

BSC Modification Proposal Form

At what stage is this document in the process?

P390

Allowing extensions to ELEXON's business and activities, subject to additional conditions.

01

Modification

02

Workgroup Report

03

Draft Modification Report

04

Final Modification Report

Purpose of Modification: This Modification seeks to introduce conditions into the BSC, subject to which ELEXON could undertake additional activities and business for the benefit of industry and the consumer. The conditions in this proposal incorporate the conditions previously agreed in respect of other permitted activities i.e. those ascribed under P330 (Allowing ELEXON to tender for the Uniform Network Code Gas Performance Assurance Framework Administrator) and P365 (Enabling ELEXON to tender for the Retail Energy Code).



The Proposer recommends that this Modification should:

- be assessed by a Workgroup and submitted into the Assessment Procedure; and
- be sent to Ofgem for approval (not a Self-Governance Modification Proposal)

This Modification will be presented by the Proposer to the BSC Panel on 12 September 2019. The Panel will consider the Proposer's recommendation and determine how best to progress the Modification.



High Impact: None



Medium Impact: BSC Parties, ELEXON



Low Impact: None

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Any questions?

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Timetable

The Proposer recommends the following timetable:

Initial consideration by Workgroup	W/C 30 September 2019
Assessment Procedure Consultation	18 November 2019 – 6 December 2019
Workgroup Report presented to Panel	9 January 2020
Report Phase Consultation	13 January 2020 – 31 January 2020
Draft Modification Report presented to Panel	13 February 2020
Final Modification Report submitted to Authority	17 February 2020

1 Summary

What is the issue?

The BSC restricts the activities of ELEXON and in the absence of a specific Modification any additional activities cannot be pursued by ELEXON (even when those activities would be of benefit to BSC Parties, industry generally and the consumer). In the past specific Modifications have been necessary which have enabled ELEXON to provide the Warm Homes Discount Reconciliation service, EMR settlement, and participate in gas assurance and REC manager appointment processes. Despite receiving industry support for taking on new activities, such individual Modifications to extend ELEXON's vires are time consuming and can be an unnecessary distraction for industry. They can also result in ELEXON being unable to pursue an opportunity within a required timeframe.

What is the proposed solution?

A framework that mirrors the protections incorporated within the previously approved Modifications (which are themselves based on tests introduced by Ofgem), plus the introduction of new, additional conditions, would increase efficiency whilst still providing the necessary safeguards for the consumer and BSC Parties.

In summary, any new activity would have to satisfy the existing conditions (which were established under approved Modification P330 and also repeated in approved modification P365), as well as additional safeguards. It is proposed that the ELEXON Board would be able to make decisions on which opportunities to pursue, subject to all of these conditions and report annually to BSC Parties on new activities that they had undertaken in that year, as well as the benefits that had been accrued by BSC Parties such as through defrayed BSC costs.

If BSC Parties were ever dissatisfied with the decisions of the Board, they still retain the right to remove (or threaten to remove) one or more of the ELEXON Board Directors.

2 Governance

Justification for proposed progression [not Self-Governance, Fast Track Self-Governance or Urgent]

Progression Route

A number of Modifications have already been progressed and approved by the Authority, which have extended the scope of activities which ELEXON undertakes. In particular P330 "Allowing ELEXON to tender for the Uniform Network Code Gas Performance Assurance Framework (PAFA) role" and P365 "Enabling ELEXON to tender for the Retail Energy Code (REC)". Each of these proposals has included provisions for a separate subsidiary to ensure that there is ring-fencing of any enduring operational costs

and risks associated with performing additional roles, beyond delivering the BSC activities. Therefore there are already agreed arrangements as to how any additional activities and business would be managed.

Self-Governance

This Modification is not proposed as a self-governance Modification Proposal, as it could have cost implications for BSC Parties. However, the benefits that could accrue from ELEXON bidding and winning other work could result in a defraying of material costs to BSC Parties. Therefore if this proposal is approved it is likely to have an effect, which could be material, on existing or future electricity consumers (Self-Governance criteria a)i).

Requested Next Steps

This Modification should be:

- assessed by a Workgroup; and
- submitted into the Assessment Procedure.

3 Why Change?

What is the issue?

Under the BSC Section C there are conditions placed upon ELEXON such that the company is unable to undertake any business or activity other than is provided for in the Code. These conditions are known as the ELEXON “vires”, in that they set out what ELEXON is allowed to do. The current “vires” have been in the BSC since inception, however a number of different opportunities have arisen, where the ELEXON Board and BSC Parties have seen merit in allowing ELEXON to either bid for work or to provide a solution to deliver Government policy. This has resulted in Parties to the BSC raising specific Modification Proposals to allow ELEXON to extend its “vires” with certain conditions as to ring-fencing of risk and how costs and benefits will be treated.

At present, each time an opportunity arises where ELEXON might be able to extend the company’s activities a Modification Proposal is required to agree a change in the “vires”. This is inefficient and an unnecessary distraction for industry and could hamper ELEXON’s ability to respond to a new business opportunity that would be beneficial to BSC Parties and the consumer.

Under the last specific Modification (P365), which amended the ELEXON vires to allow ELEXON to bid for the Retail Energy Code Manager role, one Party suggested that the Proposal did not go far enough and that the ELEXON Board should be allowed to investigate any opportunity which they felt allowed them to deliver the BSC services in a more efficient way¹. Further, in its decision letter on P365, the Authority agreed that this was perhaps something that could be considered in future.

¹ Page 14 of the BSC P365 Draft Modification Report

4 Code Specific Matters

Reference Documents

In considering this Proposal it would be beneficial for previous individual Modifications to be looked at, including P330² and P365³. These proposals successfully extended the vires of ELEXON to be able to bid for the Gas Performance Assurance Framework Administrator and the Retail Energy Code Manager whilst introducing certain safeguards, all of which are intended to be incorporated into this Modification. Similar changes were introduced (albeit via a direction of the Secretary of State rather than a Modification being raised), to introduce into the BSC provisions that enabled ELEXON to provide the Warm Homes Reconciliation service and EMR settlement service.

5 Solution

Proposed Solution

This proposal seeks to change the BSC to allow ELEXON to undertake additional activities provided certain conditions are met. These conditions include all of the conditions introduced in previous Modifications to ELEXON's vires, plus new additional conditions to provide additional safeguards.

Conditions previously included for P330 and P365, Warm Homes Reconciliation and EMR settlement:

Conditions previously included	How achieved
BSC Parties should benefit from any diversification	<p>New activity to contribute its fair share to the existing BSC overheads, so defraying costs for BSC Parties for their benefit. In addition any new activity will provide opportunities to staff to work on a wider range of activities, which will help ELEXON to retain, attract and develop its people for the benefit of industry.</p> <p>BSC Parties will not fund any use of ELEXON staff on work for the separate companies following the start of the new activity commencing. Resource usage for such work will be recorded and transfer payments made from the new or existing separate company to ELEXON.</p> <p>Note EMR activity has contributed £3.5m over the last 5 years</p>
The arrangements should not place disproportionate risk on BSC Parties	<p>New activity(ies) will be ring fenced either in a new separate company or an existing separate company and ELEXON will not guarantee the obligations or liability of the new activities. Note that this is greater separation and protection than is provided by other organisations that undertake Code administration services and which also undertake other, commercial more risky activities within that same Code services company</p>
Standards of service under the BSC should be maintained	<p>ELEXON will ensure and report that there is no adverse impact on the standards of service ELEXON provides to BSC Parties.</p> <p>Note during the many years of delivering the WHD (6 years) and EMR (5 years) there is no evidence of a deterioration in ELEXON's services.</p>

² <https://www.elexon.co.uk/consultation/p330-assessment-procedure-consultation/>

³ <https://www.elexon.co.uk/mod-proposal/p365/>

Expenditure prior to start of activity has to be repaid within 5 years of start of activity	Expenditure will be funded in the first instance by ELEXON from sums collected through the existing BSC annual budget mechanism, which is funded by BSC funding-parties. Note: This is repayable to BSC Parties within 5 years of the new activity commencing. If ELEXON funds a role that does not successfully commence then, as with P330 and P365, ELEXON would most likely have to write-off the funding.
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Proposed new Condition	Detail of Condition
Geographical limitation	<ul style="list-style-type: none"> Activity must be related to the UK
Sector limitation	<ul style="list-style-type: none"> Gas, electricity, heat and transport sector
Type of role	<ul style="list-style-type: none"> Demonstrable link to core competencies
Where any new activity is undertaken or won by ELEXON, including on a 'for profit' basis, then ELEXON would deliver that activity through a 'Permissible Affiliate' (a subsidiary of ELEXON) in accordance with the provisions of the BSC	<ul style="list-style-type: none"> If any new activities undertaken by the Permissible Affiliate resulted in a profit then any sums available for distribution would be paid as a dividend to ELEXON which would consequently offset BSC Party charges
Cost at risk (preparation and bid costs) in any year to be no more than 1% of that year's approved budget	<ul style="list-style-type: none"> 1% is considered an appropriate amount to represent a business development budget.

The ELEXON Board will take the decisions whether to bid for and agree to undertake work, subject to the conditions outlined above and where there would be a benefit to BSC Parties in defraying costs. This proposal would vest decisions on what ELEXON's activities and business should be with the ELEXON Board and the Board would have to determine whether the various conditions were satisfied. These conditions include all the conditions previously applied for P330 and P365, plus new additional conditions to safeguard the interests of BSC Parties.

6 Impacts & Other Considerations

Impacts

Securing any additional activities will enable certain existing ELEXON overheads to be defrayed, reducing the ongoing charges paid by Trading Parties and their customers. In addition, as has been recognised by Ofgem and consultation respondents⁴, giving ELEXON the ability to participate in bid processes could increase competitive pressures to those processes. Any new activity will provide opportunities to staff to work on a wider range of activities, which will help ELEXON to retain, attract and develop its people for the benefit of industry.

This Modification Proposal is an enabling Modification and therefore will have no immediate impact on Trading Parties. However, if the Proposal is approved it will allow the ELEXON Board to determine if an additional activity satisfies the existing and new conditions and can be undertaken by ELEXON.

⁴ <https://www.elexon.co.uk/wp-content/uploads/2018/01/P365-Authority-Decision.pdf>

Does this modification impact a Significant Code Review (SCR) or other significant industry change projects, if so, how?

The Proposer does not believe that this Modification is linked to any live Significant Code Reviews and requests that this Modification be exempt from the SCR process.

7 Relevant Objectives

Impact of the Modification on the Relevant Objectives:	
Relevant Objective	Identified impact
a) The efficient discharge by the Transmission Company of the obligations imposed upon it by the Transmission Licence	Neutral
(b) The efficient, economic and co-ordinated operation of the National Electricity Transmission System	Neutral
(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	Neutral
(d) Promoting efficiency in the implementation of the balancing and settlement arrangements	Positive
(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]	Neutral
(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	Neutral
(g) Compliance with the Transmission Losses Principle	Neutral

In the view of the Proposer this Modification will better facilitate Applicable BSC Objective (d) as:

- sharing the fixed costs of ELEXON across other activities allows costs to the BSC Parties to be defrayed; and
- participating in the tendering process for other activities will provide a view to BSC Parties of the competitiveness of ELEXON in delivering its existing obligations and be used to consider efficiencies that could be achieved from ELEXON and other like bodies; and
- any new activity will provide opportunities to staff to work on a wider range of activities, which will help ELEXON to retain, attract and develop its people for the benefit of industry.

These were the same reasons cited by the Proposer of P330. Due to the parallels between this Modification Proposal and P330, it is worth highlighting the reasons for Ofgem's decision to approve P330. In its decision letter, Ofgem stated that it had previously considered the case for allowing ELEXON to diversify its activities.

In accepting BSC Modification P284 'Expansion of ELEXON's role via the 'contract model'' in September 2012, Ofgem set out its view that whilst there might be benefits of diversification, robust arrangements had to be put in place to mitigate any additional risk to the BSC and BSC Parties. Ofgem considered that the following criteria would have to be met:

- BSC Parties should benefit from any diversification;
- The arrangements should not place disproportionate risk on BSC Parties;
- Standards of service under the BSC should be maintained; and

- ELEXON's BSC role should not give it any undue competitive advantage in a contestable activity.

Ofgem also stated that it would be appropriate for the ELEXON Board and BSC Parties more generally to give further consideration to a more limited diversification under the existing structure.

Ofgem stated that they agreed with the BSC Panel that P330 should be assessed against relevant objective d) only, and that there will be a neutral impact upon the other BSC objectives. Ofgem considered that the first three of the criteria set out above were captured under relevant objective d), whereas the fourth extends beyond the BSC objectives and is suitably considered as part of Ofgem's wider statutory duties. For this reason the Proposer does not believe that the fourth criteria is a matter for the BSC.

Regarding Ofgem's wider statutory duties, Ofgem stated in its P330 decision letter that whilst the benefits of ELEXON's participation in the gas PAFA tender might not directly be of consideration for the BSC Objectives, that it considered that the existence of additional bidders in the gas PAFA tender should improve the extent and quality of the competition for that contract. This was therefore consistent with Ofgem's wider statutory duties.

8 Implementation Approach

As this Modification Proposal is a 'Code only' change it is proposed that that the BSC changes are implemented 5 Working Days following determination by the Authority.

9 Legal Text

To be developed in line with the final proposal, following assessment by a Workgroup.

10 Recommendations

Proposer's Recommendation to the BSC Panel

The BSC Panel is invited to:

- Agree that P390 not be progressed as a Self-Governance Modification Proposal;
- Agree that P390 be sent into the Assessment Procedure for assessment by a Workgroup;