

## Phase

Initial Written Assessment

Definition Procedure

Assessment Procedure

Report Phase

Implementation

## P330 'Allowing ELEXON to tender for the Uniform Network Code Gas Performance Assurance Framework Administrator (PAFA) role'

Approved UNC Modification 506 will introduce performance assurance arrangements into the gas market for the first time and will require a competitive tender exercise to appoint an independent gas PAFA.

The P330 Proposer believes that ELEXON has significant experience and understanding of performance assurance techniques in the electricity industry and has transferable skills and knowledge that potentially meet the criteria for the appointment of the PAFA. This Modification therefore seeks to amend the BSC arrangements to allow ELEXON to bid for the gas PAFA contract.



The BSC Panel initially recommends **rejection** of P330

This Modification is expected to impact:

- BSCCo
- All BSC Parties

252/06

P330  
Draft Modification Report

5 May 2016

Version 1.0

Page 1 of 40

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## Contents

<b>1</b>	<b>Summary</b>	<b>3</b>
<b>2</b>	<b>Why Change?</b>	<b>4</b>
<b>3</b>	<b>Solution</b>	<b>6</b>
<b>4</b>	<b>Impacts &amp; Costs</b>	<b>8</b>
<b>5</b>	<b>Implementation</b>	<b>10</b>
<b>6</b>	<b>Workgroup's Discussions</b>	<b>11</b>
<b>7</b>	<b>Workgroup's Conclusions</b>	<b>25</b>
<b>8</b>	<b>Panel's Initial Discussions</b>	<b>27</b>
<b>9</b>	<b>Report Phase Consultation Responses</b>	<b>30</b>
<b>10</b>	<b>Recommendations</b>	<b>34</b>
	<b>Appendix 1: Business Rules for UNC MOD506</b>	<b>35</b>
	<b>Appendix 2: Workgroup Details</b>	<b>37</b>
	<b>Appendix 3: Glossary &amp; References</b>	<b>39</b>

## About This Document

This is the P330 Draft Modification Report, which ELEXON will present to the Panel at its meeting on 12 May 2016. It includes the responses received to the Report Phase Consultation on the Panel's initial recommendations. The Panel will consider all responses, and will agree a final recommendation to the Authority on whether the change should be made.

There are four parts to this document:

- This is the main document. It provides details of the solution, impacts, costs, benefits/drawbacks and proposed implementation approach. It also summarises the Workgroup's key views on the areas set by the Panel in its Terms of Reference, and contains details of the Workgroup's membership and full Terms of Reference.
- Attachment A contains the draft redlined changes to the BSC for P330.
- Attachment B contains the full responses received to the Workgroup's Assessment Procedure Consultation.
- Attachment C contains the full responses received to the Panel's Report Phase Consultation.



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252/06

P330

Draft Modification Report

5 May 2016

Version 1.0

Page 2 of 40

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## Why Change?

Approved Uniform Network Code (UNC) Modification 506 introduced performance assurance arrangements into the gas market for the first time and will require a competitive tender exercise to appoint an independent gas Performance Assurance Framework Administrator (PAFA).

The P330 Proposer believes that ELEXON has significant experience and understanding of performance assurance techniques in the electricity industry and has transferable skills and knowledge that potentially meet the criteria for the appointment of the PAFA.

## Solution

P330 will enable the ELEXON Board to decide whether or not to bid for the role of gas PAFA under the UNC (and perform the role if the contract is awarded to ELEXON). This will be done via a separate subsidiary (called 'PAFACo' in this Modification) which will be funded by ELEXON (through BSC Parties).

As ELEXON operates on a not for profit basis, if the ELEXON Board determines a bid should be submitted the costs incurred in submitting a bid will be borne by BSC Parties. Any bid costs will be capped at £100k. ELEXON will report its bid costs to the BSC Panel to ensure it does not breach this limit.

## Impacts & Costs

The cost to implement P330 is estimated at £240 (one man day) for ELEXON to implement the required document changes. This Modification only seeks to allow ELEXON to be able to bid for the gas PAFA role, therefore the effort required to implement P330 is minimal and there are no implementation impacts and costs to BSC Parties or BSC Agents.

### Bid costs

Though there are no implementation impacts or costs to BSC Parties or Party Agents associated with implementation of P330, if a bid for the gas PAFA role is submitted the costs incurred in doing so will be borne by BSC Parties. If a bid is successful, Parties will be reimbursed for the bid costs in accordance with their respective Funding Shares. Parties will not bear the costs of operating the PAFA role.

## Implementation

The Panel initially recommends an Implementation Date of 5 Working Days following Authority approval.

## Recommendation

The Panel's initial majority view is that P330 does not better facilitate Applicable BSC Objective (d) compared to the baseline. The Panel therefore initially recommends by majority that P330 should be rejected.

## 2 Why Change?

### Gas Performance Assurance Framework

Unlike the electricity market, there is currently no performance assurance regime in place in the gas market. Ofgem has discussed the benefits of having a regime with the industry and have, on a number of occasions, expressed a view that a Performance Assurance Framework (PAF) should be introduced into the gas market.

Under the Uniform Network Code (UNC) a Modification (MOD506) was raised to introduce the desired gas PAF arrangements to facilitate the monitoring and reporting of Transporter, Shipper and Transporter Agency performance. It is believed that this will incentivise parties operating in the gas market to reduce settlement risk and improve accuracy. The Authority approved MOD506 on 17 December 2015.

MOD506 requires Gas Transporters to appoint a PAFA by competitive tender. Conditions for such appointment will be set out in the [UNC Related Document 'Guidelines for Energy Settlement Performance Assurance Regime'](#).

Further information on MOD506 can be found on the [MOD506](#) page of the Gas Governance website.

### Issue 62

ScottishPower raised [Issue 62 'Amending the BSC arrangements to allow ELEXON to tender for the UNC Gas PAFA role'](#) on 2 November 2015, before the Authority decision on MOD506.

They believe that ELEXON has significant experience and understanding of Performance Assurance Techniques in the electricity industry and has transferable skills and knowledge that may potentially meet the criteria for the appointment of the PAFA. Issue 62 was raised to explore the potential for the BSC arrangements to be changed to allow ELEXON to bid for the gas PAFA contract.

The Proposer requested that the Issue Group consider the following questions when looking at whether ELEXON should participate in a competitive PAFA tender:

Questions considered under Issue 62	
1	Based on Ofgem's suggested criteria under P284, when assessing whether to propose ELEXON's participation in the gas assurance arrangements, consider the following: <ul style="list-style-type: none"><li>• how would BSC Parties benefit from any diversification;</li><li>• how the arrangements could ensure that there is no disproportionate risk placed on BSC Parties (what ring fencing provisions are required?);</li><li>• how standards of service under the BSC should be maintained; and</li><li>• how to assure that ELEXON's BSC role does not give it any undue competitive advantage in a contestable activity.</li></ul>
2	What are the potential synergies (and benefits) associated with ELEXON providing settlement assurance services for both gas and electricity?
3	Is there a time constraint on when a Modification would be required to allow ELEXON to participate in the provision of gas assurance services?

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252/06

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P330

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Draft Modification Report

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5 May 2016

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Version 1.0

---

Page 4 of 40

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Questions considered under Issue 62	
4	What are the relevant applicable BSC objectives associated with ELEXON's participation in gas assurance services?
5	Do Parties believe ELEXON should provide services on a not for profit basis, akin to the BSC?
6	Who would decide if ELEXON would submit a bid (Panel, BSC Parties, Board)?
7	How could a bid from ELEXON be funded?
8	Are there any other factors that need to be considered for a Modification to be developed that would permit ELEXON's participation in the provision of gas assurance services?

The Issue 62 Group considered the questions set out above at its meeting on 30 November 2015. Issue Group members were supportive of ELEXON participating in a competitive tender process for the gas PAFA role and there were no objections raised. They noted that ELEXON's experience and ability to run the electricity PAF arrangements and conduct the Performance Assurance Board (PAB) meetings could be of great benefit when introducing a PAF in the gas market. There were concerns raised about the short timescales in which to raise a BSC Modification to enable ELEXON to tender.

The Issue 62 Report is available on the [Issue 62 webpage](#).

## What's the issue?

The Authority approved UNC MOD506 shortly after the Issue 62 Group concluded its discussions. The Issue Group proposer, ScottishPower, believed there was a positive response from Issue Group members on the idea of ELEXON bidding for the gas PAFA role.

Currently, the BSC does not allow ELEXON to do anything that is not set out in the Code. Therefore, in order to allow the ELEXON Board the option of bidding for the gas PAFA role a Modification is required to amend the BSC. The P330 Proposer views this omission as a defect under the BSC.

### Proposed solution

P330 'Amending the BSC to allow ELEXON to tender for the Uniform Network Code Gas Performance Assurance Framework Administrator role' was raised by ScottishPower on 1 December 2015.

This Modification seeks to enable ELEXON to bid for the role of gas PAFA under the UNC (and perform the role, functions and responsibilities if the contract is awarded to ELEXON). This will be done via a separate subsidiary (called 'PAFACo' in this Modification). The decision on whether to bid for the PAFA work (and set up 'PAFACo') will sit with the ELEXON Board.

P330 will make changes to the BSC to ensure that ELEXON is ring-fenced from any enduring operational costs and risks associated with performing the role of gas PAFA (via 'PAFACo'), with ELEXON resources being shared. The Proposer believes that there should be no cross subsidy between different ELEXON services for the cost of delivering the PAFA.

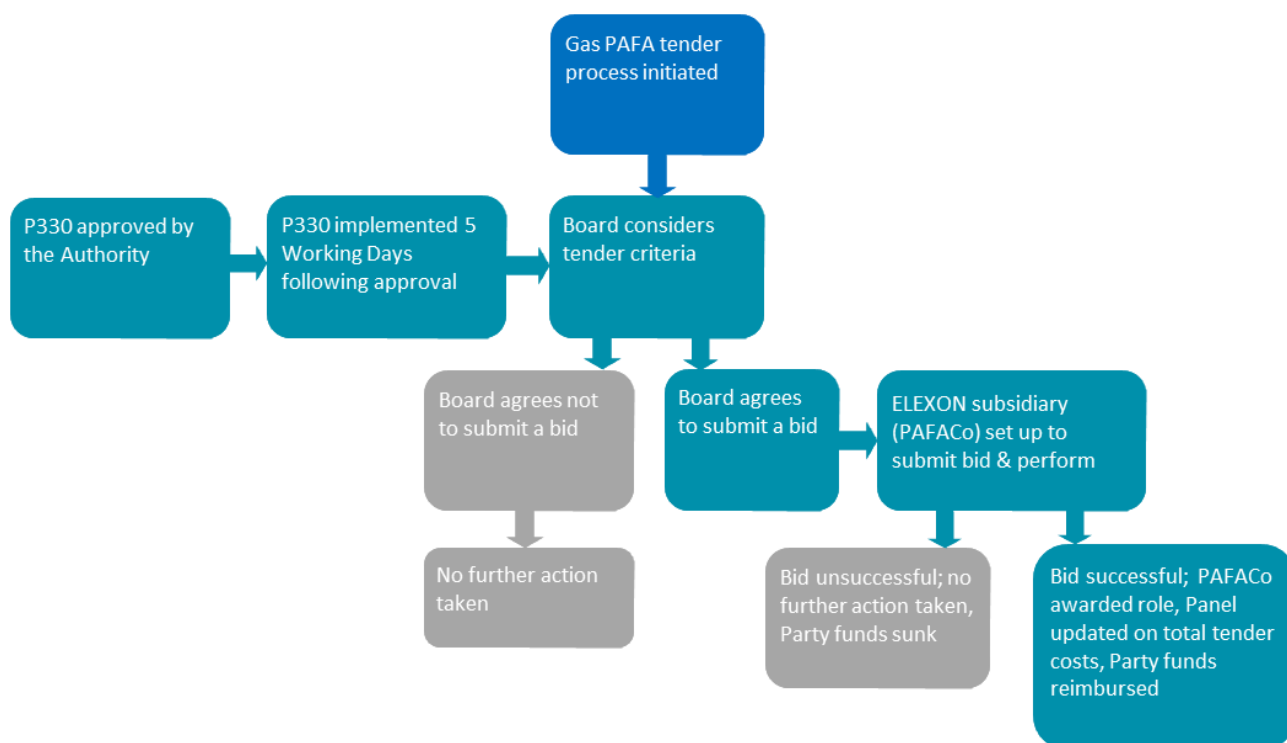
### Bid Costs

If this Modification is approved, and the ELEXON Board determines that they wish to submit a bid for the PAFA role, BSC Parties will bear the cost of such a bid, since ELEXON operates as a not for profit organisation.

Under the P330 proposed solution the total cost for internal and external resources required for the bid has been capped at £100k. This capped value allows for variations and flexibility, as the criteria for the gas PAFA tender have not yet been published. A summary of the internal and external activities required as part of the bidding process are highlighted in the table below.

Bid Activities	
Internal	
<ul style="list-style-type: none"><li>o tender evaluation</li><li>o bid preparation</li><li>o bid meetings</li><li>o negotiations and clarifications</li><li>o preparations for providing service</li></ul>	
External	
<ul style="list-style-type: none"><li>o legal support and advice (due diligence)</li><li>o other (for example, contract support and advice)</li></ul>	

Under the proposed solution, ELEXON will be allowed to provide a loan to 'PAFACo'. If the a bid for the gas PAFA role is lost there will be no liability on 'PAFACo' to repay the loan meaning funding costs will be sunk (as shown in the diagram below). If 'PAFACo' is successful in its bid the bid costs will be reimbursed to Parties in accordance with their respective Funding Shares.



## Are there any Alternative Modifications?

The Workgroup do not believe there are any Alternative Modifications that would better facilitate the Applicable BSC Objectives.

## Other ELEXON activities outside the BSC

The Issue 62 Group noted that there are already two different models contained within the BSC where ELEXON (or an ELEXON subsidiary) conducts 'non-BSC' related activities. One model sits under the Warm Homes Discount (WHD) scheme operated by ELEXON Ltd and the other under the Electricity Market Reform (EMR) services operated by the EMR Settlement Service Provider (EMRS). The Secretary of State directed both of these services.

It is worth highlighting that the tender and delivery for the gas PAFA will be less complex than the Data and Communications Company (DCC) work to which P289 originally referred. There is a working assumption under the UNC that the procurement for the gas PAFA, if MOD506 is approved by Ofgem, will be under the current [Official Journal of the European Union](#) (OJEU) procurement [threshold value](#) (£350k).

## Draft legal text

The draft legal text changes can be found in Attachment A.

252/06

P330

Draft Modification Report

5 May 2016

Version 1.0

Page 7 of 40

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### Estimated central implementation costs of P330

The cost to implement P330 is estimated at £240 (one man day) for ELEXON to implement the required document changes.

It should be noted that this Modification only seeks to enable ELEXON to be able to bid for the gas PAFA role. Therefore, the effort required to implement P330 is minimal.

### Industry impacts and costs

**There are no implementation impacts or costs to BSC Parties or Party Agents anticipated as P330 only seeks to allow for ELEXON to be able to bid for the gas PAFA role.**

However, as ELEXON operates on a not for profit basis, Parties will be asked to fund a bid submitted for this role. Under the P330 proposed solution the total cost for the bid has been capped at £100k. One respondent to the Assessment Procedure Consultation noted this as a negative impact and believes it is unacceptable for BSC Parties to have to fund the bid.

One respondent questioned whether the approach for allowing ELEXON to bid is consistent with fair and equitable procurement (i.e. it could have unintended consequences for potential competing organisations). The respondent believes that the areas where impacts on other organisations may arise and where concerns manifest are as follows:

- ELEXON's ownership profile;
- the funding basis for ELEXON to participant in the tender;
- restricting future competitive market pressures for assurance based services.

One respondent to the Assessment Consultation indicated a positive impact under this Modification. They believe that it provides an opportunity for ELEXON to expand and use its wide experience and knowledge of Performance Assurance in another area of the industry. They also feel a successful bid will provide additional opportunities such as benchmarking ELEXON's performance and applying lessons learned across both gas and electricity for the benefit of all Parties.

The full Assessment Procedure Consultation responses can be found in Attachment B.

Impact on BSC Parties and Party Agents	
Party/Party Agent	Potential Impact
All BSC Parties	No implementation impacts. However, in the event that the ELEXON Board determines that it is appropriate to establish a PAFACo and bid for the gas PAFA role, Parties will be required to fund this bid.

252/06

P330  
Draft Modification Report

5 May 2016

Version 1.0

Page 8 of 40

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#### Impact on Transmission Company

No direct impact. However, the Transmission Company may have an interest as a BSC Party.

#### Impact on BSCCo

Area of ELEXON	Potential Impact
Though it is not a direct implementation impact, if the Modification is approved, ELEXON will need to determine whether to bid for the PAFA role (following the process introduced) and, if it does bid, participate in the tender process as part of 'PAFACo'.	

#### Impact on Code

Code Section	Potential Impact
Section C	Changes will be required to implement this Modification.
Section X Annex X-1	

### Recommended Implementation Date

The Workgroup recommends an Implementation Date for P330 of **5 Working Days following Authority approval**.

The Workgroup believes that this is the most pragmatic implementation approach and will allow for the Modification to be implemented without restricting ELEXON's ability to tender if it is approved.

Seven of the nine responses to the Assessment Procedure Consultation supported the recommended Implementation Date.

One respondent submitted a response in the form of a letter and did not comment on implementation, and is therefore considered neutral.

The one respondent that did not agree with the proposed Implementation Date advised that they do not support the Modification and therefore its implementation.

### What is the scope of the PAFA role?

In order to assist the Workgroup in discharging its terms of reference, ELEXON summarised the scope of the PAFA role. This summary was drawn from the UNC MOD506 Modification report.

#### Background

A Performance Assurance Framework (PAF) is to be introduced into the gas market arrangements to facilitate the monitoring and reporting of Transporter, Shipper and Transporter Agency performance and incentivise parties to reduce settlement risk and improve accuracy. The Performance Assurance Committee (PAC) (UNCC<sup>1</sup> sub-committee) will be created to oversee the PAF and the PAFA will be appointed for the purposes of:

- producing, publishing and maintaining a Performance Report Register
- creation, management and maintenance of the PAF Risk Register; and
- determining performance levels attained by those subject to the Performance Assurance regime.

The PAFA will be required to act with all due skill, care and diligence when performing its duties and shall be impartial, ensuring that any consideration of risks is equitable in their treatment of Shippers, Transporters and the Transporter Agency.

#### Criteria

The PAC shall produce a clear set of criteria for the appointment of the PAFA. Whilst this has not yet been drafted, the current view is that the criteria will include:

- The ability of the PAFA to produce, publish and maintain a Performance Report Register and the creation, management and maintenance of the gas PAF Risk Register
- Changes to services are expected to be made in the future, therefore the PAFA should indicate its ability to deliver new services;
- Consideration of the relevant knowledge and expertise of the candidates.

#### PAFA Services

A draft of the services to be provided by the PAFA indicates the role can be broadly broken down into two main functions.

##### 1. Administration services to the PAC; this includes:

- Maintenance and publication of the Performance Reports Register (including publication of required reports to industry)
- Review of Performance Reports and consideration of effectiveness, providing recommendations to the PAC as required

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252/06

P330

Draft Modification Report

---

5 May 2016

Version 1.0

---

Page 11 of 40

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<sup>1</sup> Uniform Network Code Committee (UNCC)

- Maintenance of each Report Specification
- Attend meetings of the PAC as required
- Provide Cost Estimate and track budget for the PAFA Scope

## 2. PAF Risk Register; this includes:

- Create, manage and maintain the PAF Risk Register
- Publication of the PAF Risk Register and any necessary reports
- Operate the PAF Risk Register process.

## What are the timescales for the PAFA tender?

The Workgroup asked if the timescales for the PAFA tender process have been made public yet. The Proposer responded that the gas Distribution Companies have advised that they will use Xoserve to run the PAFA tender and expects the Transporters to set up the PAC and ratify its terms of reference (ToR). They added that the ToR was discussed and set as interim by the UNC MOD506 Workgroup. However, the exact timescale for the tender process are still unknown.

## What are ELEXON's skills in the area of Performance Assurance and what are the key attributes of these skills?

ELEXON currently delivers the PAF under the BSC. ELEXON also provides support to the PAB, which oversees the PAF. It is anticipated that the PAC will perform a similar role to that of the PAB.

ELEXON provided the Workgroup with a high-level summary of their experience in this area:

- Operating a risk-based assurance regime (including experience in assessing risks and determining how performance in relation to specific risks can be monitored).
- Defining, collecting, storing and reporting KPIs.
- Creating and maintaining of a Risk Register.
- Experience developing audit terms of reference and delivering and overseeing audit work (including setting and tracking budgets for the scope).
- Operating a process to monitor and change the scope of the service

ELEXON asked whether the Workgroup disagreed with these skills or believed they needed further clarification.

The Proposer noted that ELEXON have not just operated a risk-based assurance regime, but also helped design that regime. They believed that the experience of designing a risk-based assurance regime from the ground up and the skill of developing this regime over time should be reflected. They noted that this skill can be applied to the growth and development of the gas PAF. ELEXON has demonstrated its ability to deal with changes to the PAF regime, both from the wider industry as well as improvements that ELEXON has suggested.

The Workgroup agreed with this view and that this should be added to ELEXON's skill set.

The Proposer advised that the number of years ELEXON has had experience with designing, operating and running a risk-based assurance regime should be reflected in its skill set.

The Workgroup agreed with this view.

The Group also believed that ELEXON engages effectively with the industry throughout its PAF processes and it manages to work with multiple industry participants for better performance. The Group felt that this should be highlighted, as the ability to work with the industry on performance issues is an important part of the PAF.

The Group also noted that ELEXON works with an independent auditor under the BSC PAF and that its experiences in this area could be applied to the gas PAF in the future, as such this should be added to ELEXON's skill set list.

### **PAB's view on the P330 Workgroup discussions**

ELEXON presented details of the P330 Workgroup meeting discussions at its meeting on 25 February 2016.

A PAB member clarified that the PAB should not endorse the Modification as that is the Panel's responsibility. The PAB member noted that the PAB is only recognising the skills that it believes ELEXON possess and is therefore not endorsing the change. ELEXON confirmed that the recommendation is only for the PAB to comment on the views put forward by the P330 Workgroup.

The PAB agreed that the comments from the Workgroup captured the PAF expertise of ELEXON. A PAB member highlighted one further area for inclusion relating to the running of BSC Central Systems. ELEXON manages the performance of the BSC Central Systems and the PAB member therefore suggested including the management of contracted services. A PAB member added that the provision of information and training should also be included as relevant expertise.

The P330 Workgroup noted the PAB's views on the Modification. One member questioned how relevant it would be to include ELEXON's experience of managing contracted services as a PAF skill. ELEXON advised that, in reference to PAF, we have experience managing contracts and external service providers which can be considered a useful skill under the PAF.

ELEXON recommended to the Workgroup that these skills be presented to the PAB, who are ultimately far more involved in the PAF under the BSC. This will enable its members to provide feedback to the Workgroup on its discussions. The Proposer and the Workgroup agreed that this should be done.

### **Conclusion**

In conclusion the Proposer and the Workgroup agreed the following skills in the area of Performance Assurance:

- Designing, operating and developing a risk-based assurance regime (including experience in assessing risks and determining how performance in relation to specific risks can be monitored) since 1998.

- Defining, collecting, storing and reporting KPIs;
- Creating and maintaining of a Risk Register;
- Working with industry participants to drive better performance and improve processes;
- Experience in developing audit terms of reference and delivering and overseeing audit work (including setting and tracking budgets for the scope); Experience in working with an external independent auditor and service providers; and
- Operating a process to monitor and change the scope of the service.

ELEXON recommended to the Workgroup that these skills be presented to the PAB, who are ultimately far more involved in the PAF under the BSC. This will enable its members to provide feedback to the Workgroup on its discussions. The Proposer and the Workgroup agreed that this should be done.

## What are the potential benefits (and synergies) associated with ELEXON providing settlement assurance services for both gas and electricity?

ELEXON advised the Workgroup that any benefit under P330 is a *potential* benefit, as this Modification will only allow the ELEXON Board the option of submitting a bid for the PAFA role. It does not automatically mean that a bid will be submitted or be successful. Any potential benefits or drawbacks under the BSC will only become certain if a successful bid is submitted.

ELEXON noted the following potential benefits and drawbacks to the Workgroup:

- Should the bid be successful, there is a benefit of defrayed costs to BSC Parties. For example, defrayed overhead costs leading to a reduction in BSC Costs payable under the current funding shares calculations
- Should the bid be unsuccessful, there is a disbenefit of the costs provided by BSC Parties to fund the bid being lost.

ELEXON also noted a potential benefit to the wider industry if ELEXON bid for the role, as there will be increased competition in the bidding process; ultimately providing the best candidate in a robust process. However, it was not clear that this was something that could necessarily be considered under the BSC Objectives. Equally, if ELEXON were to be successful, there is a potential benefit that best practice from both the gas and electricity can be applied to create a consistent assurance regime across both markets.

The Workgroup agreed with the summarised benefits and drawbacks provided.

## Any other benefits or drawbacks?

The Workgroup also identified the following potential benefits under P330:

- There is potential for BSC Parties to better scrutinise ELEXON's performance. If ELEXON were to bid for the PAFA role and not be successful then Parties should question why that is. Equally, better reporting to the Panel on ELEXON's services delivered under the BSC (in order to ensure delivery of core BSC Activities are not



### Development of the PAF

The PAF was established in 1998 on the recommendation of the Pool Auditor. ELEXON worked with the industry to grow and develop the PAF arrangements.

In 2007, BSC Modification P207 introduced the new PAF Governance regime, adding flexibility and transparency into the processes.



### What are funding shares?

About a third of the overall BSC Costs are collected on a tariff-style basis. The remainder is left as a sum of money that needs to be paid.

Funding Shares are ratios calculated for each BSC Party based on their generation or supply in the last month, and these determine what share (percentage) of that remaining money they will have to pay. Parties that generate or supply more will ultimately pay a larger share of the costs.

252/06

P330  
Draft Modification Report

5 May 2016

Version 1.0

Page 14 of 40

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impacted by PAPFA bid/work) would ensure that ELEXON strive for efficiency and excellence.

- The energy industry is making moves towards a dual fuel market with dual arrangements. Having ELEXON running a PAF for both gas and electricity is a further step in that direction and would allow synergies to be realised. It is beneficial to BSC Parties to have a single point of contact for gas and electricity assurance. Although, not all BSC Parties operate as dual fuel.
- There is an opportunity to look at what does and does not work in the gas and electricity markets if ELEXON were to be awarded the gas PAFA role. ELEXON have the opportunity to better both sides using lessons learned and processes from both the electricity and gas market to share knowledge and create best practice.

The Group also identified a further potential drawback. The Group noted that although the risk has been identified that the delivery of core BSC activities may be impacted if the PAFA role was won (see section below for more detail), it was highlighted that this should be expanded to include the potential impact of bidding for the PAFA role; not just in its delivery. ELEXON advised the Workgroup that the Panel can request additional KPIs and reporting to be provided if they feel it necessary.

### Competition for PAFA role

A Workgroup member asked whether ELEXON will consider what types of organisation may also be bidding for the gas PAFA role. They believe that this will help ELEXON assess whether it should submit a bid. They added that it would be useful for the industry to know how ELEXON would hold up next to potential tender competition.

Another member noted that there is a timing issue with trying to assess potential competition. It is likely that the bidders will remain confidential until the end of the bidding process. P330 needs to be progressed ahead of this tender process kicking off and therefore it is difficult to provide the industry with information of other bidders. The previous member responded that any speculative views could help.

The Proposer advised that ELEXON could look at the major types of consultancies and service providers that may go for the role and determine the pros and cons for each type. A member advised that if the Workgroup really want answers and considerations of the potential competition before the Modification goes to Ofgem, ELEXON might as well withdraw due to the timeline and potential confidentiality of the tender processes. They added that the Workgroup should have confidence in the ELEXON Board to make the right decision.

ELEXON advised that it may be able to allude to the kinds of companies that might get involved, keeping specific company details out of the information. A member noted that there is not going to be much transparency around who is going in for a bid until the end and therefore there is no value in doing this.

### Conclusion

The Workgroup agreed the following benefits and drawbacks under P330:

#### Benefits

- Should the bid be successful, there is a benefit of defrayed costs to BSC Parties.

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252/06

P330

Draft Modification Report

---

5 May 2016

Version 1.0

Page 15 of 40

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- There is potential for BSC Parties to better scrutinise ELEXON's performance (e.g. a bid is submitted and is unsuccessful, or the bid is won and the service is not delivered appropriately).
- Having ELEXON running PAF for both gas and electricity is a further step in the direction of dual fuel arrangements, will allow for synergies to be realised and provide BSC Parties with a single point of contact for gas and electricity assurance.
- There is an opportunity to look at what does and does not work in the gas and electricity markets if ELEXON were to be awarded the gas PAFA role (using lessons learned from both gas and electricity).

### Drawbacks

- Should the bid be unsuccessful, there is a disbenefit of the costs provided by BSC Parties to fund the bid being lost.
- There is a potential risk that the delivery of core BSC activities may be impacted if ELEXON resource is used to work on a bid for the gas PAFA role.

### What risks are there to current services should ELEXON take on the gas PAFA role? What can be done (for example, through reporting) to mitigate these risks?

ELEXON highlighted the potential risks to current services and the action ELEXON can take to mitigate these risks, as detailed in the table below.

Risk	Mitigating Action
Financial risk to BSC Parties of ELEXON undertaking additional work	Ring fence costs and responsibilities of PAFA work. Similar to EMR provisions in the BSC. The creation of PAFACo (like EMRS Ltd) is a key part of this ring-fencing.
Financial risk to BSC Parties of cross subsidies	Introduce ring fence provisions, similar to EMR, which are monitored as part of the company audit. The creation of PAFACo (like EMRS Ltd) is a key part of this ring-fencing? Equally the calculation of BSC funding shares mechanism is subject to BSC Audit so no cross subsidy of funding should occur.
Delivery of core BSC activities impacted	It will fall to the ELEXON Board and the senior management team to ensure delivery of BSC obligations and continued good service.  Additional KPI reporting to the Panel could incentivise continued deliver to clearly defined BSC standards. However, this will be at the Panel's discretion.

Workgroup members agreed with the potential risks and mitigating actions put forward. The Proposer noted the potential risk of ELEXON diluting its ability to deliver its core services if it is awarded the gas PAFA role. They added that the Panel raised some concerns about this when considering the Initial Written Assessment (IWA).

A member asked whether ELEXON intend on getting additional resource in to prepare the bid or whether it would use existing employees. ELEXON advised that they would look to



use existing knowledge and staff to prepare the bid and then get resource in to ensure that the core BSC activities are delivered. However, ELEXON are likely to require some bid support.

The Proposer advised that there may be a risk to ELEXON's reputation if the Board choose to bid and was not successful, or if successful in the bid, but failed to deliver. They suggested that this may ultimately show that ELEXON cannot operate an efficient assurance regime. Other workgroup members agreed with this view and believed that the Board will need to consider providing rationale to the Panel and the industry on its decisions and performance in this matter. One member added that, understanding 'why' is quite important here. Meaning that, if ELEXON failed to win the bid, this might not be a reflection of the quality or efficiency of service delivered under the BSC.

A member asked whether the cost of the BSC PAF is broken down and published, as it would be useful to know the costs of operating that service. We advised that ELEXON publishes this information in the Annual Performance Assurance Report (APAR) on the [Performance Assurance Processes webpage](#). The actual cost of delivering the assurance service in 2014/15 was £2.8m (against a forecast of £3.3m). The forecast cost for the forthcoming period (2016/17) is £3.5m as published on the [Performance Assurance Processes webpage](#) in the Risk Operating Plan (ROP). We added that this figure is associated with the BSC PAF, which is a more complicated and wider service than that proposed under the gas PAF. The Proposer highlighted that this cost also included external audit of all parties and that this was not a feature of the gas PAF arrangements.

### **Assessment Procedure Consultation responses**

There was concern raised by some respondents to the P330 Assessment Consultation around the effort and cost to submit a bid for the gas PAFA role.

Respondents noted that there is a risk that the quality in delivery of the core BSC activities may drop due to the work required to submit a bid and perform the role if it is awarded to ELEXON. There was specific concern from one member about how ELEXON may allocate its resources to support the PAFA tender/responsibilities ahead of core BSC activities. Another respondent felt that it is inappropriate for BSC Parties to have to pay for a bid with another citing the £100k cap on bidding costs.

A Workgroup member, having considered respondents views, advised that if the Modification is asking Parties to put up to £100k forward for a bid then ELEXON/PAFACo should also be providing some sort of business plan. The Member asked whether ELEXON were able to elaborate at all on this matter. ELEXON advised that the detail and commercial elements of the gas PAFA tender are currently unknown. ELEXON have provided the maximum £100k bidding cost estimate based on the information that is available under MOD506. However, until the detailed scope is made public ELEXON is unable to provide any further information on how it may resource for the work required on the bid or a more precise estimate of how much it will cost.

Another member felt that it's the principle of BSC Parties having to pay that is the main issue for them rather than the cost itself. At the moment there is no business plan, no explanation on how the funds will be returned should ELEXON be successful in a bid and no additional analysis on the defrayment of costs noted as a benefit of the Modification. Unfortunately the only number the industry has is the £100k it may cost them for ELEXON to bid.

A member noted that the reality of putting in a bid means that knowledge may be moved from one part of ELEXON to another but the Panel reporting would mitigate any issues that arise with resourcing. They feel that it comes down to ELEXON being able to manage performance and the industry trusting the Board to ensure core BSC activities are delivered and that any bid submitted is delivered to cost.

ELEXON advised that, in addition to the Panel reporting, there will be three separate sets of audits should ELEXON win the gas PAFA work, one for each of the following:

- ELEXON (as BSCCo),
- PAFACo; and
- the BSC.

ELEXON added that these audits should confirm that the finances and proper accounting procedures have been followed which will offer some assurance on the charging out of resources between ELEXON and PAFACo.

Since the Workgroup concluded its discussions ELEXON has confirmed internally the following information on the recovery of bidding costs and defrayment:

- Recovery of bid costs
  - The cost of the bid (i.e. the loaned funds (including interest, charged at a market rate)) would be factored into the contracted rate that PAFACo would charge for the ongoing service, ensuring the funds used in a successful bid would be returned to BSC Parties over the life of the contract.
- How defrayment works
  - Defrayment of BSC costs arises through the inclusion of an overhead absorption element being included in the charge-out rate used for staff costs. For example, the [ELEXON business plan 16/17](#) shows the budgeted income from EMRS Ltd as £2.3m. A proportion of this income (approximately 32%) is the amount ELEXON receives through overhead recovery. This is the defrayment of BSC costs by which BSC Parties continue to benefit.

## Conclusion

The table below sets out the risks that the Workgroup agreed would exist under P330, and the associated actions that could mitigate those risks.

Risk	Explanation & Mitigating Action
Financial risk to BSC Parties of ELEXON undertaking additional work	Ring fence costs and responsibilities of PAFA work. Similar to EMR provisions in the BSC. The creation of PAFACo (like EMRS Ltd) is a key part of this ring-fencing.
Financial risk to BSC Parties of cross subsidies	Introduce ring fence provisions, similar to EMR, which are monitored as part of the company audit. Equally the calculation of BSC funding shares mechanism is subject to BSC Audit so no cross subsidy of funding should occur.

Risk	Explanation & Mitigating Action
Delivery of core BSC activities impacted	<p>It will fall to the ELEXON Board and the senior management team to ensure delivery of BSC obligations and continued good service.</p> <p>Additional KPI reporting to the Panel could incentivise continued delivery to existing defined BSC standards. However, this will be at the Panel's discretion.</p>
ELEXON's reputation	<p>If the Authority approves P330 and then the Board ultimately choose not to bid it may send certain messages to the industry. Equally, if the Board choose to bid and are not successful, or are successful in the bid but fail to deliver; it may ultimately show that ELEXON cannot operate an efficient assurance regime.</p> <p>The Board may want to consider providing rationale to the Panel and the industry on its decisions and performance in this matter.</p>

## Should the cost of bidding be capped? Alternatively, should the Panel be required to approve the cost of bidding separately to this Modification?

The Workgroup discussed two options for approaching the approval of tender costs:

- **Option 1:** Tender value is capped by having a specific value added in the BSC via P330, with an additional requirement for Panel to agree that work may continue on any tender in the event that costs exceed the capped amount.
- **Option 2:** Tender value is uncapped in the BSC. However, specific requirement added for the Panel to approve any tender budget, and variation to that budget put to it by BSCCo. As above, the Panel would also be required to agree that work may continue on any tender in the event that additional costs over the budgeted amount would be otherwise incurred.

The Workgroup questioned how much it will cost to tender for the gas PAFA role. ELEXON advised the Workgroup that the estimated costs associated with tendering for the SEC (under Modification P290) were quoted at 'up to' £110k.

The Proposer noted that the size of the role for the gas PAFA is smaller than that of the SEC and believes that the estimated costs to tender should also be less.

A Workgroup member advised that they cannot see how it could cost more than tens of thousands to bid.

A member wished to clarify that the Workgroup should focus on the cost of the tender and not the value of the enduring service. They added that ELEXON should not need to buy in a lot of expertise as the gas PAFA role will be building on work that's already being done. They asked ELEXON to provide an estimate of its bidding costs for the Workgroup to consider as a cap to be specified in the draft legal text.

A member questioned whether an agreed '£' figure in the legal test would be arbitrary and noted that Panel oversight/approval of funds might allow for more flexibility. The Proposer responded that what matters is that the estimated figure and level of risk is accepted by the industry. The higher the figure, the greater the risk; therefore it is important to ensure

there is an agreed capped amount. Another member believed it is important to look at the ELEXON Board for discretion rather than trying to figure out an appropriate capped figure.

A member asked whether the legal text could be written so that it's the Board that makes the decision on the tender budget. ELEXON advised that the industry may feel it is more appropriate to have a capped value as it will provide more transparency and certainty. We added that the Board could report the actual cost to tender to the Panel after the fact, which will help to ensure transparency. The Workgroup agreed with this view.

A member questioned whether there is a third option, whereby the tender costs are capped and there is no option for the Panel to approve additional expenditure. A member reiterated that, from an external perspective, 'capping only' will give the industry some certainty around the maximum amount that could be spent. The Proposer agreed with this view noting that the industry may be more comfortable with a 'capped only' approach and it will build trust with BSC Parties, which is of benefit.

## **Conclusion**

The Proposer and the Workgroup agreed that capping a specific maximum value for tender costs in the P330 legal text is the most suitable approach.

Following the Workgroup meeting, ELEXON worked on providing an estimate on the potential maximum costs to submit a bid for the gas PAFA role. ELEXON advised the Workgroup that the total cost required (comprising of both internal and external) to bid is estimated at £100k. Further information on the bidding activities can be found in Section 2.

## **What is the most appropriate Implementation Date, taking into account the tender timescales and implementation of Project Nexus?**

ELEXON recommended an Implementation Date of five or ten Working Days following Authority approval. They believe that this will allow for the Modification to be implemented without restricting ELEXON's ability to tender if it's approved.

The Proposer and the Workgroup agreed with a recommended Implementation Date of 5 Working Days following Authority approval.

## **What is the benefit of setting up a subsidiary to tender for the PAFA role?**

The Workgroup questioned why ELEXON feel it is necessary to set up a subsidiary to tender for the role as well as operate the role if the bid is won. ELEXON advised that this is the neatest way to ring-fence costs from the outset. Additionally, if the ELEXON subsidiary is going to be the enduring provider it's much cleaner and easier for the subsidiary to also tender for the role (i.e. the company that puts forward the tender should be the company that will be the enduring service provider if it wins the business).

A member questioned when the subsidiary would be set up. ELEXON advised that, the way the legal text is structured, it would be set up if a bid is imminent.

ELEXON clarified that P330 legal text is drafted so that it is the BSCCo that will make the decision to raise the subsidiary.

The Workgroup asked whether the 'PAFACo' Board will be the same as the ELEXON Board. ELEXON advised that it is anticipated that the 'PAFACo' Board will be smaller but it is not known at the moment who would be on that Board, though it will likely be constituted in a similar fashion to that of the EMRS Ltd Board, i.e. comprising a subset of ELEXON Ltd Board members and Executive Directors. The ELEXON Board will determine the makeup of the 'PAFACo' Board.

The Proposer wished to clarify what will happen with the loan provided by BSCCo to 'PAFACo'. ELEXON advised that under the proposed solution BSCCo's loan to 'PAFACo' will only be repayable if a tender bid is successful. If a bid for the PAFA role is lost there would be no liability on 'PAFACo' to repay the loan.

### **Will the competitiveness of the PAFA tender be dampened due to ELEXON involvement?**

The Workgroup discussed a concern raised by a respondent to the P330 Assessment Procedure Consultation in that ELEXON's involvement in the PAFA tender process may dampen the competitiveness of the tender.

The respondent noted that MOD506 requires Gas Transporters, which includes National Grid Electricity Transmission (NGET) to undertake a competitive procurement exercise to appoint a gas PAFA. They added that NGET is the sole owner of ELEXON and therefore question the objectivity and impartiality of the procurement exercise due to the relationship between the two companies.

The respondent also highlighted that any tender submission by ELEXON for the gas PAFA role will be funded by BSC Parties. Other organisations have different business models and will therefore have to bear the costs of submitting a bid and harbour any loss of funds should the bid fail.

The respondent therefore questioned whether the ownership of ELEXON and the funding of a bid submitted by ELEXON will act as a disincentive for others to participate within the procurement process (i.e. reducing the ability of the procurement panel to secure and therefore compare the widest possible range of competing offers).

ELEXON advised the Workgroup that the respondent's views on ELEXON's ownership has been flagged to the Transmission Company (NGET). The Transmission Company provided ELEXON with the following response which was shared with the Workgroup:

*National Grid Gas (NGG) is prevented from giving or receiving any unfair commercial advantage to any of its affiliates (e.g. NGET), and has business conduct rules in place to secure compliance, which include restrictions on the flow of confidential information and also prevent NGG from entering into any preferential or discriminatory arrangements with its affiliates.*

*ELEXON is considered an "uncontrolled subsidiary" of NGET (i.e. NGET holds the share capital and is required by licence to have a BSC but has little ability to direct or influence ELEXON as an entity).*

*There are express limitations on how and in respect of what NGET can exercise its shareholders rights (BSC Section C 2.3.1 and 2), essentially only to process matters to give effect to the BSC. NGET has no role on the Board / in the process*

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252/06

P330  
Draft Modification Report

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5 May 2016

Version 1.0

Page 21 of 40

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*of electing the directors of the Board. The actual day to day running of ELEXON is delegated to the Chief Executive who is appointed by the Board after consultation with the Panel.*

A Workgroup member noted that other potential competitors in the tender process may agree with this view and see the BSC Party funding as an 'unlimited pot' of money which could discourage an organisation from bidding. They also understand how people may view ELEXON's ownership as a potential deterrent. However, in practice there is a very large gap between ELEXON and NGET when it comes to running the day-to-day business. The member can see where the respondent is coming from however they do not feel that it is a strong argument against the Modification.

Another member noted that the £100k cap on tender costs shows potential competitors how much ELEXON are willing to spend on a bid and can therefore understand the respondent's argument.

The Proposer has confirmed that it is the Gas Distribution Companies who are procuring the service, via Xoserve. Therefore, NGET will have nothing to do with the gas PAFA tender process.

## Conclusion

The Workgroup considered these stated risks regarding competition and ultimately concluded that they are very small and that it is unlikely that prospective bidders would be dissuaded in the way that was suggested by the respondent.

## Simplicity of the gas arrangements

One respondent to the Assessment Procedure Consultation did not agree with one of the potential benefits identified by the Proposer, in that ELEXON's involvement in the gas arrangements will provide them with first-hand experience of its simplicity (which could in future help towards making the electricity arrangements more efficient). The respondent feels that some industry participants may argue that the gas arrangements are too simple and therefore there is no benefit to the electricity arrangements.

The Proposer advised that the gas arrangements are more simplistic in terms of its settlement and reconciliation arrangements. However, there is no performance assurance which is what is lacking from the arrangements. They also note that gas and electricity are two very different commodities and that no one has actually looked at whether the gas arrangements are more simplistic due to the nature of the commodity or the model. The Proposer therefore sees ELEXON's involvement in the gas industry as a benefit as the PAFA will gather information on risks and issues in each market meaning that a comparison of the two markets can be made.

A Workgroup member disagreed with this view stating that there is nothing keeping the energy industry from doing a study of both markets to better understand how they operate in order to simplify the gas and electricity arrangements.

## Applicable BSC Objectives and the Transmission License

A Workgroup member noted a response received to the Assessment Procedure Consultation about the Applicable BSC Objectives. The respondent noted that

'Transmission' does not stretch to gas with respect to the BSC (i.e. the BSC draws its interpretation from the Transmission License and the Electricity Act 1989). They also state that the Applicable BSC Objectives were framed purely for the purpose of the BSC and whilst they acknowledge that ELEXON's credentials as a potential PAFA service provider are credible, they feel the Objectives do not yet support the intention of P330.

ELEXON noted that it highlighted such potential issues with the BSC Objectives when Ofgem revised the Transmission license in May 2015 (in order to permit the consideration of Modifications such as P330).

## Has a valid defect under the BSC been identified?

The Workgroup considered an Assessment Procedure Consultation response regarding the proposed defect under P330, in that the respondent does not believe that a valid defect has been identified under the BSC.

One Workgroup member did not completely agree with the respondent's view that a defect had not been identified. They noted that a Modification is considered valid when the Proposer of that Modification feels there is a defect or issue under the BSC and that you cannot stop someone from raising a Modification when it is designed in the best intentions.

ELEXON advised that the Proposer wants ELEXON to be able to participate in the tender process for the gas PAFA. However, this is currently not allowed under the BSC which is why it is cited as the defect. A Workgroup member added that an omission from the BSC is still considered a valid defect.

## Conclusion

The Workgroup considered the views put forward by the respondent but ultimately agreed that the Proposer's defect is valid, in that the BSC does not currently allow ELEXON to be able to tender for the gas PAFA role.

## Are there any Alternative Modifications?

One respondent to the P330 Assessment Procedure Consultation recommended an alternative approach. They believe that the right approach is to first adjust ELEXON's vires, objectives and ownership model and then look at what activities ELEXON can be involved in outside of the BSC. They also note that it would be interesting to know whether opening up ELEXON's performance assurance function under the BSC to peer and competitive pressures will improve efficiency.

A Workgroup member agreed with the respondent's view that it would be more pragmatic to address ELEXON's vires etc. before implementing a Modification such as P330. The member advised that the industry should wait until P324 and P325 have been decided on before expanding ELEXON's work outside the BSC.

The member also liked the idea of a potential independent PAF that is not associated with a code administrator. There is a certain appeal to testing that function but it is outside the scope of this Modification and cannot be considered as an alternative. However, a single point for performance assurance in the energy industry is worth thinking about.

The Workgroup agreed not to take forward the respondents proposed alternative approaches.



A Workgroup member suggested another potential alternative approach. The member confirmed that they are not against the prospect of ELEXON expanding its role and being able to bid for the gas PAFA. However, they disagree with the cap of £100k and feel there should be no cap. This is because they feel the decision on how much should be spent is a business decision and should therefore sit with the ELEXON Board.

## Conclusion

The Workgroup had considered all potential alternatives for P330. The Workgroup by majority (all but one) agree that there are no alternative solutions that will better facilitate the Applicable BSC Objectives better than the proposed solution. The Workgroup therefore choose not to raise an Alternative Modification.





### Does P330 better facilitate the Applicable BSC Objectives than the current baseline?

The Proposer believes that there are potential benefits to the energy industry and BSC Parties if ELEXON were able to bid for the role of the gas PAFA. In particular it would be a step in moving to dual fuel arrangements in the energy market, where common processes are placed with a single entity to derive a common understanding, practices, synergies, cost efficiencies and ultimately consumer benefit.

The Proposer believes that P330 will better facilitate **Applicable BSC Objective (d)** as:

- sharing the fixed costs of ELEXON across the gas PAFA service allows costs to the BSC Parties to be defrayed;
- some parties cite the simplicity of the gas market arrangements, when compared to electricity arrangements. Therefore, ELEXON getting first-hand experience may enable it to identify and implement changes to better the electricity arrangements in the future; and
- bidding for the gas PAFA work may be able to give a view to BSC Parties of the competitiveness of ELEXON in delivering their existing obligations and be used to consider efficiencies.

**The majority of the Workgroup (four of seven) agreed with the Proposer's view that P330 will better facilitate Objective (d) better than the current baseline and also agreed with the Proposer's rational.**

**The Workgroup therefore by majority recommend that P330 is approved.**

A minority of the Workgroup (two of seven) disagreed and believe that P330 will be detrimental to Objective (d) for one or more of the following reasons:

- do not believe that P330 can meet the Applicable BSC objectives in principal;
- risk that the activities of putting forward a bid and running the gas PAFA service will impact the delivery of core BSC activities, which are already strained;
- do not believe that the implementation of this Modification will improve the efficiency of the balancing and settlement arrangement as there is no certain benefit arising under the BSC (for BSC Parties) – i.e. the defrayment of costs can only be realised if ELEXON is successful in its bid, while any costs incurred in an unsuccessful bid would be sunk;
- do not agree with capping the bidding costs as it would be more efficient to trust the ELEXON Board and allow it to manage the cost of any bid activity (but only if appropriate checks and balances were in place that ensured the Board was more accountable to BSC Parties such as those contemplated under Modifications P324 and P325); and
- do not agree with a capped value of £100,000 as this is too high.

### What are the Applicable BSC Objectives?

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

(b) The efficient, economic and co-ordinated operation of the National Electricity Transmission System

(c) Promoting effective competition in the generation and supply of electricity and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity

(d) Promoting efficiency in the implementation of the balancing and settlement arrangements

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

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

252/06

P330

Draft Modification Report

5 May 2016

Version 1.0

Page 25 of 40

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A minority of the Workgroup (one of seven) felt that P330 is neutral against all of the applicable BSC Objectives because:

- aside from the small implementation cost, there are no guaranteed costs or benefits arising under the BSC in relation to the BSC Objectives that can be associated with this enabling Modification - i.e. the defrayment of costs can only be realised if ELEXON is successful in its bid, while any costs incurred in an unsuccessful bid would be sunk; and
- while the Board has discretion to determine the amount spent on any bid up to the capped value (£100,000), and acknowledging that this may ultimately be less than the capped value, the cap itself is too high but cannot be lowered since the scope and commercial elements of the tender are currently unknown.

## **Implementation approach**

The Workgroup unanimously recommend an Implementation Date for P330 of 5 Working Days following Authority approval.

## **Legal text changes**

The Workgroup unanimously agreed with the draft legal text changes to the BSC, which can be found in Attachment A.

### Panel considerations

The Panel considered that it was important to ensure that the activities and costs of both a gas PAFA bid and, in the case of a successful bid, the operation of the gas PAFA service, are separate from BSC costs and do not impact on BSC activities. P330 would ensure this by ring fencing gas PAFA bid and operating costs and activities from BSC business. The creation of a separate 'PAFACo' subsidiary would be an important element of this.

The Panel considered the possibility of the gas PAFA tender being delayed due to the progression of Project Nexus. The Panel believed that delay to Project Nexus would not impact P330 or a bid by ELEXON for the gas PAFA role.

Two Panel Members were concerned by the prospect of ELEXON becoming involved in Project Nexus. Apart for the principle of P330, they did not believe that the gas PAFA role was a good tender option for ELEXON.

The Panel noted that it was not possible at this time to estimate the defrayed costs that would result for BSC Parties from ELEXON performing the gas PAFA role because the income from the gas PAFA role is not known. Panel Members believed that the bid cost cap of £100k seemed very high, particularly given the likely magnitude of the gas PAFA contract.

A Panel Member was concerned about ELEXON bidding for and potentially performing the gas PAFA role. The Member noted that under previous BSC Modifications, such as Approved Modification [P284 'Expansion of Elexon's role via the 'contract model''](#), consideration had been given to criteria specified by Ofgem which related to Parties benefiting, risks being managed and BSC standards being maintained; the Member did not believe P330 would meet these criteria<sup>2</sup> and set out the following concerns:

- They believe that external bids tend to attract greater scrutiny, and therefore also tend to draw in the best resource available, i.e. away from normal BSC work;
- KPIs are mentioned as part of the measures to mitigate risks but are not mandatory under P330;
- They believe ELEXON resource is already strained and bidding for other work would exacerbate this, citing as an example that ELEXON has been unable to complete an ongoing Aggregation Rule audit for some time; and
- They consider that the PAB and ELEXON's Performance Assurance team are already scheduled to review a great deal and are undertaking a lot of work, and they believe it is already proving difficult to perform such reviews in a timely manner, citing as an example that Supplier Charges have been due for review since 2014 but that the start date for this work is now in Q3 2016.

Overall, the Panel Member believed that an ELEXON bid for the gas PAFA role would be irresponsible because it would take critical resource away from core BSC activities. Rather than ELEXON conducting both electricity and gas PAFs being a benefit, as identified by the Workgroup, the Panel Member considered that there could be more benefit in a different

<sup>2</sup> The criteria, set out in the [Ofgem conclusions letter](#) of April 2012, are:

1. BSC Parties should benefit from any diversification;
2. The arrangements should not place disproportionate risk on BSC Parties;
3. Standards of service under the BSC should be maintained; and
4. ELEXON's BSC role should not give it any undue competitive advantage in a contestable activity.

body acting as gas PAFA. They felt this would encourage innovation and enable, after a reasonable amount of time, the performance of the two organisations and PAFs be compared with one another.

Another Panel Member agreed that ELEXON resources are under some strain, but considered that the Board should take this into account when deciding whether to bid for the gas PAFA. However, the Member believed that this is undermined by the lack of an effective means to hold the Board to account for its actions (implementation of one of the ongoing governance Modifications<sup>3</sup> may address this in the future, but neither of these are fully developed at present, let alone approved and part of the BSC baseline).

ELEXON agreed that the bid cost cap of £100k was significant, but that a cap of this magnitude is needed to ensure a decent bid can be submitted. The cap is a maximum amount and it will be up to the ELEXON Board to determine what amount should in fact be spent on a bid. ELEXON has bid for activities previously (e.g. Warm Homes), demonstrating both that ELEXON has experience managing a bid and that a reasonable amount should be spent on a bid to deliver a realistic chance of success.

The Consumer Panel Member commented that they considered the gas arrangements to be poorly assured, and that the change in gas assurance is partly motivated by the BSC PAF. They believed that ELEXON could either win the bid for the gas PAFA, or positively impact the bid process by its participation even if it is unsuccessful. The Member noted the concerns raised about a bid or the PAFA role distracting from core BSC activities, but considered that P330 would only enable a potential bid; it would be for the ELEXON Board to consider whether ELEXON is able to bid for and perform the gas PAFA role, and whether it would be beneficial to do so. The Member felt P330 had limited benefits against Objective (d), but that it would be beneficial overall.

The Ofgem representative commented that the Authority was not opposed to the principle behind P330. Noting the direction of travel for the industry indicated by the Competition and Markets Authority (CMA) findings, it may support P330 as an enabling change.

The Panel Chairman commented that in his capacity as ELEXON Board Chairman he could assure the Panel that the Board would want to make its reasons for undertaking a gas PAFA bid as clear as possible, subject to considerations around confidentiality and the constraints of a competitive tender process.

## Initial Panel views

### Applicable BSC Objectives

The majority of the Panel (five) believed that P330 **would not better facilitate Applicable BSC Objective (d)** for the reasons included in its initial discussions, and therefore supported the following views given by a minority of the Workgroup:

- they believe there is a risk that the activities of putting forward a bid and running the gas PAFA service will impact the delivery of core BSC activities, which are already strained;
- they do not believe that the implementation of this Modification will improve the efficiency of the balancing and settlement arrangement as there is no certain benefit arising under the BSC (for BSC Parties), i.e. the defrayment of costs can

<sup>3</sup> [P324 'Review of BSCCo's governance: introducing improved accountability to BSC Parties'](#) and [P325 'Improving the accountability of BSCCo to stakeholders and better aligning BSCCo governance with best practice'](#).

only be realised if ELEXON is successful in its bid, while any costs incurred in an unsuccessful bid would be sunk; and

- they believe the cap value of £100,000 is too high.

A minority of the Panel (two) believed that P330 **would better facilitate Applicable BSC Objective (d)** for the reasons given by the majority of the Workgroup and set out in Section 7.

The Panel therefore initially recommends by majority that **P330 should be rejected**.

### Legal text

The Panel unanimously agreed that the draft redlined changes to the BSC in Attachment A deliver the intention of P330.

### Implementation Date

The Panel unanimously agreed with the recommended Implementation Date of 5 Working Days following Authority approval, as set out in Section 5.

## 9 Report Phase Consultation Responses

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

### Summary of P330 Report Phase Consultation Responses

Question	Yes	No	Other
Do you agree with the Panel's initial majority recommendation that P330 should be rejected?	3	4	1
Do you agree with the Panel that the redlined changes to the BSC deliver the intention of P330?	7	-	1
Do you agree with the Panel's recommended Implementation Date?	8	-	-
Do you have any further comments on P330?	2	6	-

### Views on Panel's initial recommendation to Reject

A majority of respondents believed that P330 would better facilitate the Applicable BSC Objectives compared with the baseline and should be approved, and therefore disagreed with the Panel's initial majority recommendation that P330 should be rejected.

### Views that P330 should be rejected

Three of the eight respondents to the consultation agreed with the Panel's initial recommendation that P30 should be rejected. These respondents agreed with the reasons put forward by the majority of the Panel.

One of these respondents also commented that the gas PAFA tender might be delayed due to the progression of Project Nexus. They felt this could allow Modifications P324 and P325 to progress, and these Modifications mitigate some of the concerns around core BSC activities associated with P330. This respondent also felt it may be appropriate to consider potential changes to industry code governance to be announced in June 2016 when the CMA issues its final report on its investigation into the energy market.

Another respondent commented that the P330 solution would mean that Parties would be potentially funding a tender exercise for an activity entirely outside the scope of their licence and the legislation which governs that licensable activity. They believed it would not be fair for Parties to fund and bear the risk associated with such activities.

The latter respondent also considered that potentially adding costs to Suppliers over which they have no control or visibility of recovery may also be damaging to competition in the supply of electricity, and therefore believed P330 may have a detrimental impact on Objective (c). They also believed P330 is detrimental to objective (d) because imposing costs on BSC Parties that do not relate to the management and administration of balancing and settlement arrangements would reduce the effectiveness, efficiency and cost reflectiveness of such administration.

252/06

P330  
Draft Modification Report

5 May 2016

Version 1.0

Page 30 of 40

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## Views that P330 should be approved

Four of the eight respondents disagreed with the Panel's initial recommendation that P330 should be rejected. Another respondent did not give a conclusive response but indicated that they felt P330 would have wider benefits for the electricity and gas markets.

The four respondents that supported P330 agreed with the views of the minority of the Panel (and majority of the P330 Workgroup). These respondents did not agree that core BSC services would be adversely impacted by P330.

Respondents commented that the market is moving toward dual fuel solutions. A bid by ELEXON could lead to the development of synergies and efficiencies to the benefit of all Parties.

One respondent's view that P330 would better facilitate Objective (d) was contingent on core BSC performance not being impacted. However, they noted that under P330 the BSC Board would consider whether ELEXON should tender, and can make an informed decision only once the scope of the PAFA role and tender details are released; if the Board decides to tender the respondent would expect it to ensure core BSC services were maintained.

The response from the P330 Proposer, Scottish Power, reiterated its arguments in support of P330 and sought to clarify the following points:

- The Gas PAFA is outside Project Nexus and is not a linked deliverable to the project.
- Project Nexus is a re-development of Xoserve's central systems, bringing site specific reconciliation to the whole market, rather than just for sites with an estimated Annual Quantity of 73,200 kWh.
- The PAFA will look to assure Uniform Network Code Parties affecting settlement performance under the new Nexus arrangements (once operational) but will also have the opportunity to look at the existing arrangements, in particular if Project Nexus is delayed.
- Xoserve would be the procuring party, with a Performance Assurance Committee (PAC) of Shippers and Gas Distribution Companies aiding in the procurement process. Xoserve is owned jointly by all of the Large Gas Transporters, not National Grid alone.

The Proposer also noted that the £100k cap on bid costs was included to ease concerns of some of the Workgroup that Parties could be exposed to unlimited bid costs, but that they (and other Workgroup members) considered the cap to be unrealistic. Though high, it did address the concern of unfettered liability, and a more realistic cap level could provide insight to other bidders with respect to the resources ELEXON would deploying in a bid.

The Proposer also believed that allowing ELEXON to bid for the gas PAFA would present an opportunity to market test ELEXON and understand if it offers value for money.

As well as the four responses set out above, one respondent did not give a conclusive response. They considered P330 was difficult to justify with respect to the BSC Objectives, given the potential cost and risk to BSC Parties. However, they noted the potential unrecoverable cost (in the case of an unsuccessful bid) was relatively small. They considered P330 would have wider benefits for the electricity and gas markets as a whole, and that many BSC Parties also active in the gas markets could benefit from increased competition in the procurement and delivery of performance assurance in the gas market.

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252/06

P330

Draft Modification Report

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5 May 2016

Version 1.0

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Page 31 of 40

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## Conclusion

Though a slim majority of consultation respondents supported P330 (in line with the majority of Assessment Procedure Consultation respondents and the majority view of the Workgroup) we do not consider that any new points have been raised that could lead us to recommend that the Panel should not confirm its initial recommendation to reject P330.

However, in its final discussions the Panel may wish to consider whether the consultation responses go any way to assuage the concerns of the majority of the Panel, while noting that a significant minority of respondents shared the concerns and agreed with the initial recommendation to reject.

## Legal Text

Seven of the eight respondents agreed that the redlined BSC changes deliver the intention of P330. We do not recommend any changes to P330 legal text following the consultation.

One respondent believed that the changes would deliver P330 but made some comments and suggestions for potential improvements. These comments, queries and suggestions are set out in the table below, along with ELEXON's responses to address the points raised and explain why we do not believe any change should be made.

Summary of P330 Report Phase Consultation Responses	
Respondent comment/query/suggestion	ELEXON response
The definition PAFACo does not capture the principle of this being a company created specifically to fulfil a particular purpose; define PAFACo as a subsidiary of BSCCo with the specific purpose of tendering for and, if successful, fulfilling the PAFA role.	PAFACo is defined the way it is, i.e. neutrally, because of the various uses of the term in the proposed Annex C-1 section 2. Although the definition is neutral, PAFACo is fully described by the new Annex C-1 drafting.
Use of the term PAFA in relation to UNC performance assurance could create misunderstanding alongside the existing BSC Performance Assurance activities; to avoid potential misunderstanding use another term, e.g. UNCPAFA, Gas PAFA.	Neither Performance Assurance Framework Administrator nor Performance Assurance Framework are terms in the BSC at present. We do not consider that confusion is likely, particularly as the terms are located in a separate specific provision of Annex C-1.
A "PAFACo Board" would be created, different from the Board (the Board of Directors of BSCCo, or the BSCCo Board) which creates it; consider being more explicit about "the Board" being the BSCCo Board.	We consider that 'PAFACo Board' and 'Board' are sufficiently distinct terms.



## Summary of P330 Report Phase Consultation Responses

Respondent comment/query/suggestion	ELEXON response
Proposed Annex C-1, C2.3.6 allows the Board "in its absolute discretion, [to] resolve to write off any loan or credit provided to PAFACo for PAFA Tender Costs which relates to an unsuccessful PAFA Tender exercise", up to a specified limit - under what circumstances might the Board not write off the loan or credit, and what would the consequences be?	<p>We consider the drafting, giving the Board discretion around write off, to be a sensible approach to documenting the financing of the tender; this approach was considered by the Workgroup.</p> <p>In addition, the loan may not be fully written off (there may be some funds recoverable) - as such, Board discretion is a pragmatic approach.</p> <p>The Board would not be able to write off the loan for a successful tender.</p>
The composition of the PAFACo Board would be dictated by BSC Section C7.5, and this might conflict with provisions for appointments in proposed Annex C-1.	We do not consider that there is any conflict between the provisions of Annex C-1 and BSC Section C7.5. Section C, 10.1.1(d) excludes paragraph 7 of Section C in respect of Permitted Affiliates.

## Implementation Date

All eight respondents unanimously supported the proposed Implementation Date. Two respondents commented that prompt implementation of P330, if approved, is necessary for the Modification to be effective, i.e. to allow ELEXON to be able to enter into the PAFA tender process if the ELEXON Board decides to do so.

## 10 Recommendations

We invite the Panel to:

- **AGREE** that P330:
  - **DOES NOT** better facilitate Applicable BSC Objective (d);
- **AGREE** a recommendation that P330 should be **rejected**;
- **APPROVE** an Implementation Date of 5 Working Days following Authority approval;
- **APPROVE** the draft legal text; and
- **APPROVE** the P330 Modification Report.

## Appendix 1: Business Rules for UNC MOD506

The purpose of the UNC Modification 506 is to introduce a framework for a gas performance assurance regime and require the Gas Transporters to appoint a PAFA by a competitive tender process.

The PAFA will run the scheme, under the oversight of UNCC or any relevant sub-committee. Modification of the UNC is required to recognise the role of the PAF, the Performance Assurance Scheme and the PAFA and incorporate appropriate arrangements to monitor performance of Shippers, Transporters and the Transporter Agency and allow an incentive regime to develop.

The PAF is limited to energy once it has entered the Local Distribution Zone (including Connected System Exit Point (CSEP) Supply Points). Gas transported through the National Transmission System (NTS) and supply points connected to the NTS are excluded from the arrangements created by this modification.

The PAF is to include CSEP Supply Points and CSEP Supply Meter Points following implementation of Modification 0440 Project Nexus – iGT Single Service Provisions.

### Business Rules

1. A person, the PAFA, shall be appointed and engaged by the Gas Transporters through a PAFA Contract for the purposes of:
  - a) producing, publishing and maintaining a Performance Report Register and the creation, management and maintenance of the PAF Risk Register; and
  - b) determining performance levels attained by those subject to the Performance Assurance regime.
2. The Transporters will be required to publish a Framework Document “Guidelines for Energy Settlement Performance Assurance Regime”. The initial content of the Framework Document be that which is provided in Appendix 1 of the Final Modification Report for MOD506.
3. The Gas Transporters will use reasonable endeavours to:
  - a) Undertake a competitive tender for the appointment of the PAFA;
  - b) Use the criteria developed by the Performance Assurance Committee (PAC) to assess each tender bid as part of their assessment to select the preferred bidder;
  - c) Select, agree terms and appoint the PAFA. Where the selected PAFA does not accept the appointment, invite the next most favoured PAFA in turn; and
  - d) Upon acceptance of appointment, establish the contract with the Prospective PAFA.
4. The PAC shall provide the final versions of the document as set out in 8 of the Guidelines document to the Gas Transporters.
5. On receipt the Gas Transporters shall commence the tender process using reasonable endeavours to:
  - a) Organise any meetings held in relation to the PAFA appointment;
  - b) Provide legal resource to prepare a tender document;
  - c) Organise the advertisement of the tender to all interested parties, in accordance with national and European legislation; and

- d) communicate to Shipper Users the outcome of the tender process; invite the prospective PAFA to take up the appointment.
- 6. The start date of the PAFA Contract will be as soon as reasonably practical.
  - 7. The Gas Transporters will require that the PAFA:
    - a) Acts with all due skill, care and diligence when performing of its duties as the PAFA and shall be impartial when undertaking the function of the PAF, ensuring that any consideration of risks is equitable in their treatment of Shippers, Transporters and the Transporter Agency; and
    - b) Compiles the Performance Report Register and Risk Register in accordance with the Guidelines Document.
  - 8. The Guidelines Document may be modified if UNCC votes by majority vote in favour of a proposed change.
  - 9. The Transporters will be required to provide data and information to the PAFA and assist in interpretation of information.
  - 10. For the avoidance of doubt, it is intended that this procurement and appointment for the PAFA process can be introduced ahead of the implementation of Project Nexus.

### Workgroup's Terms of Reference

Specific areas set by the BSC Panel in the P330 Terms of Reference

What are the potential benefits (and synergies) associated with ELEXON providing settlement assurance services for both gas and electricity?

What risks are there to current services should ELEXON take on the gas PAFA role? What can be done (for example, through reporting) to mitigate these risks?

Should the cost of bidding be capped? Alternatively, should the Panel be required to approve the cost of bidding separately to this Modification?

What is the most appropriate Implementation Date, taking into account the tender timescales and implementation of Project Nexus?

What changes are needed to BSC documents, systems and processes to support P330 and what are the related costs and lead times?

Are there any Alternative Modifications?

Does P330 better facilitate the Applicable BSC Objectives than the current baseline?

### Assessment Procedure timetable

Assessment Procedure Timetable for P330

Event	Date
Present Initial Written Assessment to Panel	10 Dec 15
Workgroup Meeting	8 Feb 16
Assessment Procedure Consultation	19 Feb – 11 Mar 16
Workgroup Meeting	W/B 14 Mar 16
Present Assessment Report to Panel	14 Apr 16
Report Phase Consultation	14 – 29 Apr 16
Present Draft Modification Report to Panel	12 May 16
Issue Final Modification Report to Authority	13 May 16

## Workgroup membership and attendance

P330 Workgroup Attendance			
Name	Organisation	8 Feb 2016	24 Mar 2016
Members			
Douglas Alexander	ELEXON ( <i>Chair</i> )	✗	✓
Adam Lattimore	ELEXON ( <i>Chair</i> )	✓	✗
Talia Addy	ELEXON ( <i>Lead Analyst</i> )	✓	✓
Angela Love	Scottish Power ( <i>Proposer</i> )	☎	✓
Emma Piercy	First Utility	☎	✓
Gregory Mackenzie	British Gas	✗	✓
Andrew Colley	SSE	✗	✓
Matt Keen	Npower	✗	☎
Phil Russell	Independent	☎	✓
Tim Newton	E.ON	☎	✓
Attendees			
Adam Richardson	ELEXON ( <i>Design Authority</i> )	✓	✓
Geoff Norman	ELEXON ( <i>Lead Lawyer</i> )	✓	✓
Ravi Matharu	Npower	☎	✗
Jonathan Dixon	Ofgem	✗	✗
Michael Houston	ScottishPower	☎	✗
Kevin Woollard	British Gas	☎	✗

252/06

P330  
Draft Modification Report

5 May 2016

Version 1.0

Page 38 of 40

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## Appendix 3: Glossary & References

### Acronyms

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

Acronym	
Acronym	Definition
BSC	Balancing and Settlement Code
CSD	Code Subsidiary Document
CSEP	Connected System Exit Point
DCC	Data and Communications Company
EMR	Electricity Market Reform
NTS	National Transmission System
OJEU	Official Journal of the European Union
PAB	Performance Assurance Board
PAC	Performance Assurance Committee
PAF	Performance Assurance Framework
PAFA	Performance Assurance Framework Administrator
ToR	Terms of Reference
UNC	Uniform Network Code
UNCC	Uniform Network Code Committee
WHD	Warm Home Discount

## External links

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

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

External Links		
Page(s)	Description	URL
4	UNC Modifications 506 and 506A webpage	<a href="http://www.gasgovernance.co.uk/0506">http://www.gasgovernance.co.uk/0506</a>
4	Issue 62 webpage	<a href="https://www.elexon.co.uk/smg-issue/issue-62/">https://www.elexon.co.uk/smg-issue/issue-62/</a>
6	P330 webpage	<a href="https://www.elexon.co.uk/mod-proposal/p330/">https://www.elexon.co.uk/mod-proposal/p330/</a>
7	Official Journal of the European Union webpage	<a href="http://www.ojec.com/">http://www.ojec.com/</a>
7	Official Journal of the European Union procurement thresholds	<a href="http://www.ojec.com/thresholds.aspx">http://www.ojec.com/thresholds.aspx</a>
14	P207 Webpage	<a href="https://www.elexon.co.uk/mod-proposal/p207-introduction-of-a-new-governance-regime-to-allow-a-risk-based-performance-assurance-framework-paf-to-be-utilised-and-reinforce-the-effectiveness-of-the-current-paf/">https://www.elexon.co.uk/mod-proposal/p207-introduction-of-a-new-governance-regime-to-allow-a-risk-based-performance-assurance-framework-paf-to-be-utilised-and-reinforce-the-effectiveness-of-the-current-paf/</a>
17	Performance Assurance Processes page of ELEXON website	<a href="https://www.elexon.co.uk/reference/market-compliance/performance-assurance/performance-assurance-processes/">https://www.elexon.co.uk/reference/market-compliance/performance-assurance/performance-assurance-processes/</a>
18	BSCCo Business Plan 2016/17	<a href="https://www.elexon.co.uk/wp-content/uploads/2011/10/BSCCo-Business-Plan_201617.pdf">https://www.elexon.co.uk/wp-content/uploads/2011/10/BSCCo-Business-Plan_201617.pdf</a>
27	P284 webpage	<a href="https://www.elexon.co.uk/mod-proposal/p284/">https://www.elexon.co.uk/mod-proposal/p284/</a>