timescales. This right to review should be the responsibility of the PAB and / or BSC Panel;
- Reviews should only be carried out where a material change to the market (including technology) means that current arrangements are no longer efficient or effective as they were before the change. Frequent reviews represent a cost to the market and are usually accompanied by increased risk.

The minority of respondents felt that it was unnecessary to prescribe for a review, since it remains the gift for any Party to raise a Modification Proposal if it is concerned.

Two respondents had additional comments to make.

- One considered that it does not seem right that the applicable charges are automatically increased each year, in line with RPI, when the loss is based on costs which are unrelated to RPI. Any charge that is deemed to be a 'genuine pre-estimate of loss' should be calculated as such;
- Other central costs, if included, should also be reviewed annually, particularly as BSCCo have budgeted for considerable cost savings in forthcoming years.
- Presumably the cap will change as the Credit Assessment Price changes.

7.1.10 Peer group comparison

The minority of respondents supported the introduction of named pgc along the lines suggested by the VAMSG. The following comments were made:

- In particular this should be used to address any issues highlighted by the BSC Auditor.
- It should be a tool available to PAB as part of the escalation process and should be used to support other financially based incentives. There needs to be adequate warning, protection and appeal procedures for it to be respected within the industry, and for it to be effective. Robust

processes can be put in place to ensure that the information presented is accurate. PAB should be given flexibility to decide what information should be presented;

- This approach is low cost and can only increase the focus on the need for Suppliers to address performance issues;
- It is an additional corrective technique that should be available to the PAB;
- The information may be useful to Ofgem as part of its market monitoring work and potentially in its compliance and enforcement work.

In addition it was commented that the provisions for prior review and appeal before publication are critical and that Parties must clearly be made aware of standards they have to achieve before any figures are published.

The majority of respondents did not support named pgc for the following reasons:

- One or two discrete performance measures would be put into the public domain with the potential for editorial comment to undermine the whole organisation. This would create new and unwelcome Public Relations issues for a Supplier to deal with and therefore detract its focus from issues of data quality;
- This approach does not work well for participants that have low market shares;
- There is no evidence that pgc will have a marked effect on Supplier performance. Introducing this will increase BSCCo's administrative burden and inevitably costs, but will not deliver any justifiable benefit;
- PAB already have the ability to do coded pgc and this has not been fully utilised yet;
- Accuracy of pgc data is questionable;
- There are issues with regards to commercial confidentiality and legal questions over the right to data and use of information. It is unlikely to take account of the fact that a Supplier may have 10 sites or 1,000,000 sites, with the result that the headline figures are skewed in some way;
- PAB already have a variety of options within the current escalation process, pgc adds no additional benefit;
- The full effect of the recent PAB escalations has not been seen - the PAB escalation route is, and always will be, a stronger incentive to Suppliers to improve their performance;
- Agent market is not fully developed. Agent performance (in particular for small Suppliers) can be difficult to influence. With limited competition, Suppliers cannot simply switch agents if the service they provide causes poor performance. It has been suggested that where there is competition, Agents will serve larger clients better/faster for fear of losing the account therefore smaller Suppliers will always be at a disadvantage. Smaller independent Suppliers cannot afford to set up their own DC/DA business if one or more GSP Groups prove troublesome;
- The real issue is the impact in Settlements and the consequential effect on other Suppliers, but pgc will not provide any additional insight into these areas.

Several respondents expressed desires that should pgc be introduced:

- PAB must have structured pgc escalation process;
- It should only be used where it is clear that it will be more effective than other methods;
- It must recognise any commercial confidentiality;
- It must be accurate;

- There must also be a route of appeal for Suppliers to question the validity of their being named and for what.

One respondent did not express an opinion but commented that it believes there should be full transparency of performance on a routine basis. This would permit objective comparison, and allow attention to be concentrated on those Parties with problems. Anything short of this it believes to be for the benefit of Parties with poor performance.

7.1.11 Implementation Date

The majority of respondents agreed with the VASMG suggestion of a Calendar Day Implementation Date of July 2005. Two of these qualified their responses. One stated that this was the least disruptive option, however, the later any decision by the Authority to implement P157, the more decisions/actions will already have been taken by Suppliers which could have differed if they had been aware of the change. The other stated that if the Proposed Modification is amended or an Alternative Modification developed, a more suitable date might be found.

Other reasons in support of this date were:

- It is set in the future, therefore it gives all Parties an opportunity to address issues and Suppliers will have fair warning of the new rules in advance of implementation;
- The added benefits are that it allows pre P99 rules to be fully run off before P157 is introduced, which avoids any confusion and is a cleaner solution as all data used will be post P99 data;
- Calendar Day implementation has the advantage that there are no problems deciding how to combine the new rules with the old, especially regarding caps and redistribution which are calculated on a Party's overall position for any given month;
- Although P157 should be implemented as soon as possible there are difficulties concerning alternative Implementation Dates;
- Although retrospection should generally be avoided one respondent considered it to be justified in this instance.

One respondent in support of the date commented that it does not support retrospective modifications with material impact on Parties, and believes the Implementation Date should be tied to the Ofgem decision date in order to avoid significant retrospection, bearing in mind that not all of the chargeable Serials have significant lead times.

The one dissenting respondent believed that whilst it can see the benefits associated with the approach chosen by the Group, if the result of this modification is a more accurate, more reflective, regime of Supplier Charges, it should be implemented at the earliest practical opportunity. If a decision is reached quickly, November 2004 would seem to be the most practical option.

7.1.12 Alternative

Two alternatives were put forward by the VASMG in its consultation:

- Setting the charges in the Supplier Charges to zero; and
- The Proposed Modification without pgc.

1 respondent considered the former was a good alternative, (another gave qualified support for this approach), and 3 respondents considered the latter was a good alternative.

Support for setting Supplier Charges to zero:

- The industry should use other methods to encourage performance improvements;

- No Supplier charges are imposed in Scotland and it is believed that the market's average Performance Level there is similar to England & Wales. This seems to indicate that Supplier Charges do not necessarily have a marked influence on a Supplier's level of performance

Support for the Supplier Charges Module only was due to:

- Industry having yet to see benefits of current PAB 97% escalation process or the benefits of P99 introduced on the 1st May 2004;
- Lack of conviction that pgc has any value.

A number of respondents also provided comments about the redistribution method suggested in the consultation document, in particular the "bond rebate" option that was not issued for consultation but was circulated to the Group during the consultation period. The comments are as follows:

- One respondent believes that there may be further scope in the design of a method of re-distribution of Supplier Charges. This will be a sensitive issue between Suppliers, and it will be important to secure the confidence of all Suppliers that the method is fair;
- Further work on re-distribution may be required to avoid anomalies and possible gaming;
- the objectives of the Modification Proposal would be better achieved by means of a "Performance Bond" methodology as described in John Sykes' paper to the VASMG dated 19 May 2004;
- A modified version of the proposal without the restriction on re-distribution, without the provision for the Panel/PAB to vary the cap percentage and with appropriate changes to the rationale for the genuine pre-estimates of loss to make these legally robust.

Finally a number of other comments were made:

- Consideration should be given for Agents to be licensed and Supplier Charges passed directly to them if identified as the cause. This would directly encourage Agents to improve performance/service levels to all Suppliers;
- Financial sanctions via Supplier Charges could be abandoned altogether, and replaced with stricter escalation procedures against persistent offenders from PAB to Panel. Although, consideration would need to be given to ensure such a process was not draconian, and was more reflective of the impact of a Party's poor performance on other Parties;
- Consideration should be given to reviewing some of the targets e.g. 97% of actual NHH data at RF, as clearly larger Parties are struggling to meet this target.

Those who did not support an alternative considered:

- The suggested alternatives do not provide better mechanisms for incentivising better performance;
- Abolition of Supplier Charges is not an acceptable or credible course of action at this time;
- Effective financial incentives will be an important corrective technique within the Performance Assurance Framework;
- There is support for the introduction of named pgc;
- Other solutions to the overall problem of data timeliness and accuracy could be considered, but are outside the scope of this modification, and would undoubtedly be expensive.

7.1.13 Comments

A number of respondents provided additional comments as detailed below:

- One respondent support measures to incentivise improved Supplier performance, and believes the outline proposals can help this. However, other performance failings, particularly erroneous registrations and erroneous data such as those which caused the audit qualification and require considerable effort to rectify, will not be directly captured by the current Supplier Charges mechanism. It considers that either:
 - Measures are required to improve data accuracy in these areas; or
 - Costs of failing to provide accurate data should be borne entirely by those causing them, and not shared between all Parties.

Hopefully, revised charges will increase incentives to deliver accurate and timely data under the chargeable Supplier Serials, and this will carry over into other areas of Supplier data processing;

- It is believed that there is insufficient competition in Agent Market for Suppliers to have a choice. Consideration ought to be given as to how to encourage competition and improve service levels in the Agent market as this is at the heart of the Supplier Hub concept. Without this Supplier Hub management may fail;
- It is difficult to estimate true loss to Parties and therefore any solution can only be seen as, at best, a “gesture of goodwill” rather than actual loss. The genuine pre-estimate of loss is a difficult calculation to make but it must be made to ensure fairness and legality. It should also be borne in mind that any true loss would also include impact of poor performance on areas such as cash flow, etc. which would be difficult to calculate as part of a genuine pre-estimate of loss;
- It is also a concern that the current Supplier Charges set up has not been allowed time to work – this proposal is seeking to change a regime that is only just starting to have a real effect with the recent issue of the first few monthly invoices. The industry has not therefore seen what effect these invoices are having, or will have, on Supplier’s behaviour. Changes under P99 have only just been implemented and again the industry does not know how successful or otherwise these will be. However, if the effect of these changes is to give a better pre-estimate of loss, then they should be implemented at the earliest practical opportunity;
- The Group may wish to consider whether it would be useful to seek a provisional view from the Authority on particular aspects of the modification (for example how retention or removal of caps better facilitates Applicable BSC Objective (c));
- The BSCCo BSC Review has not been completed yet and this may aid development of this proposal. The same applies to the financial/performance benefits from P99 introduction.

7.2 Comments and views of the Modification Group

7.2.1 SP08

Value of volume of energy assumed to be uncertain

The Group considered the consultation responses that commented on the charge associated with SP08b. The Group and the respondents were all surprised at the magnitude of the charge and suggested some further analysis be done. One member considered that it was more appropriate to look at changes in volume between R1 and RF since estimates in the HH market are more uncertain than in the NHH market and these will have been replaced by R1.

The Group then considered the nature of estimates and that prior to CP696 “Allow the Half Hourly Data Aggregator (HHDA) to apply a default value where no consumption data has been provided by the Half Hourly Data Collector (HHDC)” there were more zero estimates entering Settlement at SF and that this could be the cause for the large volume change. Post CP696 default values are being used in

Settlement thus using data from after the implementation of this CP will lead to a result more realistic to current trading arrangements. This new data analysis was requested by the Group.

Cost of uncertainty

The Group considered the cost of the forecasting systems used by Parties as well as the data given to traders to use in trading. The Group considered whether the cost associated with forecasting systems used to reduce the uncertainty for each Party was appropriate for inclusion. The Group concluded that this was unsuitable since the investment to improve the accuracy of forecasting systems is justified primarily by avoiding imbalance charges, not by reducing uncertainty. In addition the Group did not think that the methodologies suggested in the consultation paper were apt and therefore the inclusion of any of these would not be open to challenge. Since the Group were convinced (as well as many respondents) that this was a small amount and all Parties were affected to the same extent, it was decided that the cost of uncertainty would not be included in the genuine pre-estimate of loss for SP08.

Central Incremental Costs

The Group considered the different consultation responses as to whether there were incremental costs centrally due to Supplier under-performance. The Group considered the potential legal problems posed by respondents regarding including this as part of the genuine pre-estimate of loss. It also considered BSCCo's legal advice, that the most important concept to note is simply that the charges levied must be a pre-estimate of the actual loss and that where it can be shown that a component of actual loss is an increment in the costs of administering the PAF in any way, then it is not only reasonable but necessary to consider this in formulating a genuine pre-estimate. The Group concluded that in its opinion there was an increment centrally that could be attributed to under-performance of Suppliers. The Group were in agreement with the respondents that BSCCo were in the best position to decide a suitable percentage of its central costs that are deemed to be incremental. BSCCo have taken away an action to estimate this.

In-house Supplier costs to correct bad data

It was queried as to whether the Group had considered this aspect in enough detail and whether it ought to be included in the genuine pre-estimate of loss calculation. The theory behind including this is that having incorrect data would lead to a NHH Supplier not reaching the 97% target at RF. If this data is not corrected and a Customer changes Supplier, the Supplier will pass on this problem to the new Supplier. Thus Suppliers that do not reach the 97% target may fail due partly to having received incorrect data. This data is not then corrected due to the cost of correction. Charging Suppliers this cost of correction would encourage them to correct in house data and hence not pass the problems on to the next Supplier. The VASMG considered that this cost was dependent on the processes, skills and systems that the individual Supplier has in place and it is difficult to quantify how much each Supplier spends on correction. It was pointed out that aspects of the genuine pre-estimate of loss should not be omitted from the calculation simply because they are difficult to estimate. The Group agreed with this in theory but considered that the cost of correction should not be included for several reasons:

- There is no direct link between charging Customers and Settlements hence the link between correcting bad Customer data and entering correct data into Settlements is not strong e.g. a Customer could be registered as having a Pre-payment Meter rather than a Credit Meter and this would need to be corrected by the Supplier but would not affect the data entering Settlement;
- There ought to be an incentive somewhere for this but the place is not necessarily the BSC and within that not Supplier Charges;
- In addition, the VASMG concluded that a realistic number to include in the genuine pre-estimate of loss could not be reached, since it felt that any numbers quoted by Suppliers (if at

all) would be widely variable. These variable numbers are, in fact, realistic since it depends what errors there are in the data and how easy they are to correct.

However the Group took away an action to provide estimated costs for correcting in-house data with the potential that these may be included as part of a genuine pre-estimate of loss calculation.

7.2.2 SP04

The Group considered the consultation responses and the requests for more data. It decided that the same analysis should be done using Profile Classes 5 and 7 (previous data was Profile Classes 6 and 8). The Group were tasked to provide BSCCo with Customer data showing the HH 365 x 48 matrix for 2003.

7.2.3 SP01 and SP02

The Group considered the consultation responses. It considered that the administration costs used to work out the genuine pre-estimate of loss calculation for SP01 and SP02, were valid for inclusion, based on BSCCo's legal advice that this could form part of the genuine pre-estimate of loss. The Group disagreed with the view of one respondent that Suppliers should be charged separately for each GSP Group as it considered that if one Supplier was late with reports in several GSP Groups, BSCCo would only make one phone call to the relevant Party. The Group also considered whether, after a period of time the charge for SP01 and SP02 could become a penalty and would no longer be a genuine pre-estimate of loss. If this were to be the case then a time cap could be put on the charge such that after for example 6 months, the charge would not be applied anymore. The Group considered this, but was of the opinion that as non compliance under SP01 and SP02 continues, the administration costs associated with it would ramp up since the matter might be taken on by more senior analysts or escalated to PAB. For this reason a time cap was not considered appropriate.

7.2.4 Caps

There were several arguments against the inclusion of a cap in P157 that were presented to the Group. These were:

- If the charges are in fact a genuine pre-estimate of loss then they ought to never become penalties;
- If the charges are a genuine pre-estimate of loss then if it is not paid it the Party who suffered the loss is not compensated;
- Force majeure provisions cover exceptional circumstances;
- A small Supplier might find that being able to predict its cash flow is more important to it than the knowledge that it has limited liability;
- Caps have the ability to reduce the effectiveness of Supplier Charges and add to the degree of complexity;
- If caps are invoked rarely then it is not worth developing an expensive computer system.

The Group considered the arguments put forward but remained unanimous in its support for the inclusion of a cap. The following reasons were given:

- Caps stop unlimited liability in exceptional circumstances rather than limiting liability under normal circumstances;
- Small Parties will, in the opinion of the Group and respondents, be put off entering the market if there was no cap and hence unlimited liability under Supplier Charges;

- Charges without caps may become penal in nature. The Group considered the following as an example of an exceptional circumstance where a cap might kick in. If a very small HH Supplier had problems with one of its Meters that accounted for 50% of its business – the Meter could be wrong and the Data Collector (DC) might enter zero value into Settlement. If the Supplier told the DC that the value should have been xMW, the DC would enter this value but will flag it as an estimate. The Supplier thus has 50% of data flagged as estimated although it was just being honest and changing from an incorrect to a correct value. In this case the Group would consider that the charge has become penal;
- Lack of caps would increase the cost to the market since no Agent would take on the risk of limitless liability from the Supplier - lack of competition amongst Agents would make it very difficult for Suppliers to transfer the risk of Supplier Charges;
- Force majeure provisions are more applicable to an event which impacts the whole market rather than just one participant;
- The new cap calculation takes Supplier size into account and hence is considered proportional and more appropriate than the current cap. In addition it is simpler to work out.

One member of the Group suggested that a cap may not be required depending on which method of redistribution was favoured by the Group. However it was pointed out that both redistribution methods being discussed have the same maximum liability that could be charged to a Party.

The Group considered the calculation it suggested for the cap (1%*Supplier Take*Credit Assessment Price). The Group considered initially that the cap calculation was appropriate but would consider it in greater detail after the Panel's discussion of the Interim Report.

7.2.5 Redistribution

The Group considered both the redistribution method suggested in the P157 consultation document "average performance" option and that suggested by a member of the Group "bond rebate" option.

The "average performance" option works as follows:

All Suppliers would be charged the genuine pre-estimate of loss for all Serials with 10% being redistributed to all BSC Parties, as at present. The average performance on SP08a of the Suppliers in the NHH market in that GSP Group (e.g.% of AAs at RF) would then be calculated and funds would be redistributed to those Suppliers performing on or above average only. Those Suppliers who are performing below the GSP Group average on SP08a would not receive any of the funds gained - THEIR NET CHARGE WILL BE A GENUINE PRE-ESTIMATE OF LOSS. Those Suppliers who are performing on or above GSP Group average on SP08a would receive all of the funds collected based on their market share - THEIR NET CHARGE WILL BE LESS THAN A GENUINE PRE-ESTIMATE OF LOSS.

For example:

Supplier 1 (50% NHH market share in GSP Group A) and Supplier 2 (30% NHH market share in GSP Group A) perform above the average of NHH performance in the GSP Group, whereas Supplier 3 (20% NHH market share in GSP Group A) performs below the average NHH performance in the GSP Group. Supplier 3 will not receive any money back from the redistribution. Suppliers 1 and 2 will receive all funds collected from all the Serials between them. Supplier 1 will receive back $50\% / (50\% + 30\%) = 62.5\%$ and Supplier 2 will receive back $30\% / (50\% + 30\%) = 37.5\%$. The VASMG considered how this option worked in the simplified model provided to them and compared it to the other options for redistribution that had been modelled.

The Group considered the negative aspects of the "average performance" option:

- There may be legal objections since some Suppliers will not receive damages due to them. Any Supplier that is underperforming is damaging other Parties, but also itself within the calculation of GSPGCF. All Suppliers should be compensated for this regardless of their own performance. BSCCo legal opinion stated that the rule against penalties relates to the reasonableness of funds paid out by a Party as 'recompense' for breach of a contract – this rule is not concerned with the use to which those funds are put once recovered as long as that use is not itself in further breach of the contract or otherwise illegal. Re-distribution is not mandatory - and need not be "netted off" against the amount of Supplier Charges levied when considering whether a pre-estimate of loss (i.e. the charge levied) is genuine. Parties therefore have the ability to agree to a different scheme by which to use the funds gained from Supplier Charges;
- The average performance method may not be appropriate for the following reason. Each GSP Group is in effect a duopoly between the incumbent Supplier and the second largest Supplier. The dynamics of the arithmetic are that the incumbent Supplier, with around 65% of the volume, effectively sets the GSP Group average performance. The average will always be close to the incumbent's performance, and whether the average is higher or lower than the incumbents is almost totally dependent on whether the second largest Supplier's performance is lower or higher than the incumbents. The "average" is therefore determined by the performance of the dominant incumbent Supplier and the dominant national Supplier. If the incumbents performance falls below the GSP Group average, then their Supplier Charges, which are based on their larger volume, are distributed to the other Suppliers, by far the largest share going to the second largest Supplier who has only a quarter the volume of the incumbent. Because the second largest Supplier's performance is the primary determinant of whether the incumbent is above or below the average, most of the Supplier Charges and redistribution may be a transfer of monies between it and the incumbent. The reverse applies because when the incumbent is above average, the second largest Supplier will almost certainly be below it, but the money flowing in the opposite direction is less because the second largest Supplier's market share in that GSP Group is less. This may make the proposed method more unstable than the current arrangements and may be capable of providing windfall gains for small Suppliers. The primary objective will always be to just beat the incumbent Supplier, and the returns from redistribution could far outweigh the costs in Supplier charges. Further work needs to be done by VASMG in this area;
- This may provide an opportunity for gaming. For example, a company operating under more than one Supplier ID could transfer "problem" MPANs from one ID to the other in order to recover a proportion of the overall Supplier Charges incurred and thus ensure the funds back are maximised to the company as a whole. This could be significant;
- There is a concern that referencing 'good' and 'poor' performance to an average performance in the GSP Group could create artificial step differences in charge redistribution;
- The proposed method is flawed as it rewards Suppliers who are still performing below the target level of performance – as the current scheme does.

Some Group members considered that there were advantages to this method:

- It encourages above average performance and thus would gradually work to encourage Parties to move above the average, hence increasing the average;
- It would also encourage eventual movement towards the target of 97%;
- It is seen by some that this model is not adversely affected by the existence of a duopoly in GSP Groups since the incumbent Supplier and second largest Supplier are incentivised by the "average performance" option to compete with each other to get above average and receive money back via the redistribution method – this will push the average up. Additionally small

Suppliers are encouraged to improve performance such that they are above the average set by the duopoly and hence receive money via redistribution.

The "bond rebate" option is an attempt to create an incentive by having a dynamic re-distribution in which the underperformer can recover its charges if it improves its performance. If not the charges are redistributed to the other Parties. This method works as follows:

Suppliers would pay their Supplier Charges as proposed⁹, with 10% being re-distributed to all Trading Parties, as at present. For SP01, SP02 and SP04 the remaining 90% would also be redistributed to all Trading Parties since the nature of these Serials does not lend itself to the "bond rebate" model.

For SP08a, b and c, the 90% would go into a bond specific to their company (separately for each Serial), and would be re-payable on the basis of future Performance Levels. Refunds would be made on a rolling 12 month basis according to how much performance had improved. For example, in September 2004 if the performance was 93%. Supplier Charges would be lodged in the bond. Come September 2005, if the performance is 96%, then new Supplier Charges are payable but a rebate equivalent to the 3% improvement over the previous 12 months is made. The other 1% is forfeit, and goes back to BSC Parties in the same way as the 10% original cut. Had the performance improved to 97%, i.e. the target, the Supplier would get it all back.

This method has the following advantages:

- The charges and rebate amounts are proportional to Supplier size;
- It is a Suppliers own money, not someone elses;
- It does not rely on averages, or relative market shares;
- It is easy to understand, calculate and predict;
- It does not rely on other Suppliers performance for the calculation;
- It is an incentive to maintain good performance, and not to let it slip;
- It gives Suppliers a mechanism by which to incentivise their agents, and share risk and reward.

It has some similar disadvantages to the "average performance" method:

- There may be similar legal objections;
- This option may also provide an opportunity for gaming;
- Performance is still incentivised in a relative manner i.e. relative to ones previous performance;
- This option also rewards Suppliers who are still performing below the target level of performance;

There are several issues to be sorted out within this and proposals have been made and will be discussed and analysed.

Issues to be considered are:

- The effect may be delayed by 12 months – until the charge and rebate kick in – the 12 month period for rebate could be shortened – if not for all Parties certainly for new entrants;
- If the money is kept in a bond who owns it and who gets the interest;
- Is it discriminatory against smaller Suppliers who might have more cash flow issues over the rebate period than larger Suppliers?

⁹ One option is for payment to be delayed until the rebate has occurred

The Group agreed to undertake further analysis of this method within the Assessment Procedure and work is continuing to resolve the issues.

The Group briefly considered the 90/10 rule and whether to leave it as is. It noted the consultation responses and considered that it would wait until the method of redistribution was finalised before considering this aspect of the use of funds.

7.2.6 Supplier Charge Reviews

The Group clarified that the review was to recalculate the genuine pre-estimate of loss according to the agreed methodology. The Group considered that there was a compromise between being sure that the genuine pre-estimate of loss was accurate and increased uncertainty in the market if frequent changes were made. It was pointed out that regular reviews to recalculate the genuine pre-estimate of loss would be based on more recent data and hence would be more accurate as would reflect changes made to the trading arrangements (as can be seen with CP696 above). The Group considered that 2 years after the Implementation Date was a suitable time for a review followed by reviews every two years.

7.2.7 Force Majeure

The Group confirmed its decision regarding force majeure after considering the consultation responses. The Group referred to discussions under Modification Proposal P115 "Disapplication of Supplier Charges Under Certain Circumstances" (P115). The VASMG concurred with the views put forward by the P115 Modification Group that there is a link between Section S and Annex S-1 and hence a link between the obligations laid down in Section S2 and the Supplier Charges regime in Annex S-1 which describes how the Supplier carries out those obligations. Supplier Force Majeure can be applied to the provisions dealing with Supplier Liquidated Damages. Further provision was considered unnecessary by the Group since each force majeure occasion would by its nature be an unpredictable event therefore specifying anything would be difficult. The Group decided that this should be considered on a case by case basis and should be left to the discretion of the PAB/Panel.

7.2.8 Peer Group Comparison (pgc)

Some members of the Group reiterated their points of view that pgc tables were unsuitable and stated support for an Alternative Modification without pgc. Other members of the Group still supported the use of pgc tables. The argument put forward mirrored those provided by consultation respondents.

In addition it was commented that the provisions for prior review and appeal before publication are critical, that Parties must clearly be made aware of standards they have to achieve before any figures are published and that the data must be published in a fair / comparable way such that Parties are not shown in an unfavourable light due merely to their market share.

The Group and consultation respondents were split over whether pgc was a positive aspect to the Proposed Modification and it was agreed that Supplier Charges without pgc may be a suitable Alternative Modification.

7.2.9 Implementation Date

The Group were still supportive of its suggested Implementation Date of July 2005 however considered that if the timetable of P157 was extended again or perhaps even with the current extension, a reassessment of this date might be necessary. The Group noted that a Calendar Day implementation would have a retrospective effect, but felt that it was justified as a date set in the future would ensure that Parties had enough time to improve performance before the new charges took effect.

8 SUMMARY OF TRANSMISSION COMPANY ANALYSIS

8.1 Analysis

The Transmission Company did not identify any impact or cost to it. It did state that it supported the continuation of Supplier Charges as an appropriate mechanism to incentivise the provision of better quality data into Settlement. It believed that the principles outlined in P157, to achieve a Supplier Charges Mechanism that is easily understood and provides effective incentives on Parties, meet BSC Applicable BSC Objectives c) for promoting effective competition in the generation and supply of electricity and d) for promoting efficiency in the implementation and administration of the balancing and Settlement arrangements. It considered that any potential benefits arising from the Proposed Modification would have to be measured against the costs of introducing the necessary changes to the existing processes.

See the Transmission Company analysis in annex 2.

8.2 Comments and views of the Modification Group

9 DOCUMENT CONTROL

9.1 Authorities

Version	Date	Author	Reviewer
0.1	19/05/04	Dena Harris	ELEXON
0.2	01/05/04	Dena Harris	P157 Modification Group - VASMG

9.2 References

Ref	Document	Owner	Issue date	Version
CP696	'Allow the Half Hourly Data Aggregator (HHDA) to apply a default where no consumption data has been provided by the Half Hourly Data Collector (HHDC).'	ELEXON	21 March 2001	1.0
P157AC	'Consultation document for Modification Proposal P157'	ELEXON	10 May 2004	1.0

ANNEX 1 MODIFICATION GROUP DETAILS

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ANNEX 2 TRANSMISSION COMPANY ANALYSIS

Q	Question	Response
1	Please outline any impact of the Proposed Modification on the ability of the Transmission Company to discharge its obligations efficiently under the Transmission Licence and on its ability to operate an efficient, economical and co-ordinated transmission system.	We do not believe that the Proposed Modification P157 has any impact on the ability of the Transmission Company to discharge its obligations under the Transmission Licence.
2	Please outline the views and rationale of the Transmission Company as to whether the Proposed Modification would better facilitate achievement of the Applicable BSC Objectives.	We support the continuation of Supplier Charges as an appropriate mechanism to incentivise the provision of better quality data into Settlement. We believe that the principles outlined in P157, to achieve a Supplier Charges Mechanism that is easily understood and provides effective incentives on Parties, meet BSC Applicable Objectives c) for promoting effective competition in the generation and supply of electricity and d) for promoting efficiency in the implementation and administration of the balancing and Settlement arrangements. However, we would endorse the views expressed by the Mod Group that any potential benefits arising from the Proposed Modification would have to be measured against the costs of introducing the necessary changes to the existing processes.
3	Please outline the impact of the Proposed Modification on the computer systems and processes of the Transmission Company, including details of any changes to such systems and processes that would be required as a result of the implementation of the Proposed Modification.	No impact has been identified from the Proposed Modification P157 on the computer systems and processes of the Transmission Company.
4	Please provide an estimate of the development, capital and operating costs (broken down in reasonable detail) which the Transmission Company anticipates that it would incur in, and as a result of, implementing the Proposed Modification.	No costs have been identified.
5	Please provide details of any consequential changes to Core Industry Documents that would be required as a result of the implementation of the Proposed Modification.	No changes have been identified.
6	Any other comments on the Proposed Modification.	

ANNEX 3 PARTY AND PARTY AGENT IMPACT ASSESSMENTS

See attached document – Attachment 1.

ANNEX 4 CONSULTATION RESPONSES

See attached document – Attachment 2.

Appendix 1: Value of volume of energy that is assumed to be uncertain

The calculations were performed separately for HH and NHH Suppliers

Data was used for May, June, October and November 2001 for a sample of 8 Suppliers, for all GSP Groups.

The percentage change in volume between SF and DF per Supplier per GSP Group (a) was compared with the corresponding percentage change in estimates (b)

The percentage change in volume per percentage change in estimates (a)/(b) was calculated followed by the volume weighted average of these values (c) - this represents the average inaccuracy in an average estimate

To find the price/cost of that energy – (P), the average of SSP, SBP and market price over a year from 11 Mar 2003 to 10 March 2004 inclusive was calculated and the average of the difference between SSP and market price and SBP and market price was calculated:

The average of SSP over a year from 11 Mar 2003 to 10 March 2004 inclusive = £15.11

The average of SBP over a year from 11 Mar 2003 to 10 March 2004 inclusive = £22.53

The average of market price from 11 Mar 2003 to 10 March 2004 inclusive = £18.79

The average of the differentials is £3.714

P=£3.714

The charge per MWh that a Supplier is below the Standard is thus computed as (c) * (P)

For this data any spurious looking data in the HH sample was removed. This was data that for any of the dates considered had an increase in estimates between SF and DF. If this occurred, the whole Supplier in that GSP Group was eliminated from the analysis.

Results: May/June 2001 and Oct/Nov 2001 –

	Average SP08a	Average SP08b,c
SF-DF volume change / % change in estimates	3.02%	119%
SF-DF volume change / % change in estimates *P	£ 0.112/MWh	£4.427/MWh

PLEASE NOTE THAT FURTHER ANALYSIS WILL BE PERFORMED AS DESCRIBED IN THE PAPER ABOVE.

Appendix 2a Cost of Uncertainty a

Cost of uncertainty

A)

The calculation would appear thus:

- Consider the cost of certainty in a run per MWh
- Calculate additional %age energy settled on AAs between Run [a]
- Calculate amount of NHH traded in a day [b]
- Calculate the additional energy settled on AAs in a day [c] = [a] * [b]

- Calculate cost to administer the Settlement Run arrangements this could be the sum of the SVAA, NETA CSA, FAA etc costs or purely the SVA side costs [d]
- Calculate cost of a Settlement Runs used to increase accuracy i.e. not the first one that is required anyway. Where 365*5 is number of Settlement Runs in a year and 4/5 excludes the first run that is required even if all data entered is fully accurate [e] = [d]/(365*5)*(4/5)
- Calculate the cost of a Settlement Run per MWh [f] = [e]/[c]
- [e]/[c] = £[f]/ MWh away from standard

	SF	R1	R2	R3	RF	Average
Target AAs	3%	17%	43%	78%	97%	
% AAs added [a]	3%	14%	26%	35%	19%	
Energy traded per day TWh [b]	0.35	0.35	0.35	0.35	0.35	
additional energy on AAs [c]	0.01	0.05	0.09	0.12	0.07	
cost of run £ [e]	21,900	21,900	21,900	21,900	21,900	
cost £/MWh [f]	2.08	0.45	0.24	0.18	0.33	0.66

Source of data:

[b] = (http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/1262_Energy.pdf) The paper is a bit dated but shows on page 2, that in 2001 350 TWh were consumed of which around 128 TWh were for domestic.

[d] = from the Business Strategy highlighted amounts used:

Item	Year to March 2005 Budget £m
BSCCO Operational	15.46
Demand Led	6.00
Contracted	28.50
NETA Funding	13.23
BSCCO BETTA Project	2.30
OVERALL TOTAL	65.49

Appendix 2b Cost of Uncertainty b

Cost of uncertainty

B)

Uncertainty associated with the potential of nobody sending any data in:

The percentage uncertainty in volume of an average EAC is x%

The cost of the uncertainty associated the imbalance differential £3.714 *x% = £y/MWh

If we want to see what would be the uncertainty if only 10% of actual data (AAs) was entered into Settlement. We can assume that if:

only 10% of actual data entered into Settlement

and at the moment 90% of actual data is entered into Settlement

then the accuracy of an EAC would decrease by 9

So the percentage uncertainty in volume of an average EAC in this case would be 9x% and the corresponding cost of uncertainty would be £9y/MWh

But we need to add a probability factor of this scenario occurring – z%

So cost of uncertainty = £9yz/MWh

Q: is it linear?

Q: can we get a value for z

Appendix 2c Cost of Uncertainty c

Cost of uncertainty

C)

Internal Pricing teams within companies appear to cost uncertainty into their pricing calculations. What the pricing team do is something like this:

- Take the customer's actual data.
- Ask the traders for pricing data
- Add on profit
- Add on a certain amount which factors in safety of customer, the rate the customer wants and a measure of the uncertainty of the customer – the latter depends on whether the customer is HH or NHH AND whether data is actual or estimated.

It is difficult to estimate what this would be.

Appendix 3 central costs

Central Costs – incremental costs

The central costs are approximated below:

Technique	Annual Costs £m	Suggested Savings £m
Audit ¹⁰	2.6	0.50
Technical Assurance of Metering Systems	0.8	0
Certification	0.03	0
BSCCO, PAB, TA (Supplier & Supplier Agents), Education, Monitoring, Disputes etc ¹¹	0.75	0.01
Total	4.18	0.51

Additional effort spent on performance issues including OSMs:

No of man days a year	211
Cost of time in 1 year	£0.04m

The market size is approximated below:

¹⁰ This is based on Parties compliance with BSC Processes and subsequent attainment of the relevant Standards without the creation of settlement error.

¹¹ The majority of cost savings that would be made would be via a reduction in the amount of support that ELEXON would provide to participants. This support comes via education provided at workshops, seminars, publication of guidance notes etc. and also a reduction in the number of required internal escalations and escalations to the Panel and its committees.

	TWh
Total market	350
NHH market	128
HH market	222

The suggested savings of the PAF costs are added to the incremental time¹² spent by BSCCo as part of its added value service for dealing with Suppliers under-performance related issues and costed at £200 per man day:

£/MWh	NHH	HH
Total	0.002	0.001

Appendix 4 SP04

Charge for uncertainty between HH and NHH metering (i.e. use of profiles) – SP04

Take some HH actual data close to the 100kW consumption – customers with consumption only just over 100kW were chosen since it was assumed that there is a natural incentive and it is expected, for very large customers to have HH Metering installed and those who breach SP04 are likely to be close to the 100kW cut off.

Step 1: to calculate error in the profile

	Period 1	Period 2	etc
Settlement Day 1	actual	HH	Customer data
Settlement Day 2	Total Sum = X		
Etc			

	Period 1	Period 2	etc
Settlement Day 1	Profile	data	Multiplied up
Settlement Day 2	Total Sum = X		
Etc			

	Period 1	Period 2	etc
Settlement Day 1	Error =	Profile	data

¹² This is calculated using the BSCCo timesheet system.

<i>Settlement Day 2</i>	Minus	actual	data
<i>Etc</i>			

Step 2: to calculate the cost of this error in the balancing mechanism – Average difference of SSP and market Price and SBP and market Price

	<i>Period 1</i>	<i>Period 2</i>	<i>etc</i>
<i>Settlement Day 1</i>	Imbalanc e	Price	Differential
<i>Settlement Day 2</i>			
<i>Etc</i>			

Step 3: to calculate the cost of the error multiply the error by the imbalance price differential to get a cost for each period over each Settlement Day

	<i>Period 1</i>	<i>Period 2</i>	<i>etc</i>
<i>Settlement Day 1</i>	Cost	of	error
<i>Settlement Day 2</i>	Imbalance price differential	Multiplied by	error
<i>Etc</i>			

Step 4: sum the cost and divide it by the number of Settlement Days to get a cost per day value

PLEASE NOTE THAT FURTHER ANALYSIS WILL BE PERFORMED AS DESCRIBED IN THE PAPER ABOVE.

Appendix 5 summary of loss and comparison with current Supplier Charges

Note: SP08b and c the same data is used SP08b is HH target of 99% at R1, SP08b is HH target of 99% at RF.

£/MWh	SP08a	SP08b	SP08c
Value of volume of energy assumed to be uncertain 1)	£0.11	£4.43	£4.43
Cost of uncertainty	? ¹³	?	?
Incremental Central Costs	£0.002	£0.001	£0.001
Total	£0.112	£4.431	£4.431
Current Supplier Charges	£0.14R3	£0.14SF	
Current Supplier Charges	£1.57RF	£1.57R1	£1.57RF

£ per day	SP04
Difference between profile and actual	£9.07
Current Supplier Charges	£2.95

¹³ It is uncertain whether a value will be added in here and what it will be. A decision will be made by the Group at a later stage.

£ per day	SP01	SP02	
Administration Costs	£20	£20	Per day only
Current Supplier Charges	£28.03	£28.03	Per GSP Group per day

Appendix 6a: Capping scenarios for consideration

Scenario: A Half Hourly Supplier with 1% of the HH and NHH market – how would this appear with the current CAP who only reaches 50% of HH meter readings at R1 and everyone else performing on target:

	Supplier % share of both NHH and HH	Supplier Take	Supplier Cap	Supplier share of 90%	Total Charges	90% charges	own receipts	Net Liability	Cap Breach	net liability SC adjusted for cap breach	Receipts from 90% SC adjusted for cap breach	SC adjusted for cap breach	NET
S1	54.0%	1,080,000	£64,800	54%	£0	£0	£0	£0	no	£0	£588	£0	-£588
S2	30.0%	600,000	£36,000	30%	£0	£0	£0	£0	no	£0	£327	£0	-£327
S3	8.0%	160,000	£9,600	8%	£0	£0	£0	£0	no	£0	£87	£0	-£87
S4	7.0%	140,000	£8,400	7%	£0	£0	£0	£0	no	£0	£76	£0	-£76
S5	1.0%	20,000	£1,200	1%	£24,941	£22,447	£224	£24,717	yes	£1,211	£11	£1,211	£1,200
Total	100%	2,000,000			£24,941	£22,447				£1,211	£1,090	£1,211	£121

The Group considered that a cap for S5 of £1,200 was too low and a Supplier with such a take should have a higher cap. Using the new methodology, the Supplier's cap would be £ (1%*20,000*Credit Assessment Price) which currently would make it £4,230.

This second scenario looks at a large Supplier who performs badly on HH R1 (90%). Its cap is now £64,800 and with the new methodology would be £228,420 – this would not have resulted in the Suppliers charge being capped and hence reduced in the scenario below.

	Supplier % share of both NHH and HH	Supplier Take	Supplier Cap	Supplier share of 90%	Total Charges	90% charges	own receipts	Net Liability	Cap Breach	net liability SC adjusted for cap breach	Receipts from 90% SC adjusted for cap breach	SC adjusted for cap breach	NET
S1	54.0%	1,080,000	£64,800	54%	£247,374	£222,637	£120,224	£127,150	yes	£126,070	£61,270	£126,070	£64,800
S2	30.0%	600,000	£36,000	30%	£0	£0	£0	£0	no	£0	£34,039	£0	£34,039
S3	8.0%	160,000	£9,600	8%	£0	£0	£0	£0	no	£0	£9,077	£0	-£9,077
S4	7.0%	140,000	£8,400	7%	£0	£0	£0	£0	no	£0	£7,942	£0	-£7,942
S5	1.0%	20,000	£1,200	1%	£0	£0	£0	£0	no	£0	£1,135	£0	-£1,135
Total	100%	2,000,000											£12,607

Appendix 6b: new and old cap comparison

Some analysis was performed comparing the value of the cap from May and June 2002 for all Suppliers with what the value would be with the new cap calculation in place. (1% of Supplier total energy in the GSP Group multiplied by Credit Assessment Price.)

On average, the new cap calculation was ~280% bigger than the old cap calculation.

A sample of the data considered appears thus – coded example

The Credit Assessment Price is £18+VAT

	Deemed take	Monthly cap	new cap	Difference between old and new caps (old-new)/old
S1	680,000	£41,000	£140,000	254%
S2	2,300	£150	£500	223%
S3	50,000	£2,600	£11,000	307%
S4	330,000	£15,000	£70,000	368%
S5	31,000	£1,700	£6,700	293%
S6	17	£1.00	£3.60	255%
S7	190,000	£10,000	£40,000	288%

Appendix 7: Performance issues suitable for pgc

The Group considered the major audit issues to decide whether these could be incentivised by Supplier Charges or pgc. The VASMG considered issues up until SSM 9, as it felt that it wanted to consider the most important issues only. (see below)

The Group agreed that the data that the Definition Report stated would be published via pgc was also appropriate.

It also considered the P99 Serials that are the current legal baseline

The Group looked at NC02, NC03 and HM06. One member state that these issues were particularly relevant with regards to the customer transfer issue and thus could be charged on or incentivised via pgc. One member highlighted the complications associated with this for example the "win, lose, win back scenario" whereby the Party who loses the gained customer to the original Supplier will get charged for lack of provision of data it never had. One member pointed out that these data items have not yet been collected and will not be until after 1 May 2004 (P99 Implementation Date) thus the trend the data will show and the problems it may highlight have not been seen yet thus it seems premature to suggest either Supplier Charges or pgcs

SSM number	Description	Comment	Supplier Charges	Peer Group Comparison
SSM 1	Inaccurate energisation status of Metering Systems	This is about energised meters that have de-energised status but the reverse exists also	Complicated, potentially inaccurate, full of loopholes – would not work as incentive	Would be appropriate if all agreed that wrongly labelled de-energised Metering Systems considered
SSM 2	Processing of erroneous EAC/AA NHH	This is a big issue that is not going to go away and has deteriorated since Xmas. The auditor has highlighted a lack of incentive to correct these especially negative ones	Not appropriate	This is suitable for pgc as long as portfolio size is taken into account as otherwise a big Supplier will seem like the worst one when this is not necessarily the case
SSM 3	Erroneous values of UMS NHH	Not sure how big this issue is i.e. the magnitude of the error	Would be premature to apply Supplier Charges as this is a nascent issue	This could be done by Agent and associated Supplier
SSM 4	Inadequate clearance of exceptions and backlogs in HH	There has been a huge improvement in this area recently and it is being monitored.	Not appropriate as TDC have instructed BSCCO to monitor this	Not appropriate as TDC have instructed BSCCO to monitor this
SSM 5	Inadequate clearance of exceptions and backlogs in NHH	The numbers are very significant in this area. Multiple exceptions per MPAN can be received	Not appropriate as the values involved are hard to quantify. Would be very complex to set up charging system	Hard to publish volumetrics as difficult to ascertain which are significant. To make it meaningful would need extra level of analysis.

SS M 6	Maintenance of Trading Party bank a/c details by FAA	n/a	n/a	n/a
SS M 7	Incorrect application of P/C flags to BM units in CRA	Not a big issue for SVAA	No	No
SS M 8	Performance of meter advance reconciliations	It is believed that no current disputes on this because no one is performing Meter Advance Reconciliations	Not appropriate	Could do by Agent and associated Supplier – no direct reporting though – can only monitor