Stage 03: Assessment Consultation

P285 'Revised treatment of RCRC for Interconnector BM Units'

Approved CUSC Modification Proposal (CMP) 202 will remove Balancing Services Use of System (BSUoS) charges/payments from Interconnector BM Units.

The Proposer believes that the BSC's Residual Cashflow Reallocation Cashflow (RCRC) can be considered as related to the imbalance cost element recovered within BSUoS, and currently all Parties are exposed to both. P285 therefore proposes that Interconnector BM Units should no longer be subject to RCRC charges/payments.

This Assessment Consultation for P285 closes:

5pm on **Friday 14 September 2012**

The Workgroup may not be able to consider late responses.

The Workgroup:
- Initially recommends **Approval** of P285

High Impact:
- Interconnector Users
- Interconnector Error Administrators
- Settlement Administrator Agent (SAA)

Medium Impact:
- All BSC Trading Parties that are subject to RCRC

Low Impact:
- ELEXON

What stage is this document in the process?

01 Initial Written Assessment

02 Definition Procedure

03 Assessment Procedure

04 Report Phase

Contents

About this Document

The purpose of this P285 Assessment Consultation is to invite BSC Parties' and other interested parties' views on the merits of P285. The P285 Workgroup will then discuss the consultation responses, before making a recommendation to the Panel on 11 October 2012 on whether to approve P285.

There are 4 parts to this document:

- This is the main consultation 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.
- Attachment A contains more information on the Workgroup's analysis and assessment. It includes the detailed analysis carried out by the Workgroup on the effects of P285. It also contains details of the Workgroup's membership and full Terms of Reference.
- Attachment B contains the draft redlined changes to the BSC for P285.
- Attachment C contains the specific questions on which the Workgroup seeks your views. Please use this form to provide your response to these questions, and to record any further views/comments you wish the Workgroup to consider.

The Workgroup is issuing P285 for parallel consultation with P286 'Revised treatment of RCRC for generation BM Units'. P286 will also impact the allocation of RCRC, although the two solutions are independent of one other. For more information about P286, please refer to the separate P286 Assessment Consultation document.

Further Information

More information is available in:

Attachment **A**: Detailed Assessment

Attachment **B**: Draft Legal Text

Attachment **C**: Assessment Consultation Questions

For further information, including a complete version of the impact assessment responses received, please see the P285 page of the ELEXON website.

Any questions?

Contact:
David Kemp

david.kemp@elexon.co.uk

020 7380 4303

1 Summary

Why Change?

CUSC Modification Proposal (CMP) 202 proposes to remove BSUoS charges from Interconnector BM Units. This proposal has been approved, which creates a potentially anomalous situation where Parties are liable for RCRC charges/payments from the Settlement imbalance process but are not liable for BSUoS charges/payments that include the cost to the system Operator of resolving those imbalances.

Solution

P285 proposes to exclude Interconnector BM Units from RCRC charges/payments.

Impacts & Costs

P285 impacts the BSC and the Settlement Administration Agent (SAA) Service Description and User Requirement Specification.

It will impact all BSC Trading Parties (notably Interconnector Users and Interconnector Error Administrators), the SAA and ECVAA, and ELEXON.

The central implementation cost of P285 is £70k, comprising £59k in SAA and ECVAA costs and £11k in ELEXON effort. Individual Party costs range from zero to £10k.

Implementation

The proposed Implementation Dates for P285 are 27 June 2013 (June 2013 BSC Systems Release) or 7 November 2013 (November 2013 BSC Systems Release), depending on when Ofgem's decision is received. The overall implementation lead time is approximately 5 months.

The Case for Change

By majority, the Workgroup believes that P285 would better facilitate the Applicable BSC Objectives, and therefore initially recommends that P285 is approved.

2 Why Change?

What is RCRC?

For each Settlement Period, each BSC Trading Party is charged or paid for any imbalance in each of their Energy Accounts. If they are short in an Energy Account (they sold/consumed more energy than they brought/generated), then they are charged for that shortfall at the System Buy Price (SBP). If they are long in an Energy Account (they brought/generated more energy than they sold/consumed), then they are paid for that excess energy at the System Sell Price (SSP).

The total amount of money paid to Trading Parties who are long in a given Settlement Period will not usually equal the total amount of money recovered from Trading Parties who are short in that Settlement Period, due to the dual imbalance cashout prices under the BSC. However, it is a requirement that the net costs arising from Trading Charges is zero. Consequently, the net of these charges must be recovered from or redistributed to all Trading Parties in order to ensure that the total charges in that Settlement Period net to zero. This recovery or redistribution is settled through the Residual Cashflow Reallocation Cashflow (RCRC).

In order to allocate these net charges, a Residual Cashflow Reallocation Proportion (RCRP) is calculated for each Energy Account in each Settlement Period. This proportion is calculated as the Energy Account's Credited Energy Volumes (QCE_{iaj}) as a proportion of the total Credited Energy Volume across the market in that Settlement Period. Each Party's RCRC payment/charge for that Settlement Period will then be the proportion of the residual cashflow equivalent to the sum of the RCRP of both their Energy Accounts.

It should be noted that RCRC represents the net money after the settlement of all Trading Charges – energy imbalances, the Balancing Mechanism payments and the System Operator BM Charge. However, the Balancing Mechanism payments and the System Operator BM Charge will always cancel each other out in a given Settlement Period. As a result, RCRC is generally formed only from the net of the imbalance charges in that Settlement Period.

How do RCRC and BSUoS interact?

The Balancing Services Use of System (BSUoS) charge is used to recover the costs incurred by the System Operator in balancing the system. These costs are generally formed from energy balancing costs, which are incurred through resolving the imbalances created by Parties failing to balance their positions, and system balancing costs, which are incurred through other activities such as managing transmission constraints. Like RCRC, these costs are recovered from or redistributed to Parties in proportion with their Credited Energy Volumes.

Both RCRC and a proportion of BSUoS charges/payments arise from the need to resolve any imbalances that occur on the system. Consequently, there is a relationship between these two charges.

Consider the scenario where the market is short overall. In order to resolve this net imbalance, the System Operator will have needed to buy extra energy through Offers made by Parties. The cost of buying this extra energy is recovered from Parties through BSUoS. At the same time, the Parties who were short, and thus contributed to the market being short overall, will have been charged for their shortfall at SBP. These payments are redistributed to Parties through RCRC.

What is the issue?

A CUSC Modification Proposal proposes to remove BSUoS charges from Interconnector BM Units. This has been approved, which creates a potentially anomalous situation where Parties are liable for RCRC charges/payments but are not liable for BSUoS charges/payments.

As the main imbalance price (SBP in this case)[1] is largely calculated from the costs incurred by the System Operator in accepting Bids and Offers, the amount of money recovered from Parties as part of the BSUoS charge for addressing imbalance and the amount of money redistributed to Parties through RCRC should be similar. However, they will not be equal as the main imbalance price will not equal the average price of balancing actions (due to the flagging of system balancing actions, the tagging of arbitrage and de minimis trades and Price Average Referencing (PAR) tagging carried out as part of the calculation of the main imbalance price). It should be noted that other System Operator costs are also recovered through BSUoS, and there is a second component to RCRC (see below). Nevertheless, BSUoS and RCRC can be considered related and opposite cashflows, and Parties are usually only exposed to the net of these charges.

If, in the scenario above, the system was long overall, then the reverse situation would exist. The System Operator would accept Bids to resolve the imbalance, and the payments (or costs) from these would be passed back to Parties through BSUoS. Consequently, SSP will be the main price, and the Parties who were long will be paid for their imbalance, the costs of which would be recovered from Parties through RCRC.

There is a second component of RCRC, which arises from offsetting any opposing imbalances that exist, for example when one Party is long and another Party is short by an equal amount. In this case, the System Operator will not have needed to take any action, as the two imbalances cancel each other out, and so there will be no resulting contribution to the BSUoS charge. However, as SBP will always be greater than or equal to SSP, the amount recovered in imbalance charges from the Party who was short will be more than the amount paid to the Party who was long. This means that there will be some additional residual cash left over that is redistributed to Parties through RCRC.

As the distribution of BSUoS and RCRC is based on Credited Energy Volumes, the Party that is liable for BSUoS charges/payments and the Party liable for RCRC charges/payments will often be the same, and they will usually pick up the same proportion of each. An exception will occur though if the relevant BM Unit is the subject of a Metered Volume Reallocation Notification (MVRN). If an MVRN is in place, then it will be the Subsidiary Party that will be charged/paid RCRC against the relevant Credited Energy Volumes. However, it will be the Lead Party that continues to be charged/paid BSUoS against those Credited Energy Volumes.

How/why does the Proposer want to change the current rules?

CUSC Modification Proposal (CMP) 202 will remove BSUoS charges from Interconnector BM Units. This proposal was raised as BSUoS charges could be perceived as a barrier to cross-border trades across Interconnectors. Under the EU Third Package, Interconnectors are treated as a part of the Transmission System. However, under the GB arrangements, Interconnector Users are treated as either generation or demand, and as such are treated in the same way as a generator or Supplier would be.

CMP202 was approved by Ofgem on 15 August 2012 for implementation on 30 August 2012. This creates an anomalous situation whereby Interconnectors may receive or pay RCRC yet no longer contribute to the System Operator cost of resolving energy imbalances. Whilst BSUoS and RCRC are separate cashflows, they are related; the System

[1] In each Settlement Period, one of SBP and SSP will be the 'main' price, which is calculated based on the Bids and Offers accepted by National Grid. The other price is the 'reverse' price, and is calculated using data on short-term trades obtained from the power exchanges. If the system is short, SBP is the main price and SSP is the reverse price. The reverse is true if the system is long.

Modification Proposal Form

A copy of the Proposer's Modification Proposal Form can be found on the P285 page of the ELEXON website.

Operator costs for energy balancing recovered through BSUoS are returned to BSC Parties via RCRC. Receipt or payment of RCRC to Interconnector Users without its corresponding BSUoS and opposite cashflow has the potential to create a distortion in cross-border trades between GB and the rest of the EU. This could also give rise to the potential for windfall gains or losses by those Parties who would no longer be liable for BSUoS.

In addition, regulations arising from the Third Package require that no additional charges are levied on cross-border trades. The RCRC charge, whilst part of the imbalance process, may be perceived as such a charge and therefore contrary to the requirements of the EU Third Package, and so should be removed to ensure compliance.

What are the potential impacts of European regulations?

European Directive 2009/72[2], which covers common rules for an internal European electricity market, recognises that "different types of market organisation will exist", and that Member States should take measures to ensure a level playing field. Recital 3 of Regulation (EC) No 714/2009[3] acknowledges obstacles to the sale of electricity on equal terms and without discrimination or disadvantage within the European community, and Article 1 sets fair rules for cross-border exchanges of electricity, in order to enhance competition. This regulation was introduced as part of the Third Package, which became legally binding on all EU Member States on 3 March 2011.

These European Regulations are directly applicable in Great Britain, and supersedes national law, so the GB (and therefore BSC) arrangements need to comply with these Regulations. If GB cannot demonstrate compliance, there is a risk that the Commission may initiate formal infringement proceedings against the GB Government. Applicable BSC Objective (e) also relates to the BSC's 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 (ACER).

The BSC's allocation of RCRC to Interconnector Users has the risk of being perceived as contrary to the aims of these regulations, as it could be perceived as a charge when RCRC is negative, and could provide an improper incentive to flow when positive. Although RCRC is related to the imbalance arrangements, and imbalance charges are permissible under the Third Package, the Proposer considers RCRC to be a 'grey' area, due to its application to all Parties, including Interconnector Users.

National Grid has also raised previous changes in order to amend the arrangements to better demonstrate compliance with the Third Package arrangements. They have already removed TNUoS charges[4], and has progressed CMP202 to remove BSUoS charges, from Interconnector Users. In addition, Approved Modification P278 'Treatment of Transmission Losses for Interconnector Users' will remove Transmission Losses from Interconnector BM Units.[5]

[2] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:211:0055:0093:EN:PDF
[3] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:211:0015:0035:EN:PDF
[4] Following Ofgem's approval of ECM-26 'Review of Interconnector Charging Arrangements'.
[5] P278 will be implemented on 29 November 2012

3 Solution

What is the proposed solution?

P285 proposes to also exclude Interconnector BM Units from RCRC. To achieve this, the Credited Energy Volumes from Interconnector BM Units (whether relating to an Interconnector User or an Interconnector Error Administrator) would be excluded from the calculation of each Party's RCRP. This will mean that Interconnector volumes would not be included in a Party's RCRP, and the share of the RCRC that would have been allocated to these Interconnector volumes will instead be reallocated across BSC Parties in proportion with their non-Interconnector Credited Energy Volumes.

P285 will not impact the Isle of Man Distribution Interconnector i.e. this Interconnector will not be excluded from RCRC. This is because it has a derogation granted to it by the Panel under Section K5.2 of the BSC such that it is not treated as an Interconnector (i.e. it does not have Interconnector BM Units or an Interconnector Error Administrator). It should be noted that any other future Interconnectors with such a derogation would also not be exempt from RCRC. However, any future Interconnectors without such a derogation and which would therefore be treated as a Transmission Interconnector would be exempt from RCRC under P285.

P285 will not impact any reporting flows such as the SAA-I014 flow, which will continue to report a Party's RCRP and RCRC values as currently. However, Parties who only hold Interconnector BM Units will receive RCRP and RCRC values of zero following the P285 Implementation Date. Parties with non-Interconnector BM Units will also see changes to their RCRP/RCRC values as a consequence of the RCRC previously allocated to Interconnector volumes being reallocated in proportion to each Party's non-Interconnector volumes.

Legal text

The proposed redlined changes to the BSC to deliver the P285 solution can be found in Attachment B.

Assessment Consultation Question
Do you agree with the Workgroup that the draft legal text delivers the intention of P285?
The Workgroup invites you to give your views using the response form in Attachment C

How does P285 interact with P286?

P285 has been raised in parallel with P286 'Revised treatment of RCRC for generation BM Units', as both of these Modifications seek to amend how RCRC is allocated among BSC Parties. P286 is seeking to exclude BM Units that are in delivering Trading Units from RCRC payments/charges, and has been raised in response to CUSC Modification Proposal (CMP) 201. Consequently, the solutions to these two Modifications are very similar, with the only differences being what type of BM Unit each seeks to exclude from RCRC. However, the solutions to these two Modifications are not dependent on one another.

The changes to the distribution of BSUoS charges under the CUSC have been raised as two separate CUSC Modifications (CMP202 seeks to exclude BSUoS charges/payments

What is the solution?

P285 proposes to exclude Interconnector BM Units from RCRC charges/ payments.

from Interconnector BM Units and CMP201 seeks to exclude BSUoS charges/payments from generation BM Units). It was for this reason that the corresponding changes to the BSC have been raised as two separate Modifications (P285 and P286), in order to align the proposed changes to the BSC with the corresponding changes to the CUSC. This will allow for greater flexibility in Ofgem's decision on the proposed changes, as by keeping the equivalent BSC changes as separate Modifications, Ofgem has the flexibility to approve or reject the BSC changes in line with its decisions on the corresponding CUSC changes.

Is a retrospective solution required?

No. It is not the Proposer's intention that the P285 solution should be applied retrospectively. The Proposer notes that the Implementation Date for CMP202 is several months prior to the earliest viable Implementation Date for P285, and that the perceived anomalous situation that P285 is seeking to remove will therefore exist for the period between the Implementation Dates for the two changes. However, the Proposer believes that the materiality of this situation will be relatively small, and that this scenario will only be temporary, and so a retrospective application of P285 would be disproportionate.

However, the Proposer notes that reducing undue delay in better aligning GB arrangement with those of the EU Third Package also reduces any risk that the RCRC is perceived as an incompatible charge and potentially questioned by the European Commission. It also reduces the amount of time that payments or charges through RCRC can give rise to anomalous market behaviour and inappropriate signals.

Is P285 impacted by the Electricity Balancing Significant Code Review?

Ofgem launched its Electricity Balancing Significant Code Review (SCR) on 1 August 2012. One of the areas that this SCR will look at is the imbalance cash-out arrangements, and any changes that arise in this area may impact the RCRC arrangements. As such, RCRC could be considered to be within the scope of this SCR.

The Proposer raised P285 before this SCR was launched. As such, it is up to the Proposer as to whether or not P285 would be put on hold while any related SCR progresses; neither the Panel nor Ofgem can do this without the Proposer's agreement (Section F5.4 of the BSC). The Proposer has elected not to put P285 on hold, and so P285 will progress irrespective of the progression of the Electricity Balancing SCR.

Some members of the Workgroup believe that the issue raised by P285 would be better discussed as part of the SCR, as this issue should be discussed as part of the wider picture. It is their view that this issue should be debated fully under the SCR, in order to resolve any underlying issues, rather than simply moving cashflows around in response to individual problems. The Proposer observes that the SCR could still examine RCRC as part of its review, and that this proposal could be considered as an interim step given the likely longer timescales involved with the SCR process and implementing any subsequent proposals. The Workgroup accepts that P285 may therefore be appropriate in order to achieve better alignment of GB arrangements with EU objectives. You can find full details of the Workgroup's discussions in this area in Section 6.

Are there any alternate solutions?

The Workgroup has considered whether there are any alternative solutions to P285; however it has not identified any which it believes would better facilitate the Applicable BSC Objectives when compared with the Proposer's solution.

One respondent to the P285 Industry Impact Assessment commented that they agreed with removing the component of RCRC that relates to the net imbalance volume. However, they disagreed with the removal of the component that arises due to offsetting imbalances, noting that this element is independent of BSUoS.

The Workgroup has considered this response, and has considered whether it is possible to separate out these two components. However, Workgroup members feel that this would be a more complex solution than the one put forward by the Proposer, which would increase risk and costs and require a longer lead time. They consider that the materiality of P285 is relatively low, and that the costs associated with a more complex solution may outweigh the materiality of the proposed solution.

In addition, the Proposer notes that a more complex solution would increase the lead time for P285, which would increase the interval between the implementation of CMP202 and the implementation of P285, and thus increase the time where Parties would be liable for RCRC while being exempt from BSUoS. The Workgroup therefore concluded not to raise this as an alternate solution to P285.

The Workgroup did not consider there to be any other alternate solution to P285, and so has concluded that there are no Alternative Modifications within the scope of P285 which would better facilitate the Applicable BSC Objectives than the Proposed Modification solution.

Assessment Consultation Question
Do you agree with the Workgroup that there is no Alternative Modification within the scope of P285 which would better facilitate the Applicable BSC Objectives than the Proposer's solution?
The Workgroup invites you to give your views using the response form in Attachment C

4 Impacts & Costs

Estimated central implementation costs of P285

The total central implementation cost for P285 is approximately £70k. This comprises:

- Approximately £59k in SAA and ECVAA costs; and
- Approximately £11k (45 man days) in ELEXON effort.

These are one-off implementation costs, and there would be no on-going central operational costs.

The SAA changes involve amending the calculation of RCRP within the SAA systems so that the Credited Energy Volumes from Interconnector BM Units are excluded. Consequential changes are needed to ECVAA systems to amend some related validation.

The ELEXON costs include managing the implementation project and updating the relevant BSC Sections, Code Subsidiary Documents and other documentation.

If the system changes for P286 are implemented at the same time as those for P285, then a cost-saving of approximately 40% can be made on their combined separate costs. See below for more information on the proposed parallel implementation approach for these two Modifications.

Indicative Industry costs of P285

BSC Parties have indicated in the P285 impact assessment that they would incur costs ranging from minimal up to £10k each in implementing P285. These costs are one-off costs in order to make the relevant changes to systems and processes for P285, and no respondents noted any on-going costs following implementation.

Respondents have stated minimal cost-savings if P285 and P286 are implemented in parallel.

Industry Impact Assessment

The full non-confidential responses made by Parties to the Industry Impact Assessment can be found on the P285 page of the ELEXON website.

Proposed parallel implementation approach with P286

P285 is being progressed in parallel with P286 'Revised treatment of RCRC for generation BM Units', as the changes proposed by P286 are very similar to those proposed by P285, with P286 proposing to exclude BM Units that are in delivering Trading Units from RCRC charges/payments.[6]

P285 has been raised in response to CMP202, which will be implemented on 30 August 2012. Consequently, the P285 Workgroup seeks to implement P285 in the earliest viable BSC Systems Release, with the June 2013 Release being the most feasible at present (see Section 5). P286 has been raised in response to CMP201, which, if approved, is unlikely to be implemented before 2015. Consequently, the P286 Workgroup seeks to implement P286 with the same Implementation Date as CMP201.

However, the proposed solutions for P285 and P286 are very similar, with the only difference being the type of BM Unit that each Modification seeks to exclude from RCRC charges/payments. Cost-savings can therefore be achieved if the central system changes for P285 and P286 were implemented at the same time.

[6] For more information on the proposed solution to P286, please see the separate P286 Assessment Consultation document.

If P285 and P286 are both approved, then the central system changes required for P286 could be deployed in parallel with those required for P285, but with the P286-specific changes left dormant until the P286 Implementation Date. Once the P286 Implementation Date is reached, the P286-specific changes could then be made live. If this approach was taken, then a cost-saving of around 40% can be achieved on the combined separate costs of each Modification.[7]

It should be noted that these cost-savings would only be achieved if both Modifications were approved. If P285 was approved but P286 rejected, then the costs of P285 would be as stated above. Equally, if P285 and P286 were implemented in separate Releases then the individual costs of each Modification would stand, as the cost-savings would not be realised as a result of parallel implementation.

This approach to implementing the central system changes would not affect the impacts on BSC Parties.

P285 impacts

Impact on BSC Systems and process	
BSC System/Process	Impact
SAA	Changes will be required to the calculation of each energy Account's RCRP.
ECVAA	Consequential changes will be required to some validation steps as a result of the SAA changes.

Impact on BSC Parties and Party Agents
Interconnector Users and Interconnector Error Administrators will no longer be charged or paid RCRC on the Credited Energy Volumes from their Interconnector BM Units. The RCRC payments/charges of all other BSC Trading Parties will increase in order to still allocate the total residual cashflow among all applicable Parties.

Impact on Transmission Company
None identified.

Impact on ELEXON	
Area of ELEXON	Impact
Release Management	ELEXON will manage the implementation project.

Impact on Code	
Code Section	Impact
Section T	Changes will be required to implement the solution. See draft legal text in Attachment B.

[7] The individual central costs of both P285 and P286 are £70k. If one Modification was approved and one rejected, that Modification would therefore incur central costs of £70k. If the Modifications were both approved but implemented separately, the total central costs would be £140k. If the Modifications were implemented in parallel, the combined costs would be £84k.

Impact on Code Subsidiary Documents	
CSD	Impact
SAA Service Description	Changes will be required to implement the solution. If P285 is approved, ELEXON will develop and consult on the necessary redlined changes as part of the implementation project.

Impact on other Configurable Items	
Configurable Item	Impact
SAA User Requirement Specification	Changes will be required to implement the solution. If P285 is approved, ELEXON will develop and consult on the necessary redlined changes as part of the implementation project.

Other Impacts	
Item impacted	Impact
ELEXON Guidance Documents	Updates will be required to the 'Calculation of RCRC' Guidance Document. If P285 is approved, ELEXON will make these changes as part of the implementation project.

5 Implementation

Recommended Implementation Dates

The Workgroup's recommended Implementation Dates for P285 are:

- 27 June 2013 (June 2013 BSC Systems Release) if ELEXON receives Ofgem's decision on or before 24 January 2013; or
- 7 November 2013 (November 2013 BSC Systems Release) if ELEXON receives Ofgem's decision after 24 January 2013 but on or before 6 June 2013.

The lead time for P285 is driven by the lead time required to make the changes to central systems. All respondents to the Impact Assessment indicated that they would need up to three months in order to implement any systems and process changes that they would need. Based on these lead times, the earliest viable Implementation Date for P285 is the June 2013 BSC Systems Release.

Parallel implementation with P286

The Workgroup has noted that the changes required to implement the P286 proposed solution are very similar to those required for P285, and that if both Modifications were approved, significant cost-saving could be achieved if the changes were deployed together compared to the combined costs for deploying each change individually. Although P286 would not be implemented until much later than P285, the changes required for its solution could be deployed in parallel with those for P285 and left dormant until the required Implementation Date. This would mean that activities such as the development, deployment and testing of the changes could be carried out in parallel, resulting in the cost-savings.

The lead time required for a joint implementation approach are only slightly longer than those for implementing one of the Modifications on its own. The Workgroup has therefore elected to use the slightly longer lead time for the combined approach as the basis for the cut-off dates for an Ofgem decision on P285.[8] However, if P285 is approved, it will be implemented in the first available BSC Release, irrespective of when P286 is approved.

If P286 is not approved at the time P285 is approved, then the central system changes would not be deployed together. The Workgroup notes that P285 has been raised in response to European legislation, while P286 has not, and that any cost-savings that would arise from implementing P285 and P286 in parallel, while not insignificant, would be far less than the costs GB would incur if the European Commission was to question any perceived non-compliance. Therefore, Ofgem may wish to achieve a quicker implementation for P285, even if that means not being able to realise any cost-savings that would arise from a parallel implementation approach.

Assessment Consultation Question
Do you agree with the Workgroup's recommended Implementation Date?
The Workgroup invites you to give your views using the response form in Attachment C

[8] P285 and P286 will be sent to Ofgem for decision in mid-December 2012.

Is P285 appropriate?

The Workgroup has considered whether any changes to the BSC are required to both demonstrate better alignment with EU objectives and to align the BSC with the changes being made under the CUSC by CMP202, and, if so, whether P285 is the correct solution.

Recommendation

By majority, the Workgroup initially recommends approval of P285.

Is RCRC impacted by European regulations?

Whilst RCRC is clearly part of the imbalance process, it is a cashflow applied to all Parties, irrespective of whether they are in or out of balance. It therefore has the potential to be perceived as a charge on Interconnector flows when negative and an improper incentive to flow when positive. Although imbalance charges are permissible under the Third Package, the Proposer considers RCRC to be a 'grey' area, due to its application to all Parties.

The Proposer notes that there is an EU aim to set fair rule for cross border exchanges, thus enhancing competition, and to remove obstacles to the sale of electricity on equal terms and without discrimination or disadvantage within the European community (Article 1 and Recital 3 of Regulation (EC) No 714/2009). Given that RCRC may positive or negative, it may result in the wrong market behaviour in respect of cross-border flows, and thus contrary to these aims.

Workgroup members have sympathy with this view, and are supportive of P285 if it would help to address this defect. Some members considered whether it is right to treat Interconnectors as a special case, but concluded that as Interconnectors are being increasingly viewed as part of the Transmission System, it would be right to treat them differently to other types of BM Units.

Are RCRC and BSUoS linked?

The Proposer believes that there is a relationship between RCRC and BSUoS, and that these two cashflows can be thought of as two sides of the same coin, as both cashflows are derived from the costs incurred by the System Operator in resolving energy imbalances on the system, as described in Section 2. As CMP202 has been approved, the current situation is that some Parties will no longer be required to pay the BSUoS charge, and so would not contribute to the costs incurred by the System Operator in resolving any imbalance on the system, but are still liable for RCRC.

Consider the scenario where a Party is perfectly balanced in a given Settlement Period, and therefore is not exposed to any imbalance charges. However, other Parties are short, and the System Operator has taken actions to ensure the system remains balanced. Under the current arrangements, this Party would be liable for a portion of the BSUoS charge to recover the costs incurred by the System Operator, and would also receive a share of the RCRC resulting from the imbalance charges levied under the BSC. These two charges would net off against each other. However, under P285, some or all of the BM Units belonging to this Party may be Interconnector BM Units, and, as CMP202 has been approved, this Party would not have to pay BSUoS against the corresponding Metered Volumes. However, they would still receive a share of the RCRC against these Metered Volumes. It is the Proposer's view that this could be deemed a windfall gain, and that this Party should not benefit in this way from imbalance caused by other Parties.

The majority of the Workgroup agree with the Proposer's view. However, one Workgroup member disagrees, and believes that BSUoS and RCRC are separate cashflows and that changes to the allocation of RCRC under the BSC are not needed in response to the proposed changes to BSUoS allocation under the CUSC. This member notes that the BSUoS charge is a cost-recovery mechanism levied by the System Operator in order to recover the costs incurred in balancing the system. This charge is not comprised solely of the costs of energy balancing actions, but also includes actions taken to alleviate system constraints as well as ancillary service charges, neither of which are related to imbalance. This cost-recovery mechanism is levied on CUSC Parties in proportion with their Metered Volumes, but this is only one of a number of ways that these costs could be recovered. In addition, it is for the System Operator to determine who it feels should be responsible for the costs incurred in balancing the system, and thus who should be liable for BSUoS under the CUSC.

In contrast, RCRC arises from the imbalance charging mechanism under the BSC, which the Workgroup member believes is separate from the cost-recovery mechanism under the CUSC described above. The imbalance charges are designed to act as an incentive to Parties to balance their positions. If a Party is better able to balance their position then their RCRC payment could be viewed as a 'reward'. One Impact Assessment respondent also considered that, while there may be a correlation between RCRC and BSUoS, the real relationship is between RCRC and cash-out; if a Party is subject to one then they should also be subject to the other, as RCRC is a component of the imbalance charging mechanism.

The Workgroup considered that if P285 is not implemented then that could impact Parties' incentive to balance. They believe that if an Interconnector User was not subject to BSUoS, but was still subject to RCRC, then they would be less incentivised to balance, as they would not have to contribute to the costs of balancing the system but would receive a subsequent payment through the RCRC mechanism. If this were the case, it may be more difficult for the System Operator to balance the system. However, the Workgroup notes that Interconnector BM Units do tend to balance their position due to the mechanism of allocating Interconnector volumes across Interconnector Users, and they tend to only be exposed to imbalance if there is a failure or curtailment of the Interconnector in the relevant Settlement Periods. The main imbalance risk with Interconnectors tends to lie with Interconnector Error Administrators. However, some Workgroup members believe the process of redistributing the net moneys across Parties may itself act as a disincentive to balance.

Although there were different views as to whether it is appropriate to amend the allocation of RCRC in response to changes to the allocation of BSUoS, the Workgroup agrees that it is important that GB is perceived as compliant with and furthering European objectives. They therefore believe that Interconnectors may be a special case, irrespective of whether or not there is a link between RCRC and BSUoS.

What is the materiality of P285?

P285 will reallocate RCRC charges/payments across BSC Parties in a different way. On the Workgroup's behalf, ELEXON has undertaken analysis of the potential effect P285 may have on the allocation of RCRC. This analysis uses real data from 2011, and models the effect that P285 would have had on the distribution of RCRC across this time should P285 have been in place and assuming that all other factors, including Parties' behaviour, remain unchanged.

Attachment A contains the full results of this analysis. Many Parties will hold both Interconnector and non-Interconnector BM Units, and so in this case, the Party would see both a reduction in RCRC charges/payments against their Interconnector BM Units and an increase in RCRC charges/payments against their non-Interconnector BM Units, resulting in a net change in their RCRC charges/payments. Taking such netting of charges/payments into consideration, the net materiality is around 3% of the total RCRC, or around -£700k of the -£21.2m RCRC pot in 2011 being moved from one Party to another.

The Workgroup noted that the results of the analysis gave a net figure for each Party. However, the impact on each Party would vary depending on whether RCRC is positive or negative, and whether the Party has a positive or negative RCRP in a given Settlement Period. Therefore, while the analysis gives a high-level view of how P285 will affect the allocation of RCRC, the impacts will vary between Settlement Periods.

One Workgroup member considered what impact P285 may have on power prices, noting that if generators were liable for an increased volume of RCRC then they may factor that change into the prices they charge for generation.

The Workgroup considered how well Parties would be able to forecast RCRC prices ahead of time, in order to be able to factor them into any changes in power prices, or whether Parties would attempt to include any windfall gains/losses they may make as a result of P285 into their prices or pass them on in another way. It should also be noted that Parties will likely have factored their BSUoS charges into their pricing calculations as well, and that if they are no longer liable for BSUoS but are still liable for RCRC then this may impact prices accordingly.

The Workgroup notes that there is uncertainty around several factors in any Settlement Period; for example, how well a Party is able to forecast imbalances. All of this uncertainty is factored into any prices, and so any uncertainty around RCRC would simply be added into this.

The Workgroup agrees that, while P285 may have an impact on the prices agreed between Parties, it would be difficult to calculate what these impacts would be without obtaining the relevant details from individual Parties, which Parties are unlikely to divulge. The wholesale price of electricity is a matter between the two Parties in a given trade, and would be agreed between themselves through bilateral trading, which lies outside of the BSC. The Workgroup notes that some analysis was carried out in this area by the CMP201 Workgroup, and the results of this analysis can be found in the CMP201 Workgroup's report to the CUSC Panel.[9]

[9] http://www.nationalgrid.com/uk/Electricity/Codes/systemcode/amendments/currentamendmentproposals/

What are the Workgroup's views against the Applicable BSC Objectives?

The following table contains the Proposer's and the Workgroup's views against each of the Applicable BSC Objectives:

Does P285 better facilitate the Applicable BSC Objectives?		
Obj	Proposer's Views	Other Workgroup Members' Views[10]
(a)	• **Yes** – Takes into consideration National Grid's obligations to account for developments arising from European legislation, and ensure that appropriate financial BSC arrangements are in place.	• **Yes** (majority) – Agree with Proposer. • **Neutral** – No impact.
(b)	• **Neutral** – No impact.	• **Neutral** – No impact.
(c)	• **Yes** – Aligning RCRC beneficiaries with those that are liable for BSUoS permits trades across Interconnectors to be based on price differentials, undistorted by RCRC charges/payments. • **Yes** – Would prevent Interconnector Users from receiving windfall gains or losses that would arise from being liable for RCRC but not liable for BSUoS.	• **Yes** (majority) – Agree with Proposer (one member specified this is contingent on CMP202 approval: if CMP202 is approved then 'Yes'; if CMP202 is rejected then 'No'). • **No** – P285 would exclude some Parties from RCRC who may be causing imbalances, reducing incentive to balance. Should treat all Parties the same. • **Neutral** – Not convinced P285 would have material impact on competition.
(d)	• **Neutral** – No impact.	• **Neutral** – No impact.
(e)	• **Yes** – Although RCRC is a redistribution of residual money from the imbalance arrangements, it can be negative, and so could be perceived as a charge on Parties trading across Interconnectors. This could be viewed as contrary to EU Third Package arrangements.	• **Yes** (majority) – Agree with Proposer. • **Neutral** – Unsure if RCRC could be considered a charge. RCRC is a component of imbalance charging, and Interconnector Users can still be exposed to imbalance under the Third Package. • **Neutral** – P285 may be premature, given possible future changes such as market coupling.

By majority, the Workgroup's initial view is that P285 does better facilitate the Applicable BSC Objectives, and should be approved. The Workgroup's initial recommendation was conditional on CMP202 also being approved by Ofgem, and the Workgroup unanimously believed that if CMP202 had been rejected then P285 should also be rejected. However, CMP202 was approved by Ofgem on 15 August 2012 for implementation on 30 August 2012.

[10] Shows the different views expressed by the other Workgroup members – not all members necessarily agree with all of these views.

Assessment Consultation Question
Do you agree with the Workgroup's initial view that P285 better facilitates the Applicable BSC Objectives when compared with the current BSC rules?
The Workgroup invites you to give your views using the response form in Attachment C