Modification Proposal P74 'Single Cost - reflective Cash - out Price' Consultation Questionnaire Responses
12 June 2002

Responses from P74 Assessment Consultation
Consultation issued 27 May 2002

Representations were received from the following parties:

No	Company	File Number	No. Parties Represented
1.	British Gas Trading	P74_ASS_001	3
2.	TXU Europe	P74_ASS_002	21
3.	Williams Energy Marketing & Trading Europe Ltd	P74_ASS_003	1
4.	Aquila Networks	P74_ASS_004	1
5.	Powergen	P74_ASS_005	3
6.	IMMINGHAM CHP LLP	P74_ASS_006	1
7.	Combined Heat and Power Association	P74_ASS_007	1
8.	London Electricity	P74_ASS_008	4
9.	Scottish and Southern	P74_ASS_009	4
10.	SEEBOARD Energy	P74_ASS_010	1
11.	Scottish Power	P74_ASS_011	4
12.	Damhead Creek Ltd	P74_ASS_012	2
13.	Campbell Carr Ltd	P74_ASS_013	5
14.	Edison Mission	P74_ASS_014	2
15.	Innogy Plc	P74_ASS_015	6
16.	RWE Trading Direct	P74_ASS_016	1
17.	AEP Energy Services	P74_ASS_017	2
18.	Eledor Limited	P74_ASS_018	1

P74_ASS_001 – British Gas Trading

Responding on Behalf of: **British Gas Trading Ltd, Centrica King's Lynn Ltd and Centrica Peterborough Ltd**

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	No. In our opinion P74 does not address the separation of system and energy balancing actions.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	No
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	P74 will decrease the value of instructed actions in relation to notified and un-notified actions by reducing the incentive on individual parties to balance their position. Instead parties will be incentivised to watch the overall position of the market and to take a position in the opposite direction to the market.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	No. P74 will weaken the incentives on parties to balance their own position and instead look to the overall direction of the market in order that they can be cashed out at the best price. This will effectively reward participants for being out of balance as they are seen as 'helping' the system, even if the SO has to take additional actions as a consequence and cannot therefore been seen as cost reflective.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	P74 should not change the level of perceived risk in the submission of Bids and Offers. We would anticipate that the same level of participation would be seen in the BM but there should be greater symmetry between the stacks i.e. fewer bids and more offers. It is conceivable that the offers could be at more expensive prices than currently seen. We do not have any comment to make on the impact on system

Q	Question	Response (Please provide rationale where possible)
		balancing but would be interested to see what the outcome of any modelling done in this area would be.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	Potentially there would be some reduction in part loading if this proposal did lead to a reduction in the imbalance price as there would be less incentive for parties to hold their own reserve as insurance against a plant trip. This could be seen as being less efficient for the market as a whole although possibly not for individual participants.
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	Yes if the contract price of a party is different from the imbalance price this might incentives a party to spill or go short into Gate Closure, preferring to take the cashout price instead of matching their FPN.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	Yes if Parties believe they could accurately predict the direction of the market. This increases the uncertainty faced by the SO and could ultimately increase the cost of balancing actions.
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	To some extent it might have an impact on the asymmetric risk faced by parties but as the fundamental physical characteristics of the participants remain it would appear unlikely to decrease significantly.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	Yes, as mentioned above we believe this modification will encourage participants to follow the market rather than to balance their own positions. We believe hunting type behaviour will result.
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	No, a market is made up of individual players and so the entity itself cannot be incentivised to balance. The incentives must be on those parties that make up the market.

Q	Question	Response (Please provide rationale where possible)
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Yes.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	We would anticipate that there would be some impact prices and liquidity in the forwards and spot markets and the level on Imbalance Prices but it is difficult to predict exactly what those interactions and changes will be.
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	It would be reasonable to assume that there would be some development of new risk management products and contracts if the demand in the market develops for them.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	This is very difficult to assess without detailed modelling and analysis. Also the impacts of imbalance prices are only one part of the impact. Consideration of RCRC, BSUoS and the SO incentive scheme is also vital to making a full assessment of the impact on participants' risk profiles.
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	It is too early to say. Some modelling of the impacts of the potential impacts of this modification proposal is required.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	It may be that an alternative proposal would be better than the original of P74 but until the modelling work is carried out to make a full assessment of P74 it is hard to judge. In our opinion the major issue is the distinction between system and energy balancing actions taken by the SO. Whilst we recognise that it may not be possible to make an absolute determination between the two it is essential that the best possible and most transparent solution is

Q	Question	Response (Please provide rationale where possible)
		found and agreed.
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	We are concerned that the implications for BSUoS and NGC's incentive scheme have not, and cannot, be discussed here. The impact of this modification has wider implications than simply the imbalance prices and these must be fully assessed.

P74_ASS_002 – TXU Europe

Responding on Behalf of (please list all BSC Parties): 21 TXU BSC Parties

Responding as which type of Party (see list in section 1.21): Generator and Supplier

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	Not sure that it is "better", but we do agree that it is a different way of handling the separation of system and energy balancing
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	This seems to be the nub of the issue – are we trying to produce a "cost reflective" Imbalance Price or are we designing a system which produces an incentive to balance. P74 implicitly assumes the former, whereas the current arrangements are based on the latter approach. As long as we are trying to "balance" we are sceptical that P74 will better achieve this than the current rules. If we say that P74 is aimed at promoting trading then it has some merit.
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to	We found section 1.6 of the consultation paper particularly difficult to understand. Having read it several times we arrived at the conclusion

Q	Question	Response (Please provide rationale where possible)
	impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	that it seemed to be arguing that there should be an Information Imbalance price rather than trying to get the same affect by changing the Energy Imbalance Price calculations.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	The baseline is not trying to target costs to those that "cause" them (i.e Generator trips) it merely allocates prices to Imbalance quantities on an ex-post basis – it is an incentive to balance rather than an attempt to allocate costs to those that cause them.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	This seems to be a neatly constructed theoretical argument – in practice we do not believe it will make any difference. If participants have a choice between a firm trade ahead of Gate Closure and a possibility of having a Bid or Offer accepted in the BM (even at a higher price / value), given the surplus capacity at present we believe they will take the firm trade.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	We do not think it would affect it in practice.
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	We do not believe that the current regime has resulted in Generators breaching the Grid Code obligations and consequently P74 will not make any difference.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	No (or if it does we do not understand why it should).
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	Perhaps we have got the wrong end of the stick, but if there is a single cash-out price which is (implicitly) assumed to be higher than SSP then

Q	Question	Response (Please provide rationale where possible)
		there is less incentive to balance than now and continue to go long as it will cost participants less than under the present rule ?
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	No
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	No (by definition the total is the sum of the individual participants)
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Possibly (at least in theory), but we have enough trouble forecasting our own demand without worrying about the net effect of everyone elses actions.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	Even if we knew the answer to this we probably would not tell you !
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	The inference of this is that with a single price, financial instruments around it (CfDs) could be written. Well, they could be but given that it would be derived from a (comparitavely) small quantity of accepted Offers or Bids it is not entirely obvious that people would be rushing to write such deals.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	One person's "appropriate" risk profile has the habit of being described by others as "cross-subsidy", we have been here before it was called RETA.
16.	Do you believe that Modification Proposal P74 better facilitates	This seems to come down to whether or not one believes that the

Q	Question	Response (Please provide rationale where possible)
	achievement of the Applicable BSC Objectives, if so, which one(s) and why?	reserve should be called by the SO and paid by everyone equally (in £/MWh) rather than participants choosing to over-contract. At least with the present rules participants have a choice and hence this can provide a commercial advantage depending how confident one feels about your own demand forecasts. At present we are inclined to say “No” to this question at presnt.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	Not at present.
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	

P74_ASS_03 – Williams Energy Marketing &Trading Europe Ltd

Responding on Behalf of : Williams Energy Marketing & Trading Europe Ltd, who are a Non Physical Trader

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	No.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	Yes. The single cash out price better values those participants who are helping the system into balance via their contractual imbalance e.g. if the system is long, those who are short are better rewarded than now.

Q	Question	Response (Please provide rationale where possible)
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	Notified actions, where beneficial to the balance of the system, will be relatively better rewarded than now. This should aid balancing of the system by providing better dynamic cashout incentives to participants. It is unclear how the value of instructed actions changes, although participants are able to set their perceived value via submitted Bid-Offers. It is possible that these may increase in value as they may only be required by NGC for refined balancing near real time. Mod P74 will inevitably require the Transmission Company to adapt its balancing strategy from its present one. This will require less early and less substantial commitment to balancing actions via forward trades and Ancillary Service contracts (inc. PGBTs) but may facilitate more innovative approaches by NGC. A likely consequence is less and cheaper intervention by NGC and hence lower overall energy balancing costs.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	Yes, in the sense that those contributing to the balancing of the system via notified actions are incentivised rather than penalised e.g. if the system is short only those participants who are short are penalised
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	By reducing/eliminating unfairly penal aspects of cashout prices, the risk-reward balance for generators should shift to the extent that the tendency would be for greater participation from a greater variety of participants, especially small and/or non-portfolio generators.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	Whilst the level of part loading is affected by a number of factors, the commercial incentives to part load would be reduced by Mod P74 and thus in general there ought to be less. This by definition would reflect that it is more efficient operationally and commercially for participants There should be greater liquidity in the traded market close to Gate Closure and better use of efficient plant in meeting demand. In terms of the overall economics of the system this is clearly more efficient.

Q	Question	Response (Please provide rationale where possible)
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	Yes. It reduces them as on balance there is less commercial incentive provided via a single cashout price to do so.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	(i) Yes, due to more dynamic cashout price signals and likely greater trading activity close to Gate Closure. (ii) Good, as it reflects a competitive, liquid, efficient, dynamic market working effectively right up to Gate Closure.
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	It reduces natural asymmetric risk to a more reasonable level (i.e. less lop-sided) and provides a natural index to enable complete risk management via hedging instruments.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	Yes. It will change the current stable incentive to over-contract. There will be a more dynamic relationship between participants FPNs and contract positions as they respond to cashout price signals i.e. if the system is long participants would wish to be short and vice versa.
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	Yes. It will provide better incentives for the system as whole to remain close to an equilibrium of zero imbalance, due to the dynamic incentives provided by the single cashout price.

Q	Question	Response (Please provide rationale where possible)
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Yes. There is potential for some volume volatility and price instability initially as participants adapt their behaviour. However, much like the start of NETA itself, as participants become more knowledgeable and sophisticated it should on the whole settle down to see limited volume volatility and perhaps occasional price instability. The key aspect is that the dynamic incentive is to converge to a stable balanced equilibrium.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	The presence of a number of significant vertically integrated players in the market makes this not certain but it should increase depth and liquidity in the traded markets as well as providing a clearer linkage between Energy Imbalance Prices and spot/forward market prices. The impact on Energy Imbalance Prices themselves is unanswerable given Mod P74 moves from a dual price system to a single price system.
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	Yes, due to the creation of a natural index, which is currently lacking under NETA. It will increase competition and efficiency in the forward markets and provide protection/stimulus for smaller and more risky forms of generation and demand
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	Risk profiles should be reduced across the board, particularly for the inherently more risky and small participants, such as unpredictable generators and small suppliers, but also to a lesser degree for large suppliers and vertically integrated players. NGC may face some initial uncertainty as the market adapts to the new cashout regime but their risk profile should also reduce slightly.
16.	Do you believe that Modification Proposal P74 better facilitates	Yes.

Q	Question	Response (Please provide rationale where possible)
	achievement of the Applicable BSC Objectives, if so, which one(s) and why?	"efficient, economic & coordinated operation by the Transmission Company of the Transmission System" by better incentivising participants "promoting effective competition in the generation and supply of electricity..." by improving trading liquidity and more efficient operation.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	Other than in an element of detail being considered by PIMG (i.e. replacement of TQEI by another variable such as QABO + BSAD, or NIV as defined in Mod P78), no.
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	Not at this stage.
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	Cannot identify any at this stage, although where possible, tangible analysis in the form of scenarios and simulations, even if they require simplifying assumptions and/or subjective refinement, are preferable to pure conjecture. Also, Mod P74 & P78 should be subjected to identical analysis/modelling to enable robust comparison, as inevitably both cannot be implemented and thus evaluating which better meets the BSC objectives is essential.

P74_ASS_004 – Aquila Networks

Please find that Aquila Networks response to P74/P78 Assessment Consultation is 'No Comment'.

regards

Rachael Gardener

Deregulation Control Group & Distribution Support Office

AQUILA NETWORKS

P74_ASS_005 - Powergen

Responding on Behalf of: **Powergen UK plc, Powergen Retail Limited, Cottam Development Centre Limited**

Responding as which type of Party (see list in section 1.21): Vertically Integrated Company

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	There will always be some bid/offer acceptances which are taken for both energy and system purposes. The issue is how many of these you allow into the energy price. P74 in removing the whole of the reverse stack will change the separation of balancing actions by removing some of these acceptances which were taken for both reasons.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	It could be argued that it leads to actions being more accurately valued in as much as it reflects the actions NGC has to take to deal with the net imbalance.
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	A bid offer acceptance to achieve market balance is of greater value than imbalances which may just happen to help the market to achieve balance. Bid/offer acceptances give NGC more control over balancing the market than relying on FPNs being delivered. Therefore, these should be valued more highly than accidental actions to balance. In terms of unnotified action (failure to meet FPN) this is a Grid Code issue, although we agree that a notified action (following FPN) is less problematic for NGC.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	If a more appropriate split of system and energy is achieved under this proposal then it will deliver a more appropriate targeting of the cost of energy balancing actions.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	It is possible that P74 will reduce the risk of imbalance and will result in the market going less long. If it does so, then we would expect more volume to be offered into the balancing mechanism and there to be a corresponding reduction in bids.

Q	Question	Response (Please provide rationale where possible)
		However, we expect P12 to have a significant effect on the market. Until we know how the market settles down after implementation, it is difficult to speculate what incremental change the modification would have over this.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	It may do although you may expect to see part loading to give flexibility to provide offers to the market. P12 is a significant factor. Until we see the market's reaction to its implementation it will be difficult to gauge the incremental effects of P74.
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	Grid Code appears to work at present and NGC has indicated that there is little self balancing after gate closure.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	P12 is the main factor in this. Whether or not this will increase the incentive to change PNs before gate closure will depend on the amount of trading which occurs up to the hour before.
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	There will always be some asymmetric risk as this is the reality of the market as the main risk generators is of tripping. However, it is to be expected that P74 would dampen the effects of this.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	As stated above under Q5, it is likely that P74 will result in participants going shorter into the market as the risk of doing so is reduced.
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	As above, we would expect parties to go shorter. As the market has tended to go long, this may bring the market closer to balance.

Q	Question	Response (Please provide rationale where possible)
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	It is possible that parties may speculatively try to anticipate the market and that it would lead to volume volatility. However, it is difficult to say with any great certainty.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	There is likely to be a depressing effect on liquidity in the forwards market as players reduce contract volume through general reduction in the length of their positions and potentially take higher volume imbalance risk (see response to Q14).
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	It will be possible for CFDs to be struck around the single imbalance price which will be more understandable by market participants. This may have the effect of reducing liquidity in the forwards/spot markets.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	Could reduce the costs of all participants to meet their risk profile (ie risk profiles themselves will not change). Should reduce the price risk to generators of trips and reduce cost to suppliers of meeting their particular risk profile.
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	As we mention below, this is difficult to answer with the uncertainty of how exactly P12 would affect the market. We believe that it is premature to implement such a change until there is sufficient experience of how the market operates under one hour gate closure.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	No.
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	As mentioned above in Q16, we do not believe that now is the right time to implement such a change. We need experience of P12 first.

Q	Question	Response (Please provide rationale where possible)
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	It is essential that the modelling takes into account the effects of P12. To model on the basis of 3½ hour gate closure would be of little use to the debate.

P74_ASS_006 - Immingham CHP LLP

Thank you for the opportunity for commenting on the P74/P78 Assessment Criteria. There is a hardening feeling in the market that the current imbalance price setting rules fail to deliver the intended outcomes. In particular, they load imbalance charges, including some associated with system balance, on out of balance parties. The methodology is therefore punitive and penal in effect.

As a general remark, we consider that both P74/P78 would better meet the applicable objectives, and the proposed assessment criteria and process seem to capture the key issues. The judgments we have made are preliminary based solely on the information provided by Elexon to date. There are some obvious omissions in the information available at this stage - the construction of the market price under P78 is an obvious example.

Either of the proposed changes, if implemented, would effect a fundamental change to the formulation of cashout prices and need to be very carefully thought through and modeled in detail. Because of the potentially wide ranging competitive effects, it is important that the proposals are worked up in considerably more detail and that modeling focuses on participant impacts by type of player as well as the position in the round.

Government has already highlighted in its 4 April 2002 response the need to establish a more cost reflective methodology for imbalance pricing, and one that does not unfairly disadvantage smaller participants and intermittent generators. It is clearly important that the modification group proceeds with due urgency. At the same time the changes proposed are fundamental to the NETA design and participant cash flows, and it is essential that the right choice is made. In this context it is not clear that the two proposals made by Electricity Direct and NGC are the only choices.

A word about the process. We would observe that PIMG, which is dealing with P74/78, is dominated by the larger incumbent players. This situation is not surprising as they have the depth of resource to tackle complex and challenging issues. We would urge you and Ofgem (to whom I am copying this letter) to open up the process and undertake focused workshops to enable the wider market get to grips with the issues.

Immingham CHP LLP

George Armistead, Director

Q	*Question*	**Response (Please provide rationale where possible)**
1	In your opinion, does Modification Proposal P74/P78 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	In the current arrangements, despite changes such as P18A, the long market leads to a very small number of Acceptances setting SBP. The impact of any action for systems reasons therefore has a disproportionate effect on SBP. Neither P74 nor P78 directly address the split between system balancing and energy balancing actions but, by leading to a more balanced market, system balancing actions on the buy side could be "diluted" by energy actions, lessening their impact. The resulting price is less likely to be extreme and will better reflect the price at which NGC is a net buyer of energy. P78 deems all actions in the opposite direction to be for systems reasons and it will strip them away from the price mechanism. It also strips equivalent volumes from the main price setting a lower price. The resultant main price should be a better reflection of the cost of energy needed for pure energy balancing reasons. The reverse price used in P78 is an approximate spot market price and this is a significantly better proxy for the value of reverse actions than is the case at present.
2	In your opinion, is Modification Proposal P74/P78 valuing actions more correctly. If so, why and if not, why not? (Section 1.5)	P74 values actions in the direction of system balance in the same way as at present. The change is in the valuation of the reverse price, and there is no direct relationship between reverse actions and the single price. P78 potentially better reflects the value of energy actions in the main price than does P74. The market price used for the reverse price is definitely more cost-reflective than the current SBP/SSP.
3	In your opinion, how does Modification Proposal P74/P78 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed actio	The reward for notified actions will be unaffected, and will still depend on BOAs, but the relative reward of unnotified actions should increase. NGC expresses the opinion that an instructed action (through a BM Acceptance) is worth more to it than an unnotified delivery or offtake that is in the direction of system balance and do not see why P74 should thereby reward such actions better than acceptances (by definition some BM acceptances must be at a less favourable price than the price proposed in P74). However, there is still a difference in the value under P74/P78. In a BM acceptance, the price is one that is acceptable to the bidder or offerer, whereas in unnotified spill/shortfall the price will be uncertain, and the participant is a price taker.

Q	*Question*	**Response (Please provide rationale where possible)**
		P78 assumes that the value of an action that helps the system accidentally is worth no more than the market price. It is certainly a better valuation than the current arrangement, which punishes such "accidental" help regardless.
4	In your opinion, does Modification Proposal P74/P78 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	P74 targets the cost of energy imbalance on those causing it and gives the benefit to those who help the system. The current system punishes regardless and certainly mis-targets the costs on positions that can help the system. P78 targets the costs of net imbalance on those who are out of balance in the same direction as the system. It values imbalances that help the system better than the present mechanism but does not offer the full reward for that help.
5	In your opinion, how does Modification Proposal P74/P78 change the perceived risk of Bid-Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you belie it would affect system balancing? (Section 1.7)	Assuming there are less strong incentives to over contract under both P74 and P78, participants may see more opportunities for offering marginal supply into the BM, and they may be less inclined to hold plant in reserve to self balance. The impact of fewer balancing actions to back off excess generation also needs to be taken into account, and again should increase options available to the SO through the BM.
6	In your opinion, how do you believe Modification Proposal P74/P78 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the syste as a whole? (Section 1.8)	Both P74 and P78 should reduce part-loading for the following reasons: • in a more balanced market, fewer bids would be taken, reducing the possible commercial upside of part loading on pulled back plant; • the cost of generator trip would be reduced and so self-reserve would be less necessary; and • a more balanced market increases the probability of an offer being accepted.
7	In your opinion, does Modification Proposal P74/P78 change the incentives to deviate from FPN over the current baseline. If so, how and why? (Section 1.9)	No. Arguably there are weaker incentives (owing to lower penalties) from adhering to contract notifications but there is no reason why FPNs should be less reliable, all other things being equal.

Q	*Question*	**Response (Please provide rationale where possible)**
8	In your opinion (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74/P78 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	We do not believe either would have a detrimental effect, not least because NGC is likely to continue to rely on its own demand forecasts. The impacts are likely to be inconsequential compared to changes arising from P12. If there is gaming of FPNs, this should be dealt with through regulatory action.
9	In your opinion, to what extent will Modification Proposal P74/P78 address the issue of asymmetr risk? (Section 1.10)	Both will mitigate risks of exposure to SBP assuming the system remains ordinarily net long.
10	In your opinion, do you believe that Modification Proposal P74/P78 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure. If so, how and why? (Sections 1.12 and 1.13)	There will remain incentives on all parties to at least balance under both proposals. If it is assumed that P78 will give rise to a wider spread in the prices than P74, then the incentives avoid negative imbalance (ie, be short) should be stronger than under P74.
11	In your opinion, do you believe that Modification Proposal P74/P78 will change the incentives for parties as a whole (i.e. in total, even if not balan on an individual basis) to balance the market as whole before Gate Closure. If so, how and why? (Section 1.11)	No. As above.
12	In your opinion, does Modification Proposal P74/P78 lead parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Parties will always seek to anticipate the direction of the market. As we have noted under both P74/P78, there will continue to be incentives to avoid being short.
13	What effect do you think Modification Proposal P74/P78 will have on liquidity and prices in the forwards and spot markets, the interrelation of	P74 should increase much needed liquidity in the spot markets because it reduces the impact of notification risk which therefore changes the costs of buying out of imbalance. This change should mean it will have less effect on forward prices, though fewer volumes overall should be

Q	*Question*	**Response (Please provide rationale where possible)**
	forwards and spot markets with Energy Imbalanc Prices and also the level of Energy Imbalance Prices themselves. (Sections 1.14, 1.15 and 1.1(	contracted over whatever timeframes. P78 will have similar effects other than on liquidity in the spot market, which could be muted by the remaining dual cash-out price effect on notification risk.
14	Do you believe that the implementation of Modification Proposal P74/P78 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	We would expect liquidity to increase under both proposals, with a consequential beneficial impact on risk management products.
15	In your opinion, what would be the impact on the risk profile of different categories of party (as listed in Section 1.21) from the implementation of Modification Proposal P74/P78 (Section 1.21)	It is premature to say in advance of more detailed analysis and modelling. However, based on a preliminary assessment, we have concerns about the ability of larger players to influence market prices. This does not mean that the changes should not be pursued , but simply that there will need to be transparency and appropriate regulatory action in the event of abuse.
16	Do you believe that Modification Proposal P74/P78 better facilitates achievement of the Applicable BSC Objectives. If so, which one(s) and why?	P74 better facilitates the Applicable BSC Objectives: • It is more cost-reflective in that it reduces panel charges arising from balancing energy. It also targets costs on those causing the imbalance rather than penalising parties who are helping the system. It therefore facilitates competition; and • It will lead to a more balanced system, reducing NGCs need to take balancing actions, which is more economic and efficient. P78 also better facilitates the Applicable BSC Objectives: • It prevents system balancing actions from polluting the energy imbalance price, making that price more cost-reflective and its sets the reverse price as less penal, which is more cost-reflective. It therefore facilitates competition; and • It reduces the incentive to over contract and can lead to more economic and efficient

Q	*Question*	**Response (Please provide rationale where possible)**
		operation of the balancing mechanism.
17	Do you believe that an alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74/P78. If so, what is it? (Section 1.23)	Not at the moment.
18	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74/P78.	The BSC applicable objectives do not take into account wider government objectives. We would refer the group to the government's draft CHP strategy issued in May.
19	Do you believe that further analysis/modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	Yes. The modelling needs to be much more thorough. It should explicitly consider the effect on intermittent generators and CHP participants.

P74_ASS_007 – Combined Heat and Power Association

These responses cover both P74 and P78 together because the effects are very similar in many instances.

Q	**Question**	**Response (Please provide rationale where possible)**
1.	In your opinion, does Modification Proposal P74/P78 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	In the current arrangements, despite changes to definition (such as P18A), the long market leads to a very small number of Acceptances setting SBP. The impact of any action for systems reasons therefore has a disproportionate effect on SBP. P74 does not directly address the split between system balancing and energy balancing actions but, by leading to a more balanced market – system balancing actions on the buy side will be "diluted" by energy actions, lessening their impact without a significant adverse impact on SSP likely. The resulting price is less likely to be extreme and will better reflect the price at which NGC is a net buyer of energy than is the case at present. P78 deems all actions in the opposite direction to be for systems reasons and so it will strip them away from the price mechanism. It also strips equivalent volumes from the main price setting a lower price. It is impossible to be certain that actions for energy reasons have not been stripped away as well but it

Q	Question	Response (Please provide rationale where possible)
		seems likely that the resultant main price will be a better reflection of the cost of energy needed for pure energy balancing reasons. The reverse price used in P78 is an approximate spot market price and this is a significantly better reflection of the value of reverse actions than is the case at present and will certainly exclude systems actions although it is less certain that the price is a proper reflection of energy cost to the system.
2.	In your opinion, is Modification Proposal P74/P78 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	P74 values actions in the direction of system balance in the same way as at present. The change is in the valuation of the reverse price. NGC balances the system based on the difference between generator FPNs and their own forecast of demand (with no reference to contract position which they do not know until up to 14 months later). The deviations from FPN are caused by generators tripping (or being late) and due to consumers in aggregate deviating from the NGC forecast. Suppliers' contract positions relative to their individual forecast of their own customers' demand (e.g. over-contracting as at present) will not alter the actions taken by NGC because the deviations of customer offtake relative to the NGC forecast will be the same. Therefore the value of actions taken by NGC will be the same regardless of any supplier's contract position and the single price proposed in P74 reflects this. P78 potentially better reflects the value of energy actions in the main price than does P74 but there seems a less soundly based case for the valuation of the reverse price because it is still applied to contract positions which NGC knows nothing of at the time of the action taken. However, the market price used for the reverse price is definitely more cost-reflective than the current SBP/SSP.
3.	In your opinion, how does Modification Proposal P74/P78 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	NGC expresses the opinion that an instructed action (through a BM Acceptance) is worth more than an unnotified delivery or offtake that is in the direction of system balance, and do not see why P74 should thereby reward such actions better than acceptances (by definition some BM acceptances must be at a less favourable price than the price proposed in P74). However, this mistakes the value of such spill/shortfall because, in a BM acceptance, the price is one that is acceptable to the bidder or offerer, whereas in unnotified spill/shortfall the risk is that the price will be unfavourable and is as likely to be a loss or a gain. This is interpreted by NGC as a reward for gambling when going against the direction of the system but it is really simply paying the value of your position to the system (i.e. it is cost-reflective) bearing in mind that there will be very few parties who will take a physical position in this way intentionally rather than due to errors in their forecasts of their own metered position. P78 asserts that the value of an action that helps the system accidentally is worth no more than the

Q	Question	Response (Please provide rationale where possible)
		market price but offers no justification for this view. It is certainly a better valuation than the current arrangement, which punishes such "accidental" help regardless but this is still not a proper reflection of the value of the offsetting volumes, which allow NGC to take less balancing actions than they would otherwise have taken.
4.	In your opinion, does Modification Proposal P74/P78 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	P74 targets the cost of energy imbalance on those causing it and gives the benefit to those who help the system whereas the current system punishes regardless and certainly mis-targets the costs on positions that help the system. P78 targets the costs of net imbalance on those who are out of balance in the same direction as the system. It values contractual imbalances that help the system better than the present mechanism but does not offer the full reward for that help.
5.	In your opinion, how does Modification Proposal P74/P78 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	This is a complex area. Currently generators are operating at part load excessively in order to provide capacity for self-reserve. Generators are offering self-reserve volumes as BM offers at present (it may, however, be worth examining the extent to which they are setting MEL to FPN to prevent such offers being accepted). If generators reduce the volume of self-reserve by selling more gensets fully and not operating on others then the volumes available as BM offers could reduce. This would be more efficient for the system overall although the cost borne by NGC for carrying reserve would increase. The phrasing of the actual question is about the risks of bid/offer submission. P74 reduces the risk of bid/offer submission because if an acceptance is made that cannot be delivered (e.g. due to a generator trip) then the cost of that failure is not necessarily changed. Given that self-reserve is offered to NGC as offers at present, the main expected change will be in the price at which such offers are made which should be lower if the cost of failure is lower. This would not otherwise affect system balancing. P78 has a similar effect to P74 but, by reducing the potential upside to cash-out in the event of failure to deliver, it can be expected to have a lesser effect on bid/offer pricing than P74. P78, by maintaining a buy-sell spread may have a lower impact on the failure risk than P74 but would still be much better than at present.

Q	Question	Response (Please provide rationale where possible)
6.	In your opinion, how do you believe Modification Proposal P74/P78 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	P74 would reduce part-loading to an extent for the following reasons: • In a more balanced market, fewer bids would be taken, reducing part loading on pulled back plant; • The cost of generator trip would be reduced and so self-reserve would be less necessary – this suggests fewer plant operating at fuller load. However, on the reverse side: • A more balanced market increases the probability of an offer being accepted, which increases the reward for part-loading (to an extent); • With fewer plant scheduled by participants onto the bars, NGC may need to schedule more part loaded plant via reserve contracts. The effect of P78 is similar but to a lesser extent.
7.	In your opinion, does Modification Proposal P74/P78 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	Currently, there are two incentives on generators to deviate from FPN: • To replace a failed plant from the portfolio when SBP is expected to be high (which is easily done from part-loaded plant but which will be used rarely); • Generating to the upper end of the expected level of output in order to avoid a marginal shortfall at SBP – this gives a lot of very small volumes of persistent spill. P74 will reduce the first of these in some circumstances (while recognising that if a large set fails completely it could tip the system short anyway), and will eliminate the bias in the second as the cost of going short will be reduced. Generators may still seek to over-deliver against FPN when they see the network going short but they risk this breach of the grid code only netting SSP anyway (especially if others do the same) and they would almost certainly be better off contracting with NGC (as PGBTs or Offers) given that they would only be doing this spill when they have good reason to believe that NGC will need the energy. In any case such opportunities will be vanishingly rare under a 1-hour gate closure. P78 will not offer the same potential incentives to deviate from FPN and will reduce the existing incentives.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74/P78 increase the incentive on parties to change Physical	P12 is the latest Modification approved that explicitly facilitates contracting close to gate closure. Given that IPNs will usually represent the contracted position at the time rather than an expectation of striking contracts, it can be expected that changes up to FPN will be more frequent. P74 will only increase opportunities for late changes to FPN to the extent that there is extra information indicating a specific direction to system balance. Opportunities for price-seeking by

Q	Question	Response (Please provide rationale where possible)
	Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	changing a physical position will only arise to the extent that there is extra information about system balance available. Given that IPNs will be less useful as a predictor of system balance due to these same late changes from other parties, excessive speculation on the physical position of the market will be muted. It should be noted that parties may still speculate on the direction of the market in the current situation in that a rising price in the spot market suggesting that the market is short will raise the expected cost of a supplier going short and so they might choose to go even longer. Some "opportunities" will still arise from P78 because an expectation of a more balanced market will change parties' perceptions of optimal position (if the spot price is rising, it suggests the system might be short, which increases the risk-adjusted value of spill so that other parties might seek to go longer). P74 does allow notifications much closer to gate closure because the risk of notification failure can be managed financially under a single price. Both P74 and P78 therefore may make system management more difficult for NGC but the big change in difficulty arose from P12 and the difficulty was thought to be outweighed by the improvements due to parties being able to balance more closely.
9.	In your opinion, to what extent will Modification Proposal P74/P78 address the issue of asymmetric risk? (Section 1.10)	There is confusion as to what is meant by asymmetric risk. Asymmetry in price risk arises primarily where the spot price (the price of buying out of the price risk) is closer to a risk-weighted expected SSP than to a risk-weighted expected SBP. The relative volatility in SBP simply raises its risk-weighted expected price. P74 will raise the opportunity cost of spilling because, as generators have the opportunity to spill at a potentially higher price, they will not offer power to suppliers at a prompt price that does not reflect this opportunity. This raises the spot price and makes the risks more symmetrical. P74 therefore addresses the causes of the observed (i.e. ex post) asymmetry in prices. P74 does not directly address the more fundamental asymmetry in volatility in SBP relative to SSP for which there are good economic reasons although some of the volatility caused by pollution of the energy price by systems actions will be diluted because these actions will only affect the "main" price, which will include much more energy in its calculation. P78 seeks to more directly address price pollution from systems actions by extensive tagging out and as such will produce a less volatile main price although the underlying relative volatility inherent in short-notice incrementing will remain. In other respects the impact of P78 will be similar to P74 but more muted.

Q	Question	Response (Please provide rationale where possible)
10.	In your opinion, do you believe that Modification Proposal P74/P78 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	As explained in *9* above, P74 will raise the cost of excessive spill, which will thereby reduce, leading to a more balanced market. Similarly, as the cost of going short remains a high price (although relatively reduced), the incentive on all parties with uncertainty about their ex post physical position remains to balance. P78 has similar incentives but is more muted because the up side of getting it wrong are less (leading to a probably longer market than P74).
11.	In your opinion, do you believe that Modification Proposal P74/P78 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	P74 will lead to a more balanced market because balancing decisions will be informed by expected market balance – which is not the case at present. Also, if suppliers seek to be closer to balance individually (by spilling less), the market will be closer to balance. P78 will be similar but the effects are more muted and so the market is likely to be longer than under P74 but less long than at present.
12.	In your opinion, does Modification Proposal P74/P78 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Parties will only price-seek under P74 to the extent that they have good information about the direction of market imbalance. The fear of hunting has to be vastly exaggerated. Generators have a slightly better view of market balance to the extent that they know if their own plant is at risk of failure. However, they will be price-takers (the “hunted”) in such a scenario – not hunters. Such generators will seek to contract out of their own adverse balance. Other generators will usually be better off by offering their flexibility to NGC rather than speculating. P78 is similar in effect – it won’t lead to significant hunting of the market direction. There is not enough information out there to make it worthwhile.
13.	What effect do you think Modification Proposal P74/P78 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	P74 will vastly increase liquidity in the spot markets because it eliminates notification risk (a failure to notify can be covered financially in a single-price environment). P74 will impact on spot prices because it changes the value of buying out of imbalance. It will have less effect on forward prices. P78 will have similar effects other than on liquidity in the spot market, which will be muted by the remaining dual cash-out price effect on notification risk. It has been asserted that, under P74, parties will not contract and simply take a “Pool” price. This misunderstands the nature of the Pool in which generators were guaranteed revenue based on the

Q	Question	Response (Please provide rationale where possible)
		day-ahead price. Without a contract, generators can only be guaranteed a low ex post spill price and so will not generator without a contract (either notified before gate closure or else on a CfD). If generators don't generate then the market will be short so suppliers have an incentive to contract to avoid SBP. The incentive to contract remains and, given that the market was about 90% contracted under the Pool, there is no reason to believe that contracting will be any less than at present (except that the market will be contracted to balance rather than being over-contracted).
14.	Do you believe that the implementation of Modification Proposal P74/P78 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	Under a single cash-out price as in P74, volume risk management can be offered across the system rather than just behind the meter. Much of this will probably be via CfDs but traders will offer other products as well because they would be able to take a physical position if the price risk was not always negative. This is fundamentally efficient and normal because risk is moving to the parties most willing to bear it. P78 does not offer the same opportunities because, although downside risk is reduced, there is no upside risk available for the risk manager.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74/P78? (Section 1.21)	• Small suppliers will benefit from both Mods but especially form P74 because the artificial penalty applied to small portfolios (with a statistically greater imbalance risk) is removed (by P74) or reduced (by P78). • Larger suppliers benefit like smaller ones in not needing to over-contract – and they can buy better risk management across the system. However, they benefit less than small suppliers because their artificial relative advantage in portfolio size is removed. • Licence Exempt Generators (LEGs) are significant winners from both Mods but especially from P74. This is because the value of spill – the price that many embedded generators have been offered in contracts – has increased to incorporate a possibility of earning either from a market price (P78) or from SBP (P74). Suppliers will therefore be able to offer prices to embedded generators at a price reflecting this. In addition, in a more balanced market, NGC will provide more of the reserve (rather than suppliers doing so via over-contracting) and so embedded benefits will improve. For LEGs in CVA, the cost of consolidation will be removed by P74 and reduced by P78. • Unpredictable generators will benefit by being able to contract to their average expected output rather than to the minimum because shortfalls will not always be punished at SBP. They will therefore spill less.

Q	Question	Response (Please provide rationale where possible)
		• Non-portfolio generators face lower trip risk and so will earn at a higher rate. To the extent that the average spot price increases, they may be able to strike better contracts, but if the forward market does not move then this will not be the case. • Portfolio generators will lose market power and so will be slightly worse off, but to the extent that their effective trip insurance cost will be lower, they will benefit. • Vertically integrated parties will similarly lose market power but will still operate in a more efficient, lower cost, market. • Non-physical traders will have the opportunity to take on a degree of physical risk under P74 (but not under P78) and so will benefit from being able to offer a fuller range of risk management products. • The transmission company will not be directly financially affected by either of these proposals because it passes through costs anyway. Longer term it stands to lose out to the extent that the growth of embedded generation will no longer be stunted by the current penal pricing system. The Consultation document fails to mention the following relevant parties: • Flexible plant will benefit from a balanced market where NGC contracts for rapid reserve when needed rather than only varying the extent to which excessive plant is pulled back. • Consolidators will lose out under P74 – they will be redundant. • Exchanges will benefit from improved liquidity under P74 due to reduced notification risk. • Consumers will benefit from a more efficient market whereby suppliers are not over-contracting and generators are not self-reserving. The spot market may move up but, to the extent that forward prices are driven by Europe through arbitrage across both the gas and electricity interconnectors, it is far from certain that consumer contract prices will move to any great degree. Longer term, consumers can only benefit from a rational market in which the risk of a "California" scenario – where uneconomic generating plant is excessively mothballed because market returns are so depressed so that the market is rapidly tipped into shortage – is reduced.
16.	Do you believe that Modification Proposal P74/P78 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	P74 clearly better facilitates the Applicable BSC Objectives: • It is more cost-reflective in that it correctly values balancing energy, which is independent of contract positions, which NGC knows nothing about at the time of the balancing action. It also targets those costs on those causing the imbalance rather than penalising parties who are helping the system (by contracting to a position that does not force excess balancing actions). It therefore

Q	Question	Response (Please provide rationale where possible)
		facilitates competition. • It will lead to a more balanced system, reducing NGC's need to take balancing actions, which is more economic and efficient. P78 also better facilitates the Applicable BSC Objectives: • It prevents more system balancing actions from polluting the energy imbalance price, making that price more cost-reflective and it sets the reverse price as less penal, which is more cost-reflective. It therefore facilitates competition. • It reduces the incentive to spill excessively leading to more economic and efficient operation of the balancing mechanism.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74/P78, if so, what is it? (Section 1.23)	N/a
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74/P78.	The Consultation Document fails to address the specific problems faced by embedded generation in the current mechanism. As noted above, the only way for such players to participate in the current process is to: • Either go into CVA and be consolidated, which is an administratively expensive process relative to the scale of generation and is not currently offering any attractive prices anyway; • Or to sell to suppliers in SVA and be offered the derisory spill price. The reason that suppliers are offering embedded generation such low prices is not related to inherent variability of output (which Ofgem has already demonstrated is generally not the case) but because the product that an embedded generator must offer to suppliers is different to the one offered by CVA generation. This is because CVA generation delivers firm energy through contracts with the generator able to manage its own meter risk, whereas an embedded generator must sell that meter risk to the supplier and has no opportunity to manage it. Another factor not covered has also been raised above. Because the current mechanism is not rewarding upward flexibility properly (because the spill market means that excessive downward flexibility is being taken), consumers are being forced to overpay for self-reserve rather than for the product that NGC would otherwise contract for. This depresses BSUoS, which has an adverse impact

Q	Question	Response (Please provide rationale where possible)
		on embedded benefits.
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	N/a

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P74_ASS_008 – London Electricity Group

Responding on Behalf of **LEG plc (representing London Electricity plc, Sweb Ltd, Jade Power Generation Ltd, and Sutton Bridge Power Ltd).**

Responding as which type of Party (see list in section 1.21): **Vertically integrated player**

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	P74 does not give a better separation of balancing actions used in setting Energy Imbalance Prices as the method for calculating SSP and SBP remains unchanged from present. The application of the price associated with the larger stack to imbalances in the opposite direction to the market means that these imbalances are subject to cashout prices that include energy balancing actions which are unrelated to the correction of these imbalances. For example if the market is short and a party is long they are paid SBP.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	No. Bid-Offer Acceptance actions remain unchanged. Imbalances in the opposite direction to the market imbalance are valued at a price that is unrelated to the actions taken to correct these imbalances (see also answer to question 1).
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to	The reward for "instructed" actions is unchanged – the action itself is still payable at the bid or offer price (except in the event of non-delivery),

Q	Question	Response (Please provide rationale where possible)
	impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	and the acceptance is taken account of in the calculation of energy imbalance cashout payments both with current cashout calculations and with P74, and so (except in the event of non-delivery) the successful deliverer of notified actions is neutral to P74. As stated in the answer to questions 1 and 2 the reward for notified actions for imbalances in the opposite direction to the market is unrelated to the cost of these actions in P74. We note that the existing, very strong, licence requirement, via the Grid Code, to submit accurate FPNs will remain in place and believe that this will mean that the Transmission Company's balancing of the system would remain similar to the current system if P74 was implemented. See also replies to questions 7 and 8.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	No. For example, parties who are long when the system is long and are creating the market imbalance are paid SSP under both P74 and the present arrangements. Discrimination issues in the "main" price as between energy and system balancing actions will remain.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	P74 could only encourage greater balancing mechanism participation if participants whose ability to deliver bids/offers introduced additional cashout uncertainty, believed that the system remained long and that they would only be exposed to SSP. However the proposer of P74 suggests that the system will be more in balance. If this were true, under P74 parties in general, being less "long", would be exposed to SBP, calculated as at present, more frequently. We therefore do not believe that participation would change significantly from present, and could even reduce.

Q	Question	Response (Please provide rationale where possible)
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	The prime driver for part-loading is not energy imbalance prices. It is clear that power exchanges cannot facilitate trading within 30 minutes of gate closure. We cannot forsee a systematic change in part-loading as a response to P74.
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	No. Further, we note that the existing, very strong, licence requirement, via the Grid Code, to submit accurate FPNs, will remain in place.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	We do not believe that P74 will increase the incentive for parties to change Physical Notifications shortly before Gate Closure.
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	Asymmetry will be removed from the pair of cashout prices calculated for any given period, but the underlying asymmetry will remain. We therefore believe that suppliers in particular will still be incentivised to take long positions and thereby avoid the risk of paying SBP if the market was short and they were short.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	No (see answer to 9.)
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	No (see answer to 9.)

Q	Question	Response (Please provide rationale where possible)
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	No as the difference between a long and short market could be as simple as one generator set tripping. In any case if parties thought the market was going to be short they would go long to get paid SBP thereby perhaps by their own action, driving the market long.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	SSP will always be driven by marginal costs and therefore P74 should have no effect on the price in other markets. We do not believe that P74 will have a major effect on liquidity or prices in the forwards or spot markets.
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	The introduction of a single price albeit 'flipping' from SSP to SBP could allow the development of hedging products based on the common exposure to a price to alll out of balance parties in a given half hour ; however it is not clear how a party could determine the quantity to hedge when hedging against exposure to cashout penalties; so in practice, no.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	Not possible to say - see also our response to question 19.
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	No as prices for imbalances in the opposite direction to the market will not be cost-reflective.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	No.
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	-
19.	Do you believe that further analysis / modelling is required over that	We particularly welcome the plan to obtain modelling which will assist in

Q	Question	Response (Please provide rationale where possible)
	currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	an assessment of the likely incentives to balance and to contract.

P74_ASS_009 – Scottish and Southern

Responding on Behalf of: **Scottish & Southern Energy Plc, Southern Electric Ltd, Keadby Generation Ltd and SSE Energy Supply Ltd.**

Responding as which type of Party (see list in section 1.21): **Vertically Integrated Player**

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P78 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	P78 - Yes – BRL is set to zero and therefore a much greater volume of bids and offers will be tagged as system related. Only the Net Imbalance energy for the period will set cashout prices. NGC costs derived from the difference between the cost of offers and the cost of bids for equal and opposite volumes of system balancing will be recovered through smear charges rather than imbalance charges. P74 does not include any change to the imbalance price calculation for net imbalance energy and therefore does not improve the separation of system and energy balancing costs. The relatively attractive “reverse” price simply transfers profits to participants who “happen” to have the right position.
2.	In your opinion, is Modification Proposal P78 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	See above
3.	In your opinion, how does Modification Proposal P78 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company’s balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	P78 doesn’t encourage position taking in the opposite sense to the system as P74 could (See 7). Therefore P78 is more likely to result in participants following their submitted PNs and it should reduce the volume of actions required by NGC.

Q	Question	Response (Please provide rationale where possible)
4.	In your opinion, does Modification Proposal P78 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	Both P74 and P78 target the net cost of imbalances on those who caused the imbalance. However, P78 holds participant with a helpful position neutral whereas P74 allows these participants to profit fortuitously at the expense of the other players.
5.	In your opinion, how does Modification Proposal P78 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	P78 should reduce the risk involved in being short and therefore encourage participation in the balancing mechanism. It should also result in participants holding a less long position at gate closure.
6.	In your opinion, how do you believe Modification Proposal P78 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	As above, the risks involved in being short should be reduced leading to a reduction in the amount of reserve held by participants and an increase in overall system efficiency.
7.	In your opinion, does Modification Proposal P78 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	P78 - No – the final imbalance prices will not be known until some time after the event. It would be extremely difficult to predict the “market price” and therefore there is little or no incentive to deviate from the FPN. P74 – With P74, participants will know that if NGC have accepted a large volume of offers then the cashout price is likely to be high. Likewise if NGC accept a large volume of bids the cashout price is likely to be low. This could give an incentive to deviate from submitted FPNs.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P78 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	Participants should be free to change PNs up to gate closure irrespective of the cashout regime. If changing PNs close to gate closure is a problem it should be addressed by modification to the gate closure period not the cashout regime. However, we believe that P74 is likely to increase the extent to which notifications are changed immediately prior to gate closure.
9.	In your opinion, to what extent will Modification Proposal P78 address	P78 should significantly reduce the asymmetric nature of the present cashout regime but will probably retain a small incentive to hold length

Q	Question	Response (Please provide rationale where possible)
	the issue of asymmetric risk? (Section 1.10)	as the weighted average cashout price for a short position is likely to be slightly more penal than the weighted average long price.
10.	In your opinion, do you believe that Modification Proposal P78 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	See 5,6 & 9 P78 should reduce the incentive to hold length and therefore result in an overall reduction in account imbalances which tend under the current system to be long.
11.	In your opinion, do you believe that Modification Proposal P78 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	P78 should significantly improve the overall system balance. Under the current regime, all participants tend to adopt a similar position at gate closure. Ie Long. This sums to a considerable overall system imbalance. P78 should reduce this incentive on individuals, introducing an element of diversity whereby some participants may adopt a short position at gate closure. The overall system imbalance should therefore be greatly reduced.
12.	In your opinion, does Modification Proposal P78 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	P78 – This is unlikely with P78 as the “market price” will not be known for some time after the event. P74 – With P74 it would be possible for participants to anticipate whether to cashout price is going to be System Sell or System Buy by monitoring NGC’s actions in the balancing mechanism. This could therefore lead to volume instability.
13.	What effect do you think Modification Proposal P78 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	P74 could result in the development of financial contracts for differences struck against the single cashout price. This could have the effect of reducing liquidity in the physical market and increasing the volume of energy cashout out in the balancing mechanism. (As with the Pool).
14.	Do you believe that the implementation of Modification Proposal P78 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition	See 13.

Q	Question	Response (Please provide rationale where possible)
	and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P78? (Section 1.21)	N/A
16.	Do you believe that Modification Proposal P78 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	P78 is more likely to target energy imbalance costs at those who cause that imbalance and therefore better satisfies that objective of the BSC. P74 is likely to provide windfall gains which do not reflect the cost of imbalance energy and leave this cost with the same participants who are paying for the net imbalance. It therefore does not help to achieve this objective of the BSC.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P78, if so, what is it? (Section 1.23)	N/A
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P78.	No
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	No

P74_ASS_010 – SEEBOARD Energy

Responding on Behalf of: **Seeboard Energy**

Responding as which type of Party (see list in section 1.21): **Supplier**

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	Yes. The calculation of energy imbalance prices and the method for removing system balancing is as now. The proposal, therefore, doesn't directly address separation but we agree that there is a secondary effect of reducing system balancing actions to the extent that they effect the reverse price.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	Yes. Again the calculation of energy imbalance prices remains as now. BOA will continue to be 'paid as bid', therefore, the value of actions by the SO is the same. In terms of top up and spill we agree that to some extent imbalances in the opposite direction of the system have a positive value to the system that is not recognised under the current arrangements.
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	The current arrangement discourages notified actions (FPN adhered to but not equal to contract) because over contracted and under contracted positions are penalised (relative to the market value of energy). This proposal changes from a system that is inherently penal to one that can also be attractive and rather than balancing may encourage participants to second-guess the system imbalance to the point that top up and spill may be more rewarded than BOA. This would potentially make it more difficult and expensive for the SO to balance the system.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	Yes. We believe that costs of balancing actions will fall more on those that are imbalanced in the same direction as the system. Also, there will be less smearing via RCRC.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of	We believe that there is a danger that participants may be incentivised to use their flexibility to choose their imbalance rather than submit

Q	Question	Response (Please provide rationale where possible)
	participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	bid/offers.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	We accept the evidence that would suggest that the asymmetric risk of imbalance prices is not key in determining the extent of part loading. We do not believe, therefore, P74 would have any material impact.
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	If participants are incentivised to second guess the system imbalance there will also be an incentive to deviate from their FPN post gate closure. If adherence to the Grid Code is insufficient and deviation from FPN becomes a problem this could be countered by a non-zero Information Imbalance Charge. However, an Information Imbalance Charge would be particularly detrimental to those participants that the mod is trying to help.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	Yes, we believe there is an increased incentive. However, assuming current measures in place are sufficient to prevent abuse we would not be unduly concerned.
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	The proposal does little to address the asymmetric risk as the price setting mechanism and the buy/sell spread remains the same albeit depending on the system imbalance.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	This mod would appear to incentivise participants to make contracting decisions based on their view of the system balance and the cash-out price rather than to balance (or over contract) as now. However, we believe that in reality this behaviour could lead to greater price volatility and risk and in turn encourage a strategy of balanced positions.
11.	In your opinion, do you believe that Modification Proposal P74 will	Yes. See 10.

Q	Question	Response (Please provide rationale where possible)
	change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Yes. See 10.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	It is arguable the extent of any interrelation between the forwards and spot market and imbalance prices. Whatever the view, we are not convinced that this mod would have any great impact on liquidity or prices or that it is particularly relevant to the assessment.
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	We do not believe that there would be any great impact on competition. We accept that in theory a system that encourages balancing (as opposed to over cover) should promote greater efficiency. We also agree that a system that encourages more precise and efficient contracting may lead to the trading of half-hourly products and consolidation for example. However, we are not convinced that this mod does these things.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	P74 focuses on unpredictable generators and small suppliers who are most disadvantaged by the current system particularly as it should encourage consolidation. We are not convinced that the risk is greatly reduced for these players. It seems to us that P74 may have greatest benefit to participants who are flexible.
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	No

Q	Question	Response (Please provide rationale where possible)
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	Yes, P78
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	No
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	No

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P74_ASS_011 - ScottishPower

Responding on Behalf of: Scottish Power UK Plc.; Scottish Power Energy Trading Ltd.; Scottish Power Generation Ltd.; Scottish Power Energy Retail Ltd.;
Responding as which type of Party (see list in section 1.21): Large Suppliers; Portfolio generators; Vertically integrated players

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system Vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	No. Modification proposal P74 uses the existing calculation of energy imbalance prices and does not directly address the issue of system balancing actions included in energy imbalance price setting.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	It is difficult to quantify how a single cash out price would take shape in the market. There is still a lot of 'settling down' to be done in the market and there is no real basis to say that it would value bids/offers or top up/spill more effectively than current methods.
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and	No, we do not think that P74 (on its own merits) will change the actions of those currently submitting PNs into the market.

Q	Question	Response (Please provide rationale where possible)
	instructed action)	
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	Response is as per question 3. The modification itself would not necessarily incentivise those currently building additional length into their PN submissions to reduce this length and submit more accurate PNs.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	It is also difficult to quantify this, in the light of P12 coming into play very shortly. We do think that the level of submissions into the BM will become more volatile as some players may hold back plant for BM participation or may decide to forwardly contract the bulk of it, depending on prevailing market conditions. P12 will amplify this as it gives a further 2½ hours worth of analysis before a decision has to be made.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	Part loading of plant is similar to building in length to a PN position – it gives the generator 'slack' to pick up a position if it is short as a result of a trip or a load dip at a station. Part loading is an inefficient method of operation, and one that has not been seen in the market for some months (with most generators operating at high load factors or indeed at their MEL). We think this is a moot point as it is not an inherent market characteristic and will not be addressed by P74 on its own.
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	No, the modification provides no incentive for participants to change their current PN actions.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	The introduction of P12 gives more time for parties to change PN submissions and also more time to monitor market conditions and make PN adjustments accordingly. This will not necessarily mean that more accurate PN submissions will be made – it could provide opportunities for certain larger players to influence the market thus providing potential 'gaming opportunities'.

Q	Question	Response (Please provide rationale where possible)
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	Asymmetric risk can only be fully eliminated if the market becomes more balanced. As already discussed, it is not the opinion that P74 will achieve this, therefore P74 may only reduce the risk but not fully address it.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	No. See comments in response to previous questions re accuracy of PN submissions.
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	No. See comments in response to question 10.
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Yes – see comments in response to question 8. This could, most definitely, lead to volume volatility and consequential price instability.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	In our view, P74 will have a detrimental effect on market liquidity. It could encourage participants to hold energy back for the BM if it feels current market conditions would facilitate higher levels of contribution from BM activity than from short term and prompt markets. Any lack of liquidity would have an upward effect on prices, thus making the prompt market more unattractive to participants. The effect would continue to perpetuate.
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17,	Comments as in response to question 13.

Q	Question	Response (Please provide rationale where possible)
	1.18, 1.19 and 1.20)	
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	Small Suppliers: Will continue to submit long (or very long) PNs to ensure they are not subject to large imbalance charges. Large Suppliers: Will continue to submit long PNs to ensure they are not subject to large imbalance charges. Licence Exemptable Generators: Will continue to submit long (or very long) PNs to ensure they are not subject to large imbalance charges. Unpredictable Generators: Will continue to submit long (or very long) PNs to ensure they are not subject to large imbalance charges. Non Portfolio Generators: Will continue to submit long PNs to ensure they are not subject to large imbalance charges. Portfolio Generators: Will continue to submit long PNs to ensure they are not subject to large imbalance charges. Vertically Integrated Players: Will continue to submit long PNs to ensure they are not subject to large imbalance charges. Non Physical Traders: Will continue to submit long PNs to ensure they are not subject to large imbalance charges. Transmission Company: As there will be no reduction in the length submitted through PNs, the energy and system balancing actions required to be completed will remain as before.
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	No. The proposal will fail to promote effective competition in the generation and supply of electricity as it could potentially reduce market liquidity and encourage some participants to withhold positions. It could also hamper the role of the System Operator in its obligations imposed under the transmission licence as it could have a detrimental effect on

Q	Question	Response (Please provide rationale where possible)
		participants within the BM and prices sought by participants for BM activity.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	It would be unwise to rule out a single cash-out method at this stage, or indeed propose an alternative calculation. The market needs more time to settle down (ideally another NETA winter) and possibly there may be some further self-regulation with the introduction of P12. If a single cash-out is still thought to be the right method of ensuring compliance with applicable BSC objectives, it should be rethought at the start of 2003.
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	No.
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	No.

P74_ASS_012 – Damhead Creek Limited

Responding on Behalf of: Damhead Creek Limited (DCL); Entergy Koch Trading Europe (EKT)

Responding as which type of Party (see list in section 1.21): Non portfolio generator; Non physical trader

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	Better separation of system vs energy actions is achieved through removing actions in the opposite direction, although we cannot be sure that energy actions have not also been removed. Imbalance prices, however, will still be 'polluted' by system actions in the same direction, for example, actions associated with transmission constraints.

Q	Question	Response (Please provide rationale where possible)
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	Through not penalising participants for 'helping' the system, actions are valued more correctly.
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	P74 does change the relative reward for notified and instructed actions as the potential is there to incentivise spill and so promote a corresponding increase in Bid/Offer prices.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	Those participants that are out of balance in the same direction as the system are targeted. Those participants that are out of balance in the opposite direction will receive, in principle, market price for their actions. This is an improvement on the present arrangements.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	P74 should reduce the perceived risk of Bid-Offer submission. It is also thought likely that P74 should tend to reduce the risk of trading in the power exchanges. Both effects should encourage participation in the Balancing Mechanism and system balancing should not be affected.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	The risk of exposure to imbalance prices is one of the reasons for the increase in part loading of plant, although, as argued in the consultation paper it is recognised that it is not the sole reason. Consequently, a move towards more cost reflective pricing in the Balancing Mechanism will tend to reduce the extent of part loaded plant on the system, that is, plant that is part loading in an attempt to protect against extreme System Buy Prices. Balancing action taken by the System Operator should be on a more efficient basis in terms of the system as a whole rather than, for example, through the provision of free reserve by participants choosing to take long positions into the Balancing Mechanism.
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section	P74 reduces the incentive for generators to deviate from FPN in the case of unforced outages as SBP will be less penal, but increases the incentive

Q	Question	Response (Please provide rationale where possible)
	1.9)	for small deviations from FPN to take advantage of market conditions.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	As with P12 and P4, P74 should increase within day trading. This would be a positive development in that it should encourage participants to balance closer to real time. At present there is a stronger incentive to deviate from Physical Notifications, if necessary, so as to avoid SBP. There remains, however, the need to safeguard against the provision of mis-information to the System Operator.
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	There will be no asymmetric risk to the buy-sell spread as it disappears but energy prices will continue to be asymmetric.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	P74 reduces the risk of imbalance to all parties. Therefore, the incentive for parties to balance their contractual positions prior to Gate Closure, rather than go long should be greater. It is believed that the reduction in imbalance risk may encourage non-physical players to take on imbalance risk post Gate Closure. This should improve liquidity in the short term markets. There may be less incentive for portfolio generators or vertically integrated companies to balance their individual trading positions as they can offset exposure to energy imbalance prices through adjusting their physical positions.
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	P74 should encourage parties to 'read' the market and if appropriate trade in the short term markets. Such activity should assist in balancing the market as a whole (individual balancing is not believed to be incompatible with market balancing). As mentioned in 10 above, P74 may facilitate non-physical related trading for risk management purposes, this should improve the incentive on physical players, both individually and collectively, to balance prior to Gate Closure. However, there is a concern that this will lead to hunting behaviour and therefore market instability.

Q	Question	Response (Please provide rationale where possible)
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Improved competition and liquidity in the market should tend towards rational market behaviour on the part of the players. The extent to which players' actions may lead to volume volatility and price instability will be dependent on the quality of market imbalance information. There is a concern that this will lead to hunting behaviour and therefore market instability.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	P74 should improve liquidity. The purpose of P74 is to move towards cost reflective energy imbalance prices - any inter-relation between forwards and spot markets with imbalance prices is believed to be irrelevant.
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	As mentioned in 10 and 11 above, it is anticipated that non physical players will become active in bearing the risk of imbalance, and this should see the development of risk management products and new types of contracts. As a result competition and efficiency of the markets should improve. There is, however, the potential for an emphasis on financial rather than physical trading, particularly by the portfolio generators and vertically integrated players.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	Small Suppliers: Benefit from reduced imbalance risk. Large Suppliers: Benefit in the same way as small suppliers. Licence Exempt Generators: Benefit from the 'enhanced' value of spill. Unpredictable Generators: (includes renewables and commissioning plant) Benefit through less punitive SBP and from the 'enhanced' value of spill. Non Portfolio Generators: Benefit through lower 'trip' risk through less punitive SBP. Portfolio Generators: Loss of market power, but will benefit through

Q	Question	Response (Please provide rationale where possible)
		lower 'trip' risk. Benefit through increased ability to self balance. Vertically Integrated Players: Loss of market power, but will benefit from improved efficiency of market as a whole. Benefit through increased ability to self balance. Non Physical Traders: Benefit through the opportunity to take on physical imbalance risk and offer risk management products. Transmission Company: Not financially affected except through its ability to hit incentive targets if BSUoS increases. Likely to have concerns about parties deviating from FPN and accuracy of information pre Gate Closure.
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	Improved removal of 'polluting' system balancing actions from the energy imbalance price tends towards a more cost reflective imbalance price. A less penal reverse price is also more cost reflective. This improved cost reflectivity better meets the Applicable BSC Objective to further promote effective competition in the generation and supply, and sale and purchase of electricity. However, increasing consolidation in the market place will serve to decrease effective competition. The incentive for parties to balance, both individually and collectively, prior to Gate Closure better meets the Applicable BSC Objective to ensure the efficient discharge by the Transmission Company of the obligations imposed under the Transmission Licence.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	DCL and EKT believe that while P78 improves the calculation of energy imbalance prices there are a number of flaws. It still does not address the problems of energy imbalance prices being polluted by system actions such as transmission constraints and actions that are not tradable in the forward markets. Further the determination of a market price will be difficult with the lack of liquidity in the half hourly forward markets.

Q	Question	Response (Please provide rationale where possible)
		Therefore, as a 'straw man' the following is presented for consideration: o Retain the definition of NIV, so removing the need for BRL; o Calculate the EIP from the 'main' stack as the average volume weighted price of all the offers/bids that would have been necessary to balance the system, after arbitrage and CADL have been applied and including BSAD volumes and prices. This must be done strictly in price order and so the defaulting rules being considered for P79 should be used, that is, it has to be possible for the System Operator to accept a submitted bid or offer. That way if the system is short 1000MW and there are 3 offers available each for 500MW at prices of £20, £21 and £30 respectively but the offer at £30 has to be accepted to relieve a transmission constraint as it also helps balance the system then the SBP would be £20.50, with the difference (£9.50) being used in the calculation of BSUoS; o Calculate the 'reverse' price as being the average volume weighted price of the first 25MWh of bids/offers that could have been accepted after CADL and arbitrage have been taken into account and by applying the same default rules as above. Using a small volume of bids/offers to derive the calculation will prevent gaming of the rules by parties submitting spurious prices for very small volumes and should be a fair reflection of a market price as the Balancing Mechanism is more liquid than the power exchanges; Change CADL to 30 minutes so that only system actions traded in the half hourly forward markets are included in EIPs.

Q	Question	Response (Please provide rationale where possible)
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	The purity of the imbalance price should be further considered. As mentioned in 1 and 17 above, imbalance prices will still be 'polluted' by system actions in the same direction, for example, actions associated with transmission constraints.
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	No.

P74_ASS_13 - Campbell Carr Ltd

Responding on Behalf of:

Electricity Direct	**Small Supplier**
BizzEnergy	**Small Supplier**
South Coast Power	**Single site generator**
Nedalo (UK) Ltd	**Embedded generator**
British Sugar	**Embedded generator**

These responses cover both P74 and P78 together because the effects are very similar in many instances.

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74/P78 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	In the current arrangements, despite changes to definition (such as P18A), the long market leads to a very small number of Acceptances setting SBP. The impact of any action for systems reasons therefore has a disproportionate effect on SBP. P74 does not directly address the split between system balancing and energy balancing actions but, by leading to a more balanced market – system balancing actions on the buy side will be "diluted" by energy actions, lessening their impact without a significant adverse impact on SSP likely. The resulting price is less likely to be extreme and will better reflect the price at which NGC is a net buyer of energy than is the case at present. P78 deems all actions in the opposite direction to be for systems reasons and so it will strip them away from the price mechanism. It also strips equivalent volumes from the main price setting a lower price. It is impossible to be certain that actions for energy reasons have not been stripped away as well but it

Q	Question	Response (Please provide rationale where possible)
		seems likely that the resultant main price will be a better reflection of the cost of energy needed for pure energy balancing reasons. The reverse price used in P78 is an approximate spot market price and this is a significantly better reflection of the value of reverse actions than is the case at present and will certainly exclude systems actions although it is less certain that the price is a proper reflection of energy cost to the system.
2.	In your opinion, is Modification Proposal P74/P78 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	P74 values actions in the direction of system balance in the same way as at present. The change is in the valuation of the reverse price. NGC balances the system based on the difference between generator FPNs and their own forecast of demand (with no reference to contract position which they do not know until up to 14 months later). The deviations from FPN are caused by generators tripping (or being late) and due to consumers in aggregate deviating from the NGC forecast. Suppliers' contract positions relative to their individual forecast of their own customers' demand (e.g. over-contracting as at present) will not alter the actions taken by NGC because the deviations of customer offtake relative to the NGC forecast will be the same. Therefore the value of actions taken by NGC will be the same regardless of any supplier's contract position and the single price proposed in P74 reflects this. P78 potentially better reflects the value of energy actions in the main price than does P74 but there seems a less soundly based case for the valuation of the reverse price because it is still applied to contract positions which NGC knows nothing of at the time of the action taken. However, the market price used for the reverse price is definitely more cost-reflective than the current SBP/SSP.
3.	In your opinion, how does Modification Proposal P74/P78 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	NGC expresses the opinion that an instructed action (through a BM Acceptance) is worth more than an unnotified delivery or offtake that is in the direction of system balance, and do not see why P74 should thereby reward such actions better than acceptances (by definition some BM acceptances must be at a less favourable price than the price proposed in P74). However, this mistakes the value of such spill/shortfall because, in a BM acceptance, the price is one that is acceptable to the bidder or offerer, whereas in unnotified spill/shortfall the risk is that the price will be unfavourable and is as likely to be a loss or a gain. This is interpreted by NGC as a reward for gambling when going against the direction of the system but it is really simply paying the value of your position to the system (i.e. it is cost-reflective) bearing in mind that there will be very few parties who will take a physical position in this way intentionally rather than due to errors in their forecasts of their own metered position. P78 asserts that the value of an action that helps the system accidentally is worth no more than the

Q	Question	Response (Please provide rationale where possible)
		market price but offers no justification for this view. It is certainly a better valuation than the current arrangement, which punishes such "accidental" help regardless but this is still not a proper reflection of the value of the offsetting volumes, which allow NGC to take less balancing actions than they would otherwise have taken.
4.	In your opinion, does Modification Proposal P74/P78 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	P74 targets the cost of energy imbalance on those causing it and gives the benefit to those who help the system whereas the current system punishes regardless and certainly mis-targets the costs on positions that help the system. P78 targets the costs of net imbalance on those who are out of balance in the same direction as the system. It values contractual imbalances that help the system better than the present mechanism but does not offer the full reward for that help.
5.	In your opinion, how does Modification Proposal P74/P78 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	This is a complex area. Currently generators are operating at part load excessively in order to provide capacity for self-reserve. Generators are offering self-reserve volumes as BM offers at present (it may, however, be worth examining the extent to which they are setting MEL to FPN to prevent such offers being accepted). If generators reduce the volume of self-reserve by selling more gensets fully and not operating on others then the volumes available as BM offers could reduce. This would be more efficient for the system overall although the cost borne by NGC for carrying reserve would increase. The phrasing of the actual question is about the risks of bid/offer submission. P74 reduces the risk of bid/offer submission because if an acceptance is made that cannot be delivered (e.g. due to a generator trip) then the cost of that failure is not necessarily changed. Given that self-reserve is offered to NGC as offers at present, the main expected change will be in the price at which such offers are made which should be lower if the cost of failure is lower. This would not otherwise affect system balancing. P78 has a similar effect to P74 but, by reducing the potential upside to cash-out in the event of failure to deliver, it can be expected to have a lesser effect on bid/offer pricing than P74. P78, by maintaining a buy-sell spread may have a lower impact on the failure risk than P74 but would still be much better than at present.

Q	Question	Response (Please provide rationale where possible)
6.	In your opinion, how do you believe Modification Proposal P74/P78 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	P74 would reduce part-loading to an extent for the following reasons: • In a more balanced market, fewer bids would be taken, reducing part loading on pulled back plant; • The cost of generator trip would be reduced and so self-reserve would be less necessary – this suggests fewer plant operating at fuller load. However, on the reverse side: • A more balanced market increases the probability of an offer being accepted, which increases the reward for part-loading (to an extent); • With fewer plant scheduled by participants onto the bars, NGC may need to schedule more part loaded plant via reserve contracts. The effect of P78 is similar but to a lesser extent.
7.	In your opinion, does Modification Proposal P74/P78 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	Currently, there are two incentives on generators to deviate from FPN: • To replace a failed plant from the portfolio when SBP is expected to be high (which is easily done from part-loaded plant but which will be used rarely); • Generating to the upper end of the expected level of output in order to avoid a marginal shortfall at SBP – this gives a lot of very small volumes of persistent spill. P74 will reduce the first of these in some circumstances (while recognising that if a large set fails completely it could tip the system short anyway), and will eliminate the bias in the second as the cost of going short will be reduced. Generators may still seek to over-deliver against FPN when they see the network going short but they risk this breach of the grid code only netting SSP anyway (especially if others do the same) and they would almost certainly be better off contracting with NGC (as PGBTs or Offers) given that they would only be doing this spill when they have good reason to believe that NGC will need the energy. In any case such opportunities will be vanishingly rare under a 1-hour gate closure. P78 will not offer the same potential incentives to deviate from FPN and will reduce the existing incentives.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74/P78 increase the incentive on parties to change Physical	P12 is the latest Modification approved that explicitly facilitates contracting close to gate closure. Given that IPNs will usually represent the contracted position at the time rather than an expectation of striking contracts, it can be expected that changes up to FPN will be more frequent. P74 will only increase opportunities for late changes to FPN to the extent that there is extra information indicating a specific direction to system balance. Opportunities for price-seeking by

Q	Question	Response (Please provide rationale where possible)
	Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	changing a physical position will only arise to the extent that there is extra information about system balance available. Given that IPNs will be less useful as a predictor of system balance due to these same late changes from other parties, excessive speculation on the physical position of the market will be muted. It should be noted that parties may still speculate on the direction of the market in the current situation in that a rising price in the spot market suggesting that the market is short will raise the expected cost of a supplier going short and so they might choose to go even longer. Some "opportunities" will still arise from P78 because an expectation of a more balanced market will change parties' perceptions of optimal position (if the spot price is rising, it suggests the system might be short, which increases the risk-adjusted value of spill so that other parties might seek to go longer). P74 does allow notifications much closer to gate closure because the risk of notification failure can be managed financially under a single price. Both P74 and P78 therefore may make system management more difficult for NGC but the big change in difficulty arose from P12 and the difficulty was thought to be outweighed by the improvements due to parties being able to balance more closely.
9.	In your opinion, to what extent will Modification Proposal P74/P78 address the issue of asymmetric risk? (Section 1.10)	There is confusion as to what is meant by asymmetric risk. Asymmetry in price risk arises primarily where the spot price (the price of buying out of the price risk) is closer to a risk-weighted expected SSP than to a risk-weighted expected SBP. The relative volatility in SBP simply raises its risk-weighted expected price. P74 will raise the opportunity cost of spilling because, as generators have the opportunity to spill at a potentially higher price, they will not offer power to suppliers at a prompt price that does not reflect this opportunity. This raises the spot price and makes the risks more symmetrical. P74 therefore addresses the causes of the observed (i.e. ex post) asymmetry in prices. P74 does not directly address the more fundamental asymmetry in volatility in SBP relative to SSP for which there are good economic reasons although some of the volatility caused by pollution of the energy price by systems actions will be diluted because these actions will only affect the "main" price, which will include much more energy in its calculation. P78 seeks to more directly address price pollution from systems actions by extensive tagging out and as such will produce a less volatile main price although the underlying relative volatility inherent in short-notice incrementing will remain. In other respects the impact of P78 will be similar to P74 but more muted.

Q	Question	Response (Please provide rationale where possible)
10.	In your opinion, do you believe that Modification Proposal P74/P78 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	As explained in *9* above, P74 will raise the cost of excessive spill, which will thereby reduce, leading to a more balanced market. Similarly, as the cost of going short remains a high price (although relatively reduced), the incentive on all parties with uncertainty about their ex post physical position remains to balance. P78 has similar incentives but is more muted because the up side of getting it wrong are less (leading to a probably longer market than P74).
11.	In your opinion, do you believe that Modification Proposal P74/P78 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	P74 will lead to a more balanced market because balancing decisions will be informed by expected market balance – which is not the case at present. Also, if suppliers seek to be closer to balance individually (by spilling less), the market will be closer to balance. P78 will be similar but the effects are more muted and so the market is likely to be longer than under P74 but less long than at present.
12.	In your opinion, does Modification Proposal P74/P78 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Parties will only price-seek under P74 to the extent that they have good information about the direction of market imbalance. The fear of hunting has to be vastly exaggerated. Generators have a slightly better view of market balance to the extent that they know if their own plant is at risk of failure. However, they will be price-takers (the "hunted") in such a scenario – not hunters. Such generators will seek to contract out of their own adverse balance. Other generators will usually be better off by offering their flexibility to NGC rather than speculating. P78 is similar in effect – it won't lead to significant hunting of the market direction. There is not enough information out there to make it worthwhile.
13.	What effect do you think Modification Proposal P74/P78 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	P74 will vastly increase liquidity in the spot markets because it eliminates notification risk (a failure to notify can be covered financially in a single-price environment). P74 will impact on spot prices because it changes the value of buying out of imbalance. It will have less effect on forward prices. P78 will have similar effects other than on liquidity in the spot market, which will be muted by the remaining dual cash-out price effect on notification risk. It has been asserted that, under P74, parties will not contract and simply take a "Pool" price. This misunderstands the nature of the Pool in which generators were guaranteed revenue based on the

Q	Question	Response (Please provide rationale where possible)
		day-ahead price. Without a contract, generators can only be guaranteed a low ex post spill price and so will not generator without a contract (either notified before gate closure or else on a CfD). If generators don't generate then the market will be short so suppliers have an incentive to contract to avoid SBP. The incentive to contract remains and, given that the market was about 90% contracted under the Pool, there is no reason to believe that contracting will be any less than at present (except that the market will be contracted to balance rather than being over-contracted).
14.	Do you believe that the implementation of Modification Proposal P74/P78 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	Under a single cash-out price as in P74, volume risk management can be offered across the system rather than just behind the meter. Much of this will probably be via CfDs but traders will offer other products as well because they would be able to take a physical position if the price risk was not always negative. This is fundamentally efficient and normal because risk is moving to the parties most willing to bear it. P78 does not offer the same opportunities because, although downside risk is reduced, there is no upside risk available for the risk manager.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74/P78? (Section 1.21)	• Small suppliers will benefit from both Mods but especially form P74 because the artificial penalty applied to small portfolios (with a statistically greater imbalance risk) is removed (by P74) or reduced (by P78). • Larger suppliers benefit like smaller ones in not needing to over-contract – and they can buy better risk management across the system. However, they benefit less than small suppliers because their artificial relative advantage in portfolio size is removed. • Licence Exempt Generators (LEGs) are significant winners from both Mods but especially from P74. This is because the value of spill – the price that many embedded generators have been offered in contracts – has increased to incorporate a possibility of earning either from a market price (P78) or from SBP (P74). Suppliers will therefore be able to offer prices to embedded generators at a price reflecting this. In addition, in a more balanced market, NGC will provide more of the reserve (rather than suppliers doing so via over-contracting) and so embedded benefits will improve. For LEGs in CVA, the cost of consolidation will be removed by P74 and reduced by P78. • Unpredictable generators will benefit by being able to contract to their average expected output rather than to the minimum because shortfalls will not always be punished at SBP. They will therefore spill less.

Q	Question	Response (Please provide rationale where possible)
		• Non-portfolio generators face lower trip risk and so will earn at a higher rate. To the extent that the average spot price increases, they may be able to strike better contracts, but if the forward market does not move then this will not be the case. • Portfolio generators will lose market power and so will be slightly worse off, but to the extent that their effective trip insurance cost will be lower, they will benefit. • Vertically integrated parties will similarly lose market power but will still operate in a more efficient, lower cost, market. • Non-physical traders will have the opportunity to take on a degree of physical risk under P74 (but not under P78) and so will benefit from being able to offer a fuller range of risk management products. • The transmission company will not be directly financially affected by either of these proposals because it passes through costs anyway. Longer term it stands to lose out to the extent that the growth of embedded generation will no longer be stunted by the current penal pricing system. The Consultation document fails to mention the following relevant parties: • Flexible plant will benefit from a balanced market where NGC contracts for rapid reserve when needed rather than only varying the extent to which excessive plant is pulled back. • Consolidators will lose out under P74 – they will be redundant. • Exchanges will benefit from improved liquidity under P74 due to reduced notification risk. • Consumers will benefit from a more efficient market whereby suppliers are not over-contracting and generators are not self-reserving. The spot market may move up but, to the extent that forward prices are driven by Europe through arbitrage across both the gas and electricity interconnectors, it is far from certain that consumer contract prices will move to any great degree. Longer term, consumers can only benefit from a rational market in which the risk of a "California" scenario – where uneconomic generating plant is excessively mothballed because market returns are so depressed so that the market is rapidly tipped into shortage – is reduced.
16.	Do you believe that Modification Proposal P74/P78 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	P74 clearly better facilitates the Applicable BSC Objectives: • It is more cost-reflective in that it correctly values balancing energy, which is independent of contract positions, which NGC knows nothing about at the time of the balancing action. It also targets those costs on those causing the imbalance rather than penalising parties who are helping the system (by contracting to a position that does not force excess balancing actions). It therefore

Q	Question	Response (Please provide rationale where possible)
		facilitates competition. • It will lead to a more balanced system, reducing NGC's need to take balancing actions, which is more economic and efficient. P78 also better facilitates the Applicable BSC Objectives: • It prevents more system balancing actions from polluting the energy imbalance price, making that price more cost-reflective and it sets the reverse price as less penal, which is more cost-reflective. It therefore facilitates competition. • It reduces the incentive to spill excessively leading to more economic and efficient operation of the balancing mechanism.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74/P78, if so, what is it? (Section 1.23)	N/a
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74/P78.	The Consultation Document fails to address the specific problems faced by embedded generation in the current mechanism. As noted above, the only way for such players to participate in the current process is to: • Either go into CVA and be consolidated, which is an administratively expensive process relative to the scale of generation and is not currently offering any attractive prices anyway; • Or to sell to suppliers in SVA and be offered the derisory spill price. The reason that suppliers are offering embedded generation such low prices is not related to inherent variability of output (which Ofgem has already demonstrated is generally not the case) but because the product that an embedded generator must offer to suppliers is different to the one offered by CVA generation. This is because CVA generation delivers firm energy through contracts with the generator able to manage its own meter risk, whereas an embedded generator must sell that meter risk to the supplier and has no opportunity to manage it. Another factor not covered has also been raised above. Because the current mechanism is not rewarding upward flexibility properly (because the spill market means that excessive downward flexibility is being taken), consumers are being forced to overpay for self-reserve rather than for the product that NGC would otherwise contract for. This depresses BSUoS, which has an adverse impact

Q	Question	Response (Please provide rationale where possible)
		on embedded benefits.
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	N/a

P74_ASS_14 - Edison Mission Energy

Responding on Behalf of: **First Hydro Company, Edison First Power**

Responding as which type of Party (see list in section 1.21): **Non portfolio generator**

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	No. P74 continues to use the BRL concept to tag trades deemed to be for system balancing purposes. The BRL mechanism is generally recognised to be flawed under the current dual cashout arrangements. However, if P74 did lead to a more balanced market as envisaged by the Proposer then NGC will have to hold more reserve on both sides of the market and the BRL would become more relevant. But, with only a single cash out price, this reserve holding will not be reflected in the cashout prices for the smaller stack.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	No. P74 would over reward any action in the opposite direction to the market.

Q	Question	Response (Please provide rationale where possible)
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	The reward will change for a short period. However, participants will quickly learn that adopting a risk management strategy that relies on doing the opposite to the rest of the market is inherently unstable.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	No. For those out of balance in the same direction as the market, targeting of energy balancing actions will remain unchanged. For those out of balance in the opposite direction to the market, costs will not properly be targeted as a better price will be achieved than if trading had taken place on the PXs. It is inappropriate that Parties that are out of balance in the opposite direction to the market receive/pay a better price than those that have balanced their positions prior to gate closure.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	Under P74, due to the asymmetry of the generator supply curve, suppliers will still be incentivised to go long. By going long, the worst case is that they receive SSP, although occasionally they could receive SBP P74 therefore has the potential to create a perpetually albeit slightly less long market (EME estimates that it will fall from being about 3.5% long to 3% long). Since the price will almost always 'flop' to SSP, the exposure to cashout in the event of a trip will be much reduced. Such a small change in system length is unlikely to lead to increased BM participation on the offer side.

Q	Question	Response (Please provide rationale where possible)
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	With respect to part loading at gate closure, the answer depends on taking a view on the probability of an offer being accepted and the differential between PXP and offer price and also the correlation between PXP and SBP. Therefore modelling should be undertaken in order to properly answer this question although see answer to Q19. Furthermore, parties will part load if it is economically efficient for them to do so. Parties choose to part load for may reasons. Currently, the market is generally long, the occasions when offers need to be accepted are far less than for bids. In a less long market, more offers will be accepted, more generators may therefore choose to part load to take advantage of increased probability of acceptance in the BM. However if there is more competition, the probability of acceptance will change little. The level of part loading is therefore unlikely to change. Since parties are each incentivised to balance their own positions, in a long market generators will choose to part load their marginal BM Unit as selling the additional output would be at a price below the marginal cost of the purchaser's plant. It would not be in generator's interests to sell at this price because it would affect prices further out on the curve. Therefore, even though such part loading is environmentally inefficient, it is unsurprising. Alternatively, if spot prices increase, and this is coupled with an increase in within day liquidity, plant may be more fully loaded as generators might prefer the certainty of PX sales compared to the uncertainty of BM sales. The degree of part loading will therefore change little under P74.
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	No. Grid Code obligations have generally provided sufficient incentives to adhere to FPN. If Grid Code obligations and the additional risk of getting

Q	Question	Response (Please provide rationale where possible)
		the market direction wrong are found to be insufficient, an information imbalance charge should be introduced.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	Parties may change their FPNs shortly before gate closure either to match a change in contract position or because they are trying to second guess market direction and create an imbalance position in the opposite direction to the market. The former must not be discouraged otherwise it defeats the purpose of P12 and also of the improvements to the notification process to improve within day liquidity. Any restriction on changes to FPN close to gate closure would discriminate against flexible plant who will be trading closer to real time and also discourage investment in systems that allow trading close to gate closure. The ability of players to change PNs close to gate closure is therefore a good thing. For incentive to deviate from FPN post gate closure please see answer to Q7. An information imbalance charge should be introduced if the Grid Code obligations are considered to be insufficient.
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	Because the offer stack has a steeper tail than the bid stack, asymmetric risk will still exist and the market will remain long albeit the length of the system will reduce slightly. This will mean that the cashout price will mostly 'flop' to the SSP. It would be an easy step to a perpetually long market where the cashout price is always SSP causing spot and forward prices to fall further. Vertically integrated companies and pure suppliers will be largely unaffected by a perpetual SSP as they are able to make profits in the domestic supply market.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	Suppliers might become less long but will stay long for the reasons given in Q5 and Q9. On the assumption that SSP most often sets the cashout price, generators will move more to balance as they will rarely be exposed to the SBP and would wish to avoid spilling at the below marginal cost.

Q	Question	Response (Please provide rationale where possible)
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	For the reasons given in Q9, the market as a whole will remain long rather than balanced.
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Yes - see answer to Q3. Volume volatility and price instability will occur but they will be short lived until participants realise there is little benefit in trying to second guess market direction.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	P74 will reduce liquidity as suppliers will have less tendency to contract away from their expected demand position although they will still be incentivised to stay long. Forward and spot prices will fall due to low cashout prices as discussed in Qs 5 and 9.
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	CfDs might emerge but they will fragment liquidity. CfDs will remove notification risk but will increase the BSC credit burden for pure suppliers and remove it entirely for generators and vertically integrated companies whose GC is greater than DC as there will be no need to notify ECVs. BSC credit cover will therefore fall entirely on pure suppliers and verticos with DC greater than GC. Pure suppliers would be disadvantaged as the costs of CfDs would be prohibitive. This will be exacerbated when live prices are used to calculate credit cover. BSC credit arrangements will therefore need to be addressed if P74 is implemented.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	The risk profile of vertically integrated companies will reduce as they will be able to net off production and consumption accounts at the same cashout price and will only have to balance one book. In particular, these companies will have an unfair advantage over other players through the use of load management options allowing self balancing post gate closure, an option that will not be open to other types pf player without breaching the Grid Code.

Q	Question	Response (Please provide rationale where possible)
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	Since P74 will perpetuate the long market, it will not improve the efficient economic and co-ordinated operation by the Transmission Company of the Transmission System It will not improve incentives to balance rather than spill as by spilling there is the possibility of receiving SBP. P74 does not therefore better facilitate the efficient discharge by the Transmission Company of the obligations under the transmission licence. Since pure suppliers will incur costs in the use of CfDs which will not apply to other types of participant, P74 will not promote competition in the sale and purchase of electricity.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	The assessment also needs to consider the incentives on NGC. Whilst these issues might be considered to be outside of the vires of the group, I note that in its determination on Mod P3, Ofgem considered that 'NGC would have faced distorted incentives relating to its balancing services purchasing strategy of variations in energy imbalance prices were related to whether it had contracted forward, rather than to fundamental market conditions' . The group does therefore need to consider what impact P74 will have on NGC's incentive scheme since NGC benefits in its incentive scheme from a long market,
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	Any analysis arising from the modelling that is reported in future consultations should be very heavily caveated and should list the assumptions made in order to simplify the modelling. There is a danger that without a detailed explanation of any limitations, respondees to the next consultation will choose the Modification that produces outcomes that meet their cashout pricing expectations without any further

Q	Question	Response (Please provide rationale where possible)
		exploration of the implications of the changes.

P74_ASS_015 – Innogy plc

Responding on Behalf of (please list all BSC Parties): This response is on behalf of Innogy plc, npower Limited, Innogy Cogen Trading Limited, npower Direct Limited, npower Northern Limited, npower Yorkshire Limited

Responding as which type of Party (see list in section 1.21):

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	P74 does not address the tagging of BOAs that creates the separation of system and energy actions. Our view is that there can only be a single value of energy at any one time for the purposes of energy balancing. P74 uses the existing methodology as a base for deriving system prices (both SSP and SBP) together with the associated process for distinguishing between system and energy balancing actions. P74 consistently values energy imbalances by deriving the price from these imbalances by reference to the overall state of the system.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	We are assuming that the 'actions' referred to here are Bid Offer Acceptances. P74 does not change the approach towards valuing BOAs taken by the SO when compared with the current methodology.
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	P74 seeks to relate the value of notified actions that assist in system balancing to the value of the actions taken in the Balancing Mechanism for the same purpose. The current methodology, however, penalises these notified actions. Consequently P74 better reflects the value of the energy at any time regardless of origin. This should facilitate the actions those willing to assist in the balancing the system and thus lower the costs faced by the Transmission Company. This should lead to more efficient system operation and energy balancing.

Q	Question	Response (Please provide rationale where possible)
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	A dual cash out process inevitably requires the construction of an "artificial" price for imbalances that are in the opposite direction to system balance (the so-called "reverse" direction). Because the cost of balancing the system is dependent upon the direction of the system imbalance (i.e. whether the system is long or short) P74 will more correctly target the cost on those causing the imbalance.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	As noted above, P74 should encourage balancing by participants thus reducing the overall costs for the system. It is therefore unlikely that P74 would have much impact on the balancing mechanism. Parties would retain the same incentive to submit bids and offers through the pay as bid auction.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	To the extent that P74 encourages parties to balance their positions, the modification should reduce the amount of part loaded plant although the decision whether to hold part loaded plant is ultimately a commercial decision taken by individual parties. Changes to the pricing mechanism may or may not have an impact on these commercial decisions.
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	The requirement to follow FPN is a Grid Code obligation. P74 cannot therefore produce any "incentives" in respect of this Licence obligation.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	In so much as P74 encourages liquidity in the prompt market and thus the ability to trade it will increase the incentive on parties to change PNs to better reflect their operating intentions after Gate Closure. This will allow NGC to balance the system based on those FPNs with greater confidence and at lower cost. It is therefore a "good thing".
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	P74 does not change the asymmetric risk associated with electricity prices, but it will change the cost of accommodating this risk as the

Q	Question	Response (Please provide rationale where possible)
		imbalance price better reflects the value of the energy.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	The dual cash out pricing arrangement that currently applies encourages parties to be systematically long because of the endemic asymmetry between SSP and SBP. A single cash out price should encourage parties to better balance their position since this will generally minimise their costs. To manage their risk parties may go either long or short at times of price asymmetry under a single cash out price but this will generally only be at times of peaks and troughs. At these times the interests of generators and suppliers will be in opposite directions thus still encouraging balance in the overall market.
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	As noted in response to Question 10 the present pricing arrangements do not encourage balancing by parties. A single cash out price will generally make the balanced position one of least cost and thus provides a better incentive to balance. It should also encourage liquidity in the prompt market that in turn will facilitate balancing.
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Parties may try to anticipate the direction of system balance, but in the absence of perfect information it will be difficult to systematically ensure that parties are on the “right side” of the market (whichever side this is). This should reduce volume volatility although price volatility may well increase thus further encouraging balancing.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	Our view is that P74 should enhance liquidity in the spot market and ensure prices that better reflect resource costs. The same economic drivers should then be apparent in both markets and the relationship between the prices of both markets will then follow the same market fundamentals. The level of the prices will depend on the market.
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition	The stronger incentive for parties to balance will encourage the development of new risk management products. This should encourage competition in the provision of these products and the efficiency of the

Q	Question	Response (Please provide rationale where possible)
	and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	forward and spot markets.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	To the extent that P74 removes the significant SBP and SSP price spread and perversity in reverse prices, the risk profile of the whole market should reduce with potential benefits for all parties. We do not believe that P74 will change the relative risk profiles between parties or different classes of party.
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	P74 will better facilitate BSC objectives 1.2.1 (b) (ii) and 1.2.1 (b) (iii), for all the reasons given within this consultation response.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	It should be worth examining a single imbalance price using the P78 Net Imbalance Volume methodology as an alternative split between system and energy balancing. Assessment of this alternative should indicate if it better facilitates the relevant objectives.
18.	Are there any other issues not identified in the supporting document, which you believe should be considered during the assessment of Modification Proposal P74.	No
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	

P74_ASS_016 – RWE Trading Direct

Responding on Behalf of **RWE Trading Direct:**

Responding as which type of Party: **Small Supplier**

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	For the main price the separation of System actions and Energy actions is not altered but the reverse price is no longer based on those few actions taken in that direction which may not provide a representative cost, however by using the same price as the main price all parties who are out of balance face the same cost which is more representative of the cost of balancing.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	Not for the main price as the methodology remains the same. For the reverse price the actions are not valued at all, unlike the current proposals.
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	Participants may under P78 feel that taking a position opposite to the market position (i.e. long if the market is expected to be short) will mean greater rewards are possible if the prices available in the market just before gate closure are below the expected reverse price. As the reverse price may frequently provide this incentive, participants may believe the reward large enough to warrant the risk. If a party took a position opposite to the market of a significant size there would be a significant chance of altering the direction of the market and this interaction will reduce the amount of "hunting" under P74 to a level that should not significantly impact the Transmission Company.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	No, the distribution of cost to participants is not changed, however the differential in costs faced by large and small participants will be reduced as the price of both SSP and SBP will be nearer the market price.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of	P74 should bring the market to a position nearer balance therefore increasing the need for the Transmission Company to accept Offers to

Q	Question	Response (Please provide rationale where possible)
	participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	increase Generation or reduce Demand so more participants should be encouraged to participate in the Balancing Mechanism especially in the mid to high price range thus reducing the cost of any extreme situations and increasing available plant in the Balancing Mechanism. In addition the reduction in the difference between SSP and SBP and the market price will reduce the cost of failure and therefore the risk thus increasing participation.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	Unknown
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	The only additional incentive to deviate from FPN is in order to take advantage of the reverse price after Gate Closure so as to increase a participants certainty of which price will be the reverse price, but as this would violate the grid code sufficient deterrents should already be in place.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	The need to predict the reverse price in order to determine a participants strategy may encourage parties to increase trading in the period before gate closure, however as the cost of being short (in a short market) is still higher than the cost of being long participants may be reluctant to try to guess the direction of the market and if this is not predictable then significant changes in strategy just prior to Gate Closure are unlikely.
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	Asymmetric risk is not eliminated just reduced
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	Yes, parties will be incentivised to be more in balance, as the risk of being short will be reduced, however the incentive to forecast accurately will still be significant.

Q	Question	Response (Please provide rationale where possible)
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	Under P74 parties will be likely to be less long and therefore the market as whole will also be less long.
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	See response to question 1
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	As parties are likely to try to trade nearer to balanced then liquidity in the short term markets should be increased, as participants will be more sensitive to changes in expected demand levels.
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	Yes, risk management products will be able to be developed with the introduction of a single price cash out.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	As RWE TDL probably fits into the category of small supplier we would expect our risk profile to reduce as SSP and SBP are closer to the market price. Despite Customer not being a category we would expect their costs to be reduced due to the reduction in risk their supplier will have to accept on their behalf.
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	Yes 3b by encouraging an overall market position that is closer to balance the extent of the actions taken by NGC should be reduced, thus improving the efficiency of the system.

Q	Question	Response (Please provide rationale where possible)
		3c by allowing the development of risk management tools and encouraging additional short term trading P74 should promote competition.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	No
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	No
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	Yes, modelling may not provide all the answers but may provide some useful insights into the way P78 may affect the market. The form of the modelling should be discussed at the relevant Modifications Group with assistance from experts in this specific field.

P74_ASS_017 – AEP Energy Services

Responding on Behalf of: **AEP Energy Services Ltd and AEP Energy Services UK Generation Ltd**

Responding as which type of Party (see list in section 1.21): **Trading Party**

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	No. Modification P74 does not address the problems associated with the current 'tagging' of system balancing actions. The tagging mechanism has been shown not to work as was intended.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	No it is not. Bid-offer spreads are a common feature of all markets and by applying a single price to parties with short and long imbalances the proposal would not value actions on one side of the market correctly.

Q	Question	Response (Please provide rationale where possible)
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	Do not see any benefit to the assessment of the modification from introducing this distinction. As long as System Operator can rely on accurate FPNs it should balance the system based only on FPN data and demand forecasts. P74 weakens the commercial incentives on Parties to balance contractually through the removal of the dual price. This could lead to a greater role for the Transmission Company in system balancing.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	No because of the removal of the dual cash-out price.
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	Would reduce perceived risk and may increase participation in the Balancing Mechanism. Likely to increase costs of system balancing by significantly reducing the commercial incentives for parties to balance ahead of gate closure.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	Not a relevant consideration in assessing the modification. The imbalance price should reflect the costs of imbalances on both sides of the market. Market participants are then best placed to respond to this dynamic price signal and judge whether part-loading is an appropriate commercial response.
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	No. Adequate arrangements are already in place through the Grid Code to ensure accurate FPN submission. NGC has not reported significant problems to date and Ofgem has powers to fine where breaches take place.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	Yes. Parties changing Physical Notifications shortly before Gate Closure could be 'good' or 'bad' depending on the circumstances. If changes in PNs are the result of Parties seeking to trade out imbalances within day and more accurately reflect actual metered generation and demand in the relevant settlement period then this would reduce the role and costs of the Transmission Company's system balancing actions. This would be

Q	Question	Response (Please provide rationale where possible)
		a 'good' thing. If changes in PNs reflected the attempts of Parties to go long or short into imbalance and the cash-out price was not cost-reflective and was less costly than trading out the imbalance then this would be a 'bad' thing. This proposal would be more likely to encourage the latter sort of behaviour.
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	The question implies that any asymmetry is problematic. P74 addresses any perceived asymmetry by definition. However, if the asymmetry is cost reflective (and there are good reasons why it might be given the relative costs associated with flexing up and down) then it should not be addressed.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	Yes, for the reasons already outlined.
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	Yes, for the reasons already outlined.
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Yes, for the reasons already outlined.
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	P74, by reducing the commercial incentives to balance, would lead to greater imbalance volumes and less forward trading of energy, thereby lowering liquidity. Energy imbalance prices be more volatile as a result. The effect on the level of prices is difficult to forecast.
14.	Do you believe that the implementation of Modification Proposal P74 will	No as the modification will reduce incentives to forward contract.

Q	Question	Response (Please provide rationale where possible)
	encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	Would artificially reduce the risk of certain parties (e.g. small suppliers, unpredictable generators) at the expense of other parties through the application of imbalance prices that do not reflect costs.
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	No.
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	No.
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	More attention should be focused on the problems with the current tagging mechanism to ensure that any change to the rules removes actions that clearly relate to system balancing (e.g. Transmission Constraints) from energy imbalance prices.
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	Additional analysis and modelling is not necessary.

P74_ASS_018 – Eledor Limited

Responding on Behalf of (please list all BSC Parties): **Eledor Limited**

Responding as which type of Party (see list in section 1.21): **Non Physical Trader (Consolidator)**

Q	Question	Response (Please provide rationale where possible)
1.	In your opinion, does Modification Proposal P74 give a better separation of balancing actions (i.e. system vs energy) used in setting the Energy Imbalance Price(s), if so, how? (Section 1.1)	No.
2.	In your opinion, is Modification Proposal P74 valuing actions more correctly, if so, why and if not, why not? (Section 1.5)	No. Participants who are long or short are exposed to a price that may vary between SBP and SSP. The cost of imbalance faced by individual participants is not cost reflective or directly related to the corresponding energy balancing action.
3.	In your opinion, how does Modification Proposal P74 change the relative reward for notified and instructed actions and how do you believe this to impact on the Transmission Company's balancing of the system, and do you believe this is appropriate? (Section 1.6 defines notified and instructed action)	Modification P74 distorts the position. For example the imbalance charge potentially seen by an individual participant who goes short would vary between SBP and SSP dependent on the Net Imbalance Volume. The exposure to potential punitive dual cashout prices would be reduced, although the price volatility would increase for being out of balance in a particular direction. Participants taking notified actions would be exposed to more favourable imbalance charges. As there is less risk in taking notified actions, it follows that more notified actions may be taken to reduce the potential risk of exposure to SBP. Failure to deliver instructed actions would also expose participants to less punitive non delivery charges.
4.	In your opinion, does Modification Proposal P74 more correctly target the cost of energy balancing actions to those causing the imbalance over the current baseline? (Section 1.6)	No. A fundamental principle of NETA has been the incentive to self balance. The cost of imbalance faced by individual participants is not cost reflective or directly related to the corresponding energy balancing action.

Q	Question	Response (Please provide rationale where possible)
5.	In your opinion, how does Modification Proposal P74 change the perceived risk of Bid - Offer submission, how would it change the level of participation seen in the Balancing Mechanism under the current baseline and how do you believe it would affect system balancing? (Section 1.7)	Failure to deliver instructed actions would expose participants to a less punitive non delivery charge. This may reduce some of the risk perceived when submitting bid/offer price ladders and have the duel effect of increasing reducing the margin between SBP and SSP should the volume of accepted bid and offers remain the same.
6.	In your opinion, how do you believe Modification Proposal P74 would affect the level of part loading seen under the current arrangements and in what way do you believe it would be more or less efficient for participants and for the system as a whole? (Section 1.8)	Actions that may be taken to increase load in gate closure without instruction from NGC are limited. The incentives for participants to enter gate closure part loaded depends primarily on the perceived rewards of instructed actions. P74 potentially mitigates the risk of exposure to non delivery charges and hence may encourage more parties to enter the Balancing Mechanism at part load seeking income from instructed actions
7.	In your opinion, does Modification Proposal P74 change the incentives to deviate from FPN over the current baseline, if so, how and why? (Section 1.9)	Generators who believe they may obtain SBP (rather than SSP) through increasing the load from FPN (without instruction from NGC) will have a greater incentive over the current position and payment at SSP.
8.	In your opinion, (noting the forthcoming implementation of Modification P12 to reduce Gate Closure to one hour), does Modification Proposal P74 increase the incentive on parties to change Physical Notifications shortly before Gate Closure and do you believe this to be a good or bad thing? (Sections 1.9, 1.11, 1.12, 1.13)	P74 increases the incentive for parties to take notified actions. As the incentive to self balance is less pronounced, the incentive on parties to maintain accurate FPNs is reduced. With gate closure moving to one hour this is undesirable as NGC will have less time to take more actions to correct variance from the FPN position.
9.	In your opinion, to what extent will Modification Proposal P74 address the issue of asymmetric risk? (Section 1.10)	Short term power requirements have to be met by flexible power generators or demand management mechanisms. Such resources generally have low utilisation and have to recover fixed costs (rent) over a shorter period of running hours. The Bid Offer spread needs to be maintained to remunerate short term flexible resources. Firm prices signals are required to incentivise participants to invest in such resources and maintain their operational viability. P74 potentially gives less incentive to participants to self balance,

Q	Question	Response (Please provide rationale where possible)
		especially if faced with short term power bid offer spreads shortly before gate closure. This would increase the volume of short term power bid/offer acceptances. This would have the effect of increasing the long and short stack. It does not seem to reflect the issue that actions to increase load at short notice are different from actions to decrease load at short notice.
10.	In your opinion, do you believe that Modification Proposal P74 will change the incentives on parties to balance their individual (contractual) trading positions before Gate Closure, if so, how and why? (Sections 1.12 and 1.13)	The incentives on Parties to self balance before gate closure will be reduced as the exposure to punitive dual cash out prices is reduced. Furthermore, parties (with for instance those with large volumes of excess and flexible generating capacity) will have the capability of manipulating the market position by changing between IPN to FPN positions. This will make NGCs role more challenging upon movement of gate closure to one hour before real time. A variance in IPN to FPN may increase the volume of balancing mechanism activity. This may further incentivise owners of excess flexible generating capacity to manipulate the mechanism and realise enhanced income from balancing mechanism activity.
11.	In your opinion, do you believe that Modification Proposal P74 will change the incentives for parties as a whole (i.e. in total, even if not balanced on an individual basis) to balance the market as a whole before Gate Closure, if so, how and why? (Section 1.11)	Yes. There are less incentives to balance due to the potential cash out prices being less punitive.
12.	In your opinion, does Modification Proposal P74 lead Parties to anticipate the 'direction' of the market, and therefore the Energy Imbalance Price. Could this lead to volume volatility and consequential price instability in the market? (Sections 1.12 and 1.13)	Yes. Parties with the correct profile (i.e. Large volumes of flexible, low utilisation excess generating capacity) may also attempt to manipulate the “direction” of the market, especially at peak periods when the SBP- SSP margin is most pronounced. Plants with load restrictions due to environmental constraints could also be used to manipulate the market in this way.

Q	Question	Response (Please provide rationale where possible)
13.	What effect do you think Modification Proposal P74 will have on liquidity and prices in the forwards and spot markets, the interrelation of forwards and spot markets with Energy Imbalance Prices and also the level of Energy Imbalance Prices themselves? (Sections 1.14, 1.15 and 1.16)	P74 has the effect of reducing the incentives to self balance. Portfolio players and vertically integrated players who currently retain flexible capacity to manage their own delivery and supply risk may be more willing to offer such capacity in the day ahead markets, hence increasing liquidity. This will be due to the lower risk of exposure to the dual cash out prices and potential guaranteed benefits of power revenues in the dayahead market. However, the bid offer spread in the dayahead market will be more distorted than at present. Power sales at short notice prior to gate closure would still need to be fulfilled by flexible plant. This plant could obtain high prices in the Balancing Mechanisms and hence parties would be unwilling to sell volumes from such plant at prices significantly lower than that they may obtain in the Balancing Mechanism. Parties seeking power may choose to take their chances on the direction of the single imbalance charge rather than pay such prices prior to gate closure and enter gate closure in Balanced position. Plants that are able to respond within one hour are the most flexible and generally the most expensive, hence, the overall “system” cost of fulfilling the imbalance will be increased due to a later balancing action being required. Furthermore P74 would make the short term markets more imperfect than the status quo as the price transparency will be more opaque and parties responsible for an imbalance in a direction will not be responsible for the costs of actions to rectify the imbalance.

Q	Question	Response (Please provide rationale where possible)
14.	Do you believe that the implementation of Modification Proposal P74 will encourage the development of risk management products and new types of contracts, and what effect do you think this will have on competition and the efficiency of the forwards and spot markets? (Sections 1.17, 1.18, 1.19 and 1.20)	P74 would actively discourage the development of risk management products and new types of contracts for third parties. It allows portfolio players and vertically integrated players to strengthen their influence over short term power markets, and increases their income from such activity at the overall expense of the system and eventually the customer. They have more perfect information and greater price transparency due to their internal position. Such portfolio players currently are able to enjoy the benefits of internal risk management products. Reducing the perceived margins in providing risk management services such as Consolidation will discourage market entry by Independent Service Providers. Influence of short term power prices allows a party a trading advantage in the forward markets. An imperfect short term market distorts the forward market as parties seek to maximise their income and mitigate risk. As mentioned above P74 makes the short term market more imperfect and makes price transparency more opaque.
15.	In your opinion what would be the impact on the risk profile of different categories of party (as listed in section 1.21) from the implementation of Modification Proposal P74? (Section 1.21)	• small suppliers- Overall increased risk • Large suppliers- Decreased risk • LEGs- Overall increased risk • Unpredictable generators- Overall increased risk • Non portfolio generators- Overall increased risk • Portfolio generators- Decreased risk • Vertically integrated players- Decreased risk • Non Physical Traders- increased risk and consolidation is discouraged • Transmission Company- increased risk
16.	Do you believe that Modification Proposal P74 better facilitates achievement of the Applicable BSC Objectives, if so, which one(s) and why?	No. It has the opposite effect.

Q	Question	Response (Please provide rationale where possible)
17.	Do you believe that an Alternative Modification Proposal better facilitates achievement of the Applicable BSC Objectives than Modification Proposal P74, if so, what is it? (Section 1.23)	No
18.	Are there any other issues not identified in the supporting document which you believe should be considered during the assessment of Modification Proposal P74.	Portfolio Players and vertically integrated players currently have the ability to employ internal Risk Management Strategies both within gate closure and prior to gate closure. P74 moves this advantage over independent players to the dayahead market and to earnings that may be realised from the Balancing Mechanism. In a perfect market independent service providers would be able to deliver services (and benefits) to small and independent players comparable with those naturally realised by portfolio and vertically integrated players. P74 discourages the emergence of such service providers.
19.	Do you believe that further analysis / modelling is required over that currently identified by the PIMG (in the supporting document), and if so, what specific form should this take?	OFGEM is currently endeavouring to encourage players to enter the market as independent consolidators. P74 would actively discourage such market entry.