

Phase

Initial Written Assessment

Definition Procedure

Assessment Procedure

Report Phase

Implementation

Improving efficiency of Default Funding Share process and Energy Supply Company Administration

This Modification seeks to allow the Funds Administration Agent (FAA) to process a Default Funding Share for unpaid Trading Charges earlier to reduce the cost of the borrowing facility and reduce the risk of shortfall. The Modification will also allow the Panel to instruct the FAA to release Trading Charges where the default relates to an Energy Supply Company Administration (ESCA).



Elexon recommends the Panel raises the attached Modification Proposal in accordance with the provisions of Section F - Modification Procedures F2.1.1 (d)(i)



Elexon recommends this Modification is progressed directly to the Report Phase with an initial recommendation to approve



Elexon does not consider that this Modification impacts the European Electricity Balancing Guideline (EBGL) Article 18 terms and conditions held within the BSC

This Modification is expected to impact:

- All BSC Parties
- Elexon

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About This Document



Not sure where to start? We suggest reading the following sections:

- Have 5 mins? Read section 1
- Have 15 mins? Read sections 1, 4, 5 and 6
- Have 30 mins? Read all sections
- Have longer? Read all sections and the annexes and attachments
- *You can find the definitions of the terms and acronyms used in this document in the [BSC Glossary](#)*

This document is a recommendation to the Balancing and Settlement Code (BSC) Panel to raise a Modification Proposal (Attachment A) in accordance with BSC Section F2.1.1(d)(i).

Elexon will present this paper to the BSC Panel at its meeting on 8 September 2022. If the BSC Panel agrees to raise the Modification Proposal, this document will form its Initial Written Assessment (IWA), and the Proposal Form will be updated and published on the Elexon website accordingly.

There are three parts to this document:

- This is the main document. It provides details of the Modification Proposal, an assessment of the potential impacts and a recommendation of how the Modification should progress.
- Attachment A contains the Proposal Form.
- Attachment B contains the proposed legal text changes to give effect to this Modification.

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1 Summary

What is the issue?

The Default Funding Share (DFS) process requires nine Working Days (WD) from generating the Advice Note to receiving funds. The unpaid amount is mutualised and invoiced to all other BSC Parties pro rata after six WD. This leaves the Funds Administration Agent (FAA) with insufficient funds to balance payments to zero until the non-payment is recovered. The FAA must therefore use a borrowing facility to cover the debt with debt interest paid by all customers.

If there are insufficient funds to cover payments out, the FAA will operate a shortfall process. This results in payments out to BSC Parties being scaled back until the funds can be recovered by DFS.

This can have an impact on BSC Party cash flow and creates a significant administrative burden for the FAA, putting daily Trading Charge processes at risk. Further, the shortfall process does not impact all Parties equally, those that have amounts payable are not impacted.

What is the proposed solution?

The proposed solution is based on a change to FAA system, the BSC and Code Subsidiary Documents to allow Trading Charges for BSC Parties in Section H Default to be mutualised from the Advice Note date Advice Note/Notification date onwards without delay to reduce the duration of outstanding payments.

Impacts and costs

This Modification is expected to impact all BSC Parties as they are all affected by DFS amounts. However, it will only be a small impact as Parties will be billed the same amount but they will receive their invoices earlier. It will also impact the FAA as the FAA generates Advice Notes and Backing Sheets for Trading Charges each WD. The same Trading Charges will be billed just on a different timescale.

This Modification is expected to impact [BSC Section N `Clearing, Invoicing and Payment`¹](#), [FAA User Requirements Specification²](#) and [FAA Service Description documents³](#). A small system change is required to the FAA system to allow DFS to be performed earlier.

Costs Estimates			
Organisation	Implementation (£k)	On-going (£k)	Impacts
Elxon	11-13	0	Implementation costs driven by the system changes to the FAA system. Also minor costs from changes to the BSC documents.
NGESO	0	0	No impact identified

¹ <https://www.elxon.co.uk/the-bsc/bsc-section-n-clearing-invoicing-and-payment/>

² <https://www.elxon.co.uk/csd/funds-administration-agent-user-requirements-specification-faa-urs/>

³ <https://www.elxon.co.uk/csd/service-description-for-funds-administration/>

Costs Estimates			
Organisation	Implementation (£k)	On-going (£k)	Impacts
Industry	0	0	No impact identified
Total	11-13	0	

Implementation

We propose this Modification is implemented via a special release, 10 WD after the Self-Governance Objection window closes.

Recommendation

We recommend the Panel raise this Modification Proposal as it will better facilitate Applicable BSC Objective (d) by promoting efficiency in the DFS process (in accordance with F2.1.1(d)(i)). Should the Panel agree to raise the Modification, we recommend that the Modification Proposal is progressed straight to Report Phase as the proposal is of a minor nature and the solution is fully developed. We also believe it has no impact on the EBGL balancing terms and conditions and that it meets the Self-Governance criteria.



2 Why Change?

What is the issue?

The DFS process is performed in the event of non-payment of Trading Charges by a BSC Party with insufficient Credit Cover to clear the unpaid amount. This typically requires nine WD from generating the Advice Note to receiving funds. The unpaid amount is mutualised and invoiced to all other BSC Parties pro rata after six WD. These timings are a result of legacy procedures which involved manual operation and printing of notices by postal arrangements.

This then leaves the Funds Administration Agent with insufficient funds to balance payments to zero until the non-payment is recovered. The FAA must therefore use a borrowing facility to cover the debt with debt interest paid by all customers. The FAA is also limited by the BSC to be able to hold a maximum borrowing facility of £10m, but is currently set at £5m.

If there are insufficient funds to cover payments out, the FAA will operate a shortfall process. This results in payments out to BSC Parties being scaled back until the funds can be recovered via the DFS. This can have an impact on BSC Party cash flow and creates a significant administrative burden for the FAA, putting daily Trading Charge processes at risk. Further, the shortfall process does not impact all Parties equally, those that have amounts payable are not impacted.

When a BSC party goes in Administration, Section N allows for monies due to the party to be withheld and be used to offset their debt. However in the event of an ESCA, because the party is in Administration and paying off their debts, Section N cannot be enforced.

Background

What happens when a Party Defaults?

When a Party defaults that share of the BSC Costs are considered a 'bad debt'. For every month within a BSC year all identified 'bad debt' from within that BSC year is aggregated to give a running total of the "Annual Default Costs".

Part of the "Annual Default Costs" is recovered monthly using the "Monthly Default Costs" (I.e. as 1/12 of Annual Default Costs). To recover this monthly amount, the 'Monthly Default Costs' is divided among other Parties, and are charged through the DFS. The DFS is calculated by re-calculating the General Funding Share, but without the share of money owed by the Defaulting Party/Parties. This gives each non-Defaulting Party its share of the BSC Costs excluding the bad debt. Each Party will then pick up this amount of the Monthly Default Costs, and this will result in each Party acquiring the same percentage increase in its overall payment.

Desired outcomes

The desired outcome is a reduction in the likelihood of performing the shortfall process and a reduced cost to serve by lower utilisation of the borrowing facility. This is achieved as a result of mutualising debts through DFS earlier.

General Funding Share

The General Funding Share is the proportion of all BSCCo Charges paid by a Party. The Default Funding Share is the General Funding Share calculated ignoring the defaulting Party.

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The Panel would be able to instruct the FAA to make payments to the BSC Party that is in ESCA to allow the administrator to continue to operate the business with a normal BSC cashflow timescale.

3 Solution

Proposed solution

The proposed solution is based on a change to FAA system, the BSC and Code Subsidiary Documents to allow Trading Charges for a Defaulting Party (BSC Parties in Section H Default) to be mutualised from the Advice Note/Notification date (ND) onwards without delay, reducing the duration of outstanding payments from 6 WD (ND+9) to 0 WD (ND+3).

Diagram 1 demonstrates the payment scenarios which can occur in relation to payments. Under normal operation payments are made and received at ND+3 and balance to zero. In the event of a payment default where the Party has Credit Cover, the Credit Cover is used to resolve the default. There is a two WD borrowing period in practice as the Credit Cover is not technically utilised immediately, often the payment would be made a day after notification of the missed payment.

Where the Credit Cover is zero and the Payment is not received, the BSC requires the DFS to be actioned on ND+5 and therefore the mutualisation would go into Advice Notes on ND+6, allowing 3 WD for BSC Parties to make payment of the mutualised amounts when added to their Trading Charges.

Where the Party is in Section H Default, the Panel can instruct the FAA to treat the Party as a 'Defaulting Party' meaning that no payments will be made to the Defaulting Party and DFS is expected, so can be brought forward by two WD.

In each example, there is a funding gap for different durations from two to six WD. The proposed solution demonstrates that on instruction to treat the Party as a Defaulting Party, the funding gap can be completely removed and stop the need for use of the Borrowing Account. This is dependent on identifying an Event of Default under BSC Section H and Panel approval to treat the Party as a Defaulting Party.

Diagram 1: Billing Timeline

Scenario	Notification Date (ND)	ND+1WD	ND+2	ND+3	ND+4	ND+5	ND+6	ND+7	ND+8	ND+9
Normal Operation	Advice Note (Invoice)			Payment Received						
Payment Default with Credit Cover	Advice Note (Invoice)			Payment Not Received		Credit Cover Used				
Payment Default no Credit Cover	Advice Note (Invoice)			Payment Not Received			Default Funding Share Advice Notes			Mutualised Payments Received
Payment Default (Section H Default)	Advice Note (Invoice)			Payment Not Received	Default Funding Share Advice Notes			Mutualised Payments Received		
Proposed Solution (Section H Default)	Default Funding Share Immediately – Default Funding Share Advice Note			Payment Received						

Payments to a Party in ESCA are controlled through operational procedures by the FAA. There is no system solution required to make payments to a Party in ESCA. The decision to make payments to the Party would be made by the Panel following analysis and recommendation presented by Elexon.

Benefits

Cost to serve

The borrowing facility available to the FAA in the form of an overdraft has a standing charge and interest payable at a market rate. The costs are charged to BSC Parties. By

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reducing the unpaid amounts to be mutualised through DFS, the duration and amount of borrowing is reduced. The current cost of borrowing includes a fixed fee and variable interest fees, both of which are expected to reduce with earlier Default Funding Share.

Probability of Shortfall

The shortfall procedure has not been utilised in the history of the BSC, however with higher Energy Imbalance Prices persisting, more frequent peak prices and other challenging market conditions the probability of operating the shortfall procedure has increased. The procedure may be seen as a burden for both the FAA operation and BSC Parties. This is taking into consideration the additional administrative efforts and customers managing changes to expected cash flow. This is because the shortfall process requires a scaling back of payments out on the payment date followed by further undo procedures once mutualised amounts have been recovered.

Manual Process Risk

As part of the Kinnect Programme, considerations for FAA's re-development are under review. Currently, the FAA is dependent on a number of manual procedures, which means the operation of shortfall carries a manual process risk. Reducing the probability of shortfall reduces the risk of peaks in manual processing.

Market wide Impact of ESCA

Enabling BSC cash flow to continue, subject to BSC Panel decision, would enable the administrator to continue to operate the business with potentially lower borrowing from HM Treasury.

Applicable BSC Objectives

This Modification will better facilitate BSC Applicable Objective (d) 'Promoting efficiency in the implementation of the balancing and settlement arrangements' because it will shorten the DFS process which will lead to reducing the cost of borrowing facility and reducing the risk of shortfall. This more efficient procedure will benefit all BSC Parties.

Implementation Approach

Elexon recommends an Implementation Date for this Modification 10 WD after the Self-Governance appeal window closes. This is so the benefits can be realised as soon as possible and importantly before December 2022, when the highest risk of needing to call on the shortfall process exists.

There is a six week lead time for the system changes to be completed, the work will progress in parallel to the Modification so both the document changes and system changes can be implemented at the same time.



What are the Applicable BSC Objectives?

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

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

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

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

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

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

(g) Compliance with the Transmission Losses Principle

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4 Proposed Progression

Next steps

This IWA will be presented to the BSC Panel at its meeting on 8 September 2022, where we will invite the Panel to raise this Modification under Section F 2.1.1(d)(i) – as we believe it better facilitates Applicable BSC Objective (d).

If the Panel agrees to raise this Modification, it will then need to determine how it should be progressed. We recommend this Proposal progresses straight to the Report Phase. We believe this Modification is suitable for progressing straight to the Report Phase as the proposal is of a minor nature, amending timelines of a process, not the process itself. Further, the solution is fully developed, brings a range of benefits, with minor costs to implement and no anticipated impact on industry.

EBGL Impact

There are no EBGL impacts as a result of this Modification. The draft legal text does not make any change to any BSC Sections that constitute EBGL Article 18 Terms and Conditions as detailed in the Annex F-2 of the BSC, nor does it extend them.

Self-Governance

This Modification will not materially amend any BSC processes or procedures, it will simply allow the FAA to process a Default Funding Share for unpaid Trading Charges at an earlier date. As such, we do not believe it will materially impact the Self-Governance Criteria and so should be treated as a Self-Governance Modification.

Timetable

Following presentation of the Initial Written Assessment to the Panel, it is proposed that this Modification will be circulated for a 12 WD Report Phase Consultation before the Draft Modification Report is presented for decision at the BSC Panel meeting on 13 October 2022.

Proposed Progression Timetable for Modification	
Event	Date
Present Initial Written Assessment to Panel	8 September 2022
Report Phase Consultation (12 WD)	12 September 2022 – 27 September 2022
Present Draft Modification Report to Panel	13 October 2022
Self-Governance Appeals Window (15 WD)	13 October – 3 November 2022
Publish Final Modification Report	14 October 2022

What is the Self-Governance Criteria?

A Modification that, if implemented:

- (a) does not involve any amendments whether in whole or in part to the EBGL Article 18 terms and conditions; except to the extent required to correct an error in the EBGL Article 18 terms and conditions or as a result of a factual change, including but not limited to:
 - (i) correcting minor typographical errors;
 - (ii) correcting formatting and consistency errors, such as paragraph numbering; or
 - (iii) updating out of date references to other documents or paragraphs;
- (b) is unlikely to have a material effect on:
 - (i) existing or future electricity consumers; and
 - (ii) competition in the generation, distribution, or supply of electricity or any commercial activities connected with the generation, distribution, or supply of electricity; and
 - (iii) the operation of the national electricity transmission system; and
 - (iv) matters relating to sustainable development, safety or security of supply, or the management of market or network emergencies; and
 - (v) the Code's governance procedures or modification procedures; and

(b) is unlikely to discriminate between different classes of Parties.

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5 Impacts and costs

The central implementation costs of this Modification will be less than £1k to make the necessary changes to the BSC Section and CSDs and £10k to £12k for the changes to the FAA systems. No ongoing costs are expected.

We do not expect there to be any implementation costs for Parties and Party Agents resulting from this Modification.

Implementation cost estimates			
Organisation	Item	Implementation (£k)	Comment
Elxon	Systems	10 - 12	Costs associated with changes to the FAA system.
	Documents	1	Costs associated with drafting and implementing Section N, FAA User Requirements Specification and FAA Service Description
	Other	0	No impact identified
NGESO	Systems	0	No impact identified
	Other	0	No impact identified
Industry	Systems & processes	0	No impact identified
Total		11 - 13	

Impact on BSC Parties and Party Agents		
Party/Party Agent	Potential Impact	Potential cost
All BSC Parties	BSC Parties will be billed the same amount but will be billed earlier to prevent the need to borrow and reduce the risk of shortfall. BSC Parties should not observe any operational change.	None

Impact on the NETSO	
Potential Impact	Potential cost
No impact	None

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Impact on BSCCo		
Area of Elexon	Potential Impact	Potential cost
Settlement & Invoicing	Updates to documents and additional FAA business rule to manage.	L

Impact on BSC Settlement Risks

This Modification does not directly affect any BSC Settlement risks as it is a small change to Elexon's Default process.

Impact on BSC Systems and processes	
BSC System/Process	Potential Impact
FAA	The FAA can currently apply a DFS at day 'D' the payment date and subsequent dates. The FAA system will require a change to allow DFS to be performed at the Notification Date (3 days earlier than day 'D') which is the date on which the Advice Note is published.

Impact on BSC Agent/service provider contractual arrangements	
BSC Agent/service provider contract	Potential Impact
FAA	The FAA generates Advice Notes and Backing Sheets for Trading Charges each WD. The same Trading Charges will be billed just on a different timescale. Therefore the change only impacts the FAA which is the BSC Agent at the final stage of the Balancing and Settlement process.

Impact on Code	
Code Section	Potential Impact
BSC Section N 'Clearing, Invoicing and Payment'	Introduction of new clause to allow DFS from the Notification Date as prescribed in the Settlement Calendar.

Impact on EBGL Article 18 terms and conditions

No impacts identified. This Modification is also not expected to extend the EBGL balancing terms and conditions

Impact on Code Subsidiary Documents	
CSD	Potential Impact
FAA User Requirements Specification	Include new requirement to perform DFS from Notification Date for Defaulting Party. At the time of writing we aim to complete the drafting of the CSDs before it goes out for consultation.

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Impact on Code Subsidiary Documents	
CSD	Potential Impact
FAA Service Description	Include new requirement to perform DFS from Notification Date for Defaulting Party. At the time of writing we aim to complete the drafting of the CSDs before it goes out for consultation.

Impact on other Configurable Items	
Configurable Item	Potential Impact
None	No impact identified

Impact on Core Industry Documents and other documents	
Document	Potential Impact
Ancillary Services Agreements	No impact identified
Connection and Use of System Code	
Data Transfer Services Agreement	
Distribution Code	
Grid Code	
Retail Energy Code	
Supplemental Agreements	
System Operator-Transmission Owner Code	
Transmission Licence	
Use of Interconnector Agreement	

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

We do not believe that this Modification impacts any ongoing SCRs. We have requested that Ofgem treat this as a SCR Exempt Modification Proposal.



What are the consumer benefit areas?

- 1)** Will this change mean that the energy system can operate more safely and reliably now and in the future in a way that benefits end consumers?
- 2)** Will this change lower consumers' bills by controlling, reducing, and optimising spend, for example on balancing and operating the system?
- 3)** Will this proposal support:
 - i) new providers and technologies?
 - ii) a move to hydrogen or lower greenhouse gases?
 - iii) the journey toward statutory net-zero targets?
 - iv) decarbonisation?
- 4)** Will this change improve the quality of service for some or all end consumers. Improved service quality ultimately benefits the end consumer due to interactions in the value chains across the industry being more seamless, efficient and effective.
- 5)** Are there any other identified changes to society, such as jobs or the economy.

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Impact of the Modification on the environment and consumer benefit areas:

Consumer benefit area	Identified impact
1) Improved safety and reliability	Neutral
2) Lower bills than would otherwise be the case	Neutral
3) Reduced environmental damage	Neutral
4) Improved quality of service	Neutral
5) Benefits for society as a whole	Neutral

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6 Recommendations

We invite the Panel to:

- **RAISE** this Modification Proposal in Attachment A, in accordance with BSC Section F2.1.1 (d) (i)
- **AGREE** that this Modification:
 - **DOES** better facilitate Applicable BSC Objective (d);
- **AGREE** that this Modification can progress directly to the Report Phase;
- **AGREE** that this Modification **DOES NOT** impact the EBGL Article 18 terms and conditions held within the BSC;
- **AGREE** an initial recommendation that this Modification should be **approved**
- **AGREE** an initial Implementation Date of 10 Working Days after the Self-Governance appeal window closes;
- **AGREE** the draft legal text;
- **AGREE** an initial view that this Modification should be treated as a Self-Governance Modification; and
- **NOTE** that Elexon will issue the Draft Modification Report (including the draft BSC legal text) for a 12 WD consultation and will present the results to the Panel at its meeting on 13 October 2022.