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| Modification proposal: | Balancing and Settlement Code (BSC) P232: Black Start and Fuel Security Compensation and Single Imbalance Price Derivation (P232) | | |
| Decision: | The Authority ¹ directs that the alternative proposal be made ² | | |
| Target audience: | National Grid Electricity Transmission Plc (NGET), Parties to the BSC and other interested parties | | |
| Date of publication: | 25 June 2009 | Implementation Date: | November BSC Systems Release |

Background to the modification proposal

Modification P232 "Black Start and Fuel Security Compensation and Single Imbalance Price Derivation" was raised by National Grid Electricity Transmission (NGET) on 23 December 2008 to improve the transparency of the compensation arrangements associated with a Black Start or Fuel Security Code (FSC) incident. It also proposes a potential methodology for the calculation of a Single Imbalance Price (SIP) to apply for each Settlement Period (SP) that falls within a Black Start period or FSC event³. This proposal is based on the investigations and subsequent conclusions reached by Issue Groups 32 and 33⁴.

A Black Start refers to the recovery process for restoring electricity on the National Transmission System (NTS) following either a Partial or Total Shutdown of the NTS⁵. Section G of the BSC sets out the Black Start provisions in the event that NGET signals that there has been a Partial or Total Shutdown. Once a Black Start period has been declared the operation of the Balancing Mechanism (BM) is suspended, a SIP applies and generators who are given Emergency Instructions⁶ under the Grid Code are entitled to compensation for any Avoidable Costs.

The FSC sets out the framework within which the Secretary of State may exercise powers contained in the Electricity Act 1989 to call and manage a Fuel Security Period (FSP)⁷. Amongst other things, it provides the Secretary of State with the power to direct a generator to operate in a certain way in order to manage the FSP. The FSC also outlines how those affected by a FSP can make a claim for remuneration for any Exceptional Costs. In issuing directions, the Secretary of State in consultation with the Authority and the Panel, may also deem it necessary to deviate from the normal operation of the BM. Where appropriate, it may direct that a SIP applies, limits on BM prices based on historic data apply, and the Credit Assessment Price⁸ (CAP) be revised.

¹ The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

² This document is notice of the reasons for this decision as required by section 49A of the Electricity Act 1989.

³ Where capitalised words and phrases are used within this note, those words and phrases will usually have the meaning given within the BSC.

⁴ See Elexon's website for the Issue 32 "Black Start" and Issue 33 "Fuel Security (FSC) Guidance" workgroup reports: www.elexon.co.uk

⁵ Under extreme conditions (e.g. multiple circuit tripping during severe weather), parts of the NTS could become disconnected from the main system, or islanded. In addition, there could be a Partial Shutdown where all generation has ceased in an island, or a Total Shutdown where all generation has ceased in the total system and there is no electricity supply from external Interconnectors. See Grid Code OC9.1.1.

⁶ An Emergency Instruction has the meaning given to that term in the Grid Code.

⁷ For the FSC document see: www.berr.gov.uk/files/file41951.pdf; For the FSC Guidance Note see: www.berr.gov.uk/files/file41952.pdf

⁸ The value of CAP is determined by the Panel, and determines the equivalent financial amount corresponding to a given amount of Energy Indebtedness (measured in MWh). See BSC Section M 1.4.1.

Another proposal, modification P231, was raised in parallel with P232 for an Authority decision. P231 proposes to improve the transparency of the arrangements and obligations associated with Black Start periods and FSC events.

The modification proposal

P232 proposes a suite of changes to the Black Start and FSC compensation arrangements including improving the transparency around the compensation arrangements.

SIP Methodology

P232 seeks to introduce a potential methodology for the calculation of SIP for the SPs that fall under a Black Start period or FSC event. Specifically, P232 proposes that:

- A SIP should be derived by taking the mean of the System Buy Price (SBP) and System Sell Price (SSP) for each SP over the previous 30 calendar days in order to determine a 'proxy' for the price of bulk electricity⁹ during a Black Start period or FSC event;
- A SP that was subject to a FSC event or instruction, a Black Start Period or an Emergency Instruction would not be used and would be replaced with another appropriate historical SP;
- The Panel would determine an alternative pricing methodology for the price of bulk electricity during the Black Start period or FSC event if the Panel deemed it to be more appropriate as a 'proxy'; and

The SIP, once determined by the Panel, is subject to the approval of the Authority.

Compensation Arrangements

Under the BSC and FSC, generators may seek compensation for certain costs incurred in following directions issued during a Black Start period or FSC event. P232 seeks to improve the transparency of the compensation arrangements by proposing a number of refinements to existing BSC processes. These refinements relate to:

- The inclusion of certain operational costs as Avoidable Costs;
- The claims application process (including allowing an extra 60 business days for a claimant to submit extra evidence);
- Claims Committee procedures; and
- A recommended FSC cost recovery mechanism.

Please see Annex 1 for a summary of the proposals in relation to the SIP and the Black Start and FSC compensation arrangements.

The **alternative modification P232** is identical in all respects to the original modification except that it removes the extra 60 business days allowed under the original modification for claimants to submit extra evidence in support of their claims.

It is also proposed that a new BSC Procedure¹⁰ (BSCP) be developed to accompany the implementation of P232. The new BSCP would contain guidance for market participants on claim submission and determination. The BSCP would also include specific guidance

⁹ "Bulk electricity" means electricity traded under contracts which may be performed by the notification of Energy Contract Volumes in accordance with Section P. See Section T of the BSC.

¹⁰ BSC Procedures set out procedures to be complied with in matters relating to the implementation of the BSC. They can, from time to time, be modified by the Panel in accordance with the BSC.

on the establishment of a Claims Committee – in effect suggested Terms of Reference. This BSCP would sit with the Panel so as to encourage regular review and familiarity.

BSC Panel¹¹ recommendation

The Final Modification Report (FMR) was considered by the BSC Panel at its meeting on 14th May 2009. The Panel unanimously agreed that modification proposal P232 and its alternative better facilitated applicable BSC objectives (b), (c) and (d).

Further, the Panel unanimously agreed that the alternative modification better facilitated applicable BSC objectives (c) and (d) when compared to the original modification. The Panel therefore recommended the implementation of the alternative modification. Please see the FMR for full details of their views.

The Authority's decision

The Authority has considered the issues raised by P232 and the FMR dated 20 May 2009. The Authority has considered and taken into account the responses to Elexon's¹² consultation which are attached to the FMR¹³. The Authority has concluded that:

1. Implementation of the alternative modification proposal will better facilitate the achievement of the relevant objectives of the BSC¹⁴; and
2. Directing that the alternative modification be made is consistent with the Authority's principal objective and statutory duties¹⁵.

Reasons for the Authority's decision

The Authority agrees with the view of the Panel that both the original and alternative modification proposals will better facilitate the achievement of the applicable BSC objectives. However, the Authority has concluded that the alternative modification would better facilitate the achievement of the applicable BSC objectives when compared to the original modification.

In coming to a view on whether P232 would better facilitate the applicable BSC objectives, we consider it necessary to assess the two key components of the modification - the issue of the single imbalance price and the compensation arrangements - separately. In respect of the SIP, we consider that it is particularly important to understand the intent of the SIP, what the SIP should ultimately reflect and how the changes proposed by P232 will impact on both these considerations.

Single imbalance price

For the duration of a Black Start period, generators can only operate in response to, and in accordance with, Emergency Instructions issued by NGET. This is because, for safety reasons, the NTS must undergo a phased resynchronisation led by NGET who, in these circumstances, will have command and control. This implies that neither individual players, nor the market, should be considered to be in a position of "imbalance".

¹¹ The BSC Panel is established and constituted pursuant to and in accordance with Section B of the BSC.

¹² The role and powers, functions and responsibilities of Elexon are set out in Section C of the BSC.

¹³ BSC modification proposals, modification reports and representations can be viewed on the Elexon website at www.elexon.com

¹⁴ As set out in Standard Condition C3(3) of NGET's Transmission Licence, see: http://epr.ofgem.gov.uk/document_fetch.php?documentid=4151

¹⁵ The Authority's statutory duties are wider than matters which the Panel must take into consideration and are detailed mainly in the Electricity Act 1989.

In this context, the SIP is not an imbalance price in the traditional sense and should not be considered equivalent, in form or effect, to emergency cash-out prices invoked in the event of a gas emergency where market mechanisms can remain in operation. Rather, the SIP is a price that generators receive for the energy they generate during a Black Start period. It is also a price that suppliers pay for the energy purchased during a Black Start period. This price, as set out in the BSC, is to be determined by the Panel as representative of the price of bulk electricity.

Having considered carefully the issues raised in responses to the consultation, we consider there are two key issues related to the SIP component of P232 that need to be addressed.

First, we understand that the modification group considered a number of alternative methodologies for the calculation of the SIP but concluded that no single methodology was likely to be correct¹⁶. However, in an effort to improve the transparency of the pricing mechanism, they considered that the 30-day average of SBP and SSP was likely to be a good proxy for the price of bulk electricity.

To be clear, we would have concerns if P232 proposed to *mandate* the use of a 30 day average of SBP and SSP to calculate SIP. This is because we do not believe that this methodology would necessarily be representative of the price of bulk electricity in every instance. For example, if a Black Start period were to occur in early November, the SIP would be calculated using a 30-day average of summer prices which may significantly underestimate the price of bulk electricity. The fact that the Panel will retain the flexibility to implement an alternative price mechanism where it is appropriate to do so, coupled with the fact that the SIP is subject to approval by the Authority, provides comfort that an unrepresentative SIP would not be implemented.

Second, it is our view that the benefits of transparency and clarity gained by including a potential mechanism for calculating SIP need to be weighed against the risk associated with setting out a methodology which, in some circumstances, may prove to be inappropriate and therefore not implemented. Market participants have to assess their risk and financial exposure to a range of events as part of normal commercial operations to try to avoid the risk of falling into financial difficulty. Providing a more transparent potential price setting mechanism will assist in such an assessment. This view is supported by a range of market participants (generators, suppliers, Elexon) involved throughout the development and consultation process, who clearly value having transparency of a SIP methodology.

On this basis, we consider that the benefits of a transparent potential price setting mechanism will outweigh the risks of setting out a potential pricing methodology which may, in some instances, be inappropriate and therefore not implemented.

Objective (b): "the efficient, economic and co-ordinated operation of the GB transmission system"

Respondents were generally of the view that by providing increased clarity with respect to SIP and compensation arrangements, market participants would have a better understanding of the post-event Black Start and FSC arrangements. This would help market participants understand their roles and responsibilities during such an event, thereby assisting in the economic, efficient and co-ordinated operation of the GB transmission system.

¹⁶ See the P232 Assessment Consultation for further details of the other potential SIP methodologies considered by the Issue Group.

For the reasons set out below, we consider that P232 will, on balance, promote the economic, efficient and coordinated operation of the GB transmission system. With regard to applicable objective (b), we do not believe that either the original or the alternative P232 better facilitates this applicable objective more than the other.

Single imbalance price

A more transparent potential price setting mechanism provides market participants with increased clarity with respect to how costs may be recovered. Such transparency is clearly valued by market participants, although such a methodology may not be appropriate in all cases. The ability to alter the methodology where it is inappropriate is an important factor in our decision to accept this modification.

Compensation Arrangements

Overall, respondents considered that the changes to the compensation arrangements would allow generators to have a better understanding of how their Avoidable Costs (Black Start) or Exceptional Costs (FSC event) could be recovered post-event, thereby encouraging compliance with NGET during the event and subsequently improving the efficiency of operations during a Black Start or FSC event.

We agree that by ensuring that the claims process is clearly defined ahead of any Black Start or FSC event, confusion during any such event should be reduced, allowing market participants to concentrate on their obligations to assist in the transition back to normal market operation. Further, post-event, market participants should be clear on how to submit any claims for Avoidable Costs or Exceptional Costs incurred, and within which timescales to claim. This should allow market participants, and subsequently NGET, to focus on their individual Black Start and FSC obligations, which will in turn facilitate the efficient, economic and coordinated operation of the GB transmission system.

Objective (c): "the promotion of 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"

Only two respondents to the P232 consultation considered objective (c) to be relevant. One respondent noted that, by clarifying the process by which parties are able to recover Avoidable or Exceptional Costs - costs which competitors may not have incurred - the changes proposed by P232 would likely further applicable objective (c).

For the reasons set out below, we consider that the alternative P232 will promote effective competition in the generation and supply, sale and purchase, of electricity, better than the original P232.

Single imbalance price

We consider that providing clarity around a potential SIP methodology should be beneficial to competition by providing a degree of transparency to the market as to how the Panel may determine the price of bulk electricity. With regard to a Black Start period, this may be particularly important for those generators who may not have incurred, or who have chosen not to claim for Avoidable Costs, such as smaller generators. It may also be particularly important for suppliers who are not eligible to claim for Avoidable Costs. These market participants will be more sensitive to the value of SIP given that this payment will not be absorbed within the amount awarded for Avoidable Costs.

To understand this further, the BSC states that the Black Start Compensation Amount is the difference between the Avoidable Costs determined by the Panel and the product of the SIP for any BM Unit Metered Volume. Therefore, where a generator claims for and is awarded an amount for Avoidable Costs, the value of SIP is in effect irrelevant.

This is not the case for those generators who do not claim for, or are not awarded, Avoidable Costs. These generators will only be paid SIP for any BM Unit Metered Volume. Similarly, suppliers will pay at the SIP for volume used. Therefore the value of SIP, in particular how it is determined by the Panel, is particularly important for these Parties.

Overall, we consider that improving the clarity around the Panel's potential determination of SIP will provide transparency to all market participants, in particular to smaller generators and intermittent generators. Whilst we consider this could reduce uncertainties facing different categories of generators and suppliers in relation to compensation payments, of itself it is likely to have little impact on competition particularly given that there are no market arrangements in operation during a Black Start period.

Compensation Arrangements

In respect of the proposed refinements to the compensation arrangements, we consider that improving the transparency and hence accessibility of the Black Start and FSC post-event processes and procedures will create a level playing field and reduce the scope for differing interpretations by market participants. In this respect, P232 will allow parties to make more informed decisions regarding financial matters post-event, thereby allowing market participants to concentrate on assisting in the orderly transition back into effective competition.

Original versus alternative modification P232

We consider that the alternative P232 is likely to better facilitate objective (c) than the original P232 as requiring the Panel to wait for an additional 60 days for a Party to submit evidence to accompany its claim could potentially cause delays to the overall claims determination process, and so potentially delay payment of claims, which may have an adverse impact on competition.

Objective (d): "the promotion of efficiency in the implementation and administration of the balancing and settlement arrangements"

Respondents generally agreed that in providing clarity on a potential SIP methodology and the claims application processes, P232 would promote efficiency in the implementation and administration of the BSC arrangements.

For the reasons set out below, we consider that alternative P232 will promote efficiency in the implementation and administration of the balancing and settlement arrangements, better than the original P232 solution.

Single imbalance price

We do not believe introducing the proposed potential SIP methodology into the BSC will significantly improve efficiency in the administration of the BSC as we believe relevant parties, namely the Panel, will still be required to undertake a detailed assessment of SIP once a Black Start period or FSC event has been declared. This is necessary in order to ensure the SIP is reflective of the price of bulk electricity in light of the circumstances at the time.

Further, in the instance that a Black Start period or FSC event does not occur swiftly and is preceded by a period of irregular market conditions, the determination of SIP may be particularly complex and potentially lead to an increase in administrative costs for both Elexon and Ofgem.

Compensation Arrangements

We consider that having the Black Start and FSC compensation arrangements clearly defined ahead of any such event should significantly enhance efficiency in the administration and implementation of the BSC. Clarity and transparency of the post-event arrangements should allow for market participants to focus on collating evidence and completing their applications within the required timescales. The Panel will also be better able to focus on establishing the Claims Committee and terms of reference, ready for the claims determination process to begin.

Original versus alternative modification P232

Two respondents in favour of the original modification considered that the extra 60 days for the submission of further evidence would provide a degree of certainty that that extra evidence would be considered by the Panel in every case.

However, we consider that any benefit gained from this time extension could, at least in part, be realised through existing arrangements which allow market participants to request, on an individual basis, a time extension from the Panel in order to collate evidence and submit their claims over and above the initial 20 day period (Black Start) or 60 day period (FSC event) within which claims must be submitted. Whilst we recognise that this route is accompanied by a risk that the Panel may deny a Party's request for an extension, we would expect the Panel to make a fair and reasonable judgement on a case by case basis.

Wider Statutory Duties

By improving the clarity and transparency of the SIP methodology and compensation arrangements associated with a Black Start or FSC event, we consider that P232 is likely to have a positive impact on security of supply. By improving arrangements in the BSC, market participants will be better equipped to undertake their individual roles and responsibilities in an efficient and effective way, thus limiting the impact and duration of a Black Start period or FSC event.

Other issues

The FSC states that Exceptional Costs are to be recovered from suppliers via a mechanism to be determined by Ofgem. Issue Group 33 recommended that if Ofgem were to choose a BSC route for that mechanism, basing it on the Funding Shares methodology¹⁷ would be appropriate. However, this is only a recommendation. We recognise that there is still a degree of uncertainty around how Ofgem will determine the cost recovery mechanism. We are therefore looking to progress work in this area in consultation with the industry where appropriate going forward.

Implementation

¹⁷ The Funding Shares methodology is a charging methodology designed to ensure that each BSC Party pays the correct shares of ELEXON's costs. The Funding Shares are based on the relative metered energy of each BSC Party. See Section D of the BSC.

We agree that implementation should be included in the next planned BSC Systems Release which falls at least 4 months from the date of this decision. In order to achieve the potential cost savings of implementing P232 together with P231 (in the instance that P231 is also approved by the Authority), we also agree that P231 and P232 should be implemented together.

Decision notice

In accordance with Standard Condition C3 of NGET's Transmission Licence, the Authority, hereby directs that alternative modification proposal BSC P232 "*Black Start and Fuel Security Compensation and Single Imbalance Price Derivation*" be made.

Ian Marlee

Director, Trading Arrangements

Signed on behalf of the Authority and authorised for that purpose.

Annex 1

Modification Proposal

Single Imbalance Price (SIP)

P232 seeks to introduce a potential SIP calculation methodology for all SPs which fall under a Black Start period or FSC event by expanding BSC Section T1.6 to state that:

- A SIP should be derived by taking the mean of the System Buy Price (SBP) and System Sell Price (SSP) for a given SP over a predefined number of days (no contract notifications or Bids or Offers would be included) in order to seek to determine a 'proxy' for the price of bulk electricity during the Black Start period or FSC event.
- The default approach would be to use the data over the previous 30 Settlement Days. However, an SP that was subject to a FSC event or instruction, a Black Start period or an Emergency Instruction would not be used and would be replaced with another appropriate historical SP.
- The Panel would determine an alternative pricing methodology if the Panel deemed it to be more appropriate as a 'proxy' for the bulk price of electricity during the Black Start period or FSC event.
- Once the methodology has been agreed for the entire Black Start period or FSC event, any review of the methodology which results in an adjustment, can be implemented going forward only (not retrospectively once it has first been agreed).
- For Clock Change days that occur during the Black Start period or Fuel Security Code event, Settlement Periods 3 and 4 shall be excluded for a short day and be used twice for a long day. For Clock Change days that occur during the historical period, the period shall be increased to 31 days with the Clock Change day being discounted.

Compensation Arrangements

1. Inclusion of operational costs

"Warm up" or "Hot Standby" costs incurred are allowed to be claimed as Avoidable Costs.

2. Claim application process

Claims applications can be made by BM Lead Parties in receipt of an Emergency Instruction (Black Start) or a direction from the Security of State (FSC event). An application for compensation can only be made in the case of Avoidable Costs (Black Start) or Exceptional Costs (FSC event) having been incurred. Submission of claims and evidence following the conclusion of a Black Start or FSC event must be done within the following timescales:

- Claimants are allowed 20 working days (or such period that the Panel may determine) to submit a claim from the conclusion of a Black Start period and 60 days (or such period that the Panel may determine) to submit a claim from the conclusion of an FSC event;
- Claimants wishing to request additional time to submit their claim must do so within the aforementioned timescales;
- An extra 60 business days are to be allowed for the claimant to submit further evidence (although this can alter the total amount which was set out in the initial application);

- The Panel or the Claims committee can ask for any extra evidence or information from the claimant (beyond the timescales set out above) as they see fit.

Interim payments shall be applied by and processed in the same manner as for total or final claims. In addition, the total amount received in claim applications and the total amount approved for payment is to be published.

3. Claims Committee procedures

The Panel will establish a Claims Committee to be chosen by them and which may consist of them, for the determination of all applications for compensation for Avoidable or Exceptional Costs. For the avoidance of doubt, Claims Committee decisions are Panel decisions. The P232 solution states that:

- The BSC Panel, or Claims Committee as delegated, will determine the process for the determination of each individual claim;
- There are no limits on the use of technical experts or groups of technical experts to sit on a Claims Committee (or sub-committee of the Claims Committee) to provide determinations of, or advice on, the claims.
- Meetings of the BSC Panel, or the Claims Committee as delegated, to consider claims will be confidential.
- Claims will have a “zero floor” meaning no negative determination can be made. Claims may be withdrawn by the Claimant at any Stage of the process up until the determination is made.

4. Cost Recovery Mechanism

If Ofgem require FSC costs to be recovered under the BSC, the P232 Modification Group recommends the use of the Funding Shares methodology.

Alternative Modification Proposal

The alternative modification is identical in all respects to the original modification except that it removes the extra 60 business days allowed under the original modification for claimants to submit extra evidence in support of its claim.