



Direct Dial: 020-7901 7412  
11 June 2002

The National Grid Company, BSC Signatories and  
Other Interested Parties

Your Ref:  
Our Ref: MP No: P59

Dear Colleague

**Modification to the Balancing and Settlement Code ("BSC") - Notice in relation to  
Modification Proposal P59: "The Acceptance of Bids and Offers to Honour a BM Unit's  
Dynamic Parameters Beyond the Balancing Mechanism Window"**

The Gas and Electricity Markets Authority (the "Authority") has carefully considered the issues raised in the Modification Report dated 26 April 2002 for Modification Proposal P59 "The Acceptance of Bids and Offers to Honour a BM Unit's Dynamic Parameters Beyond the Balancing Mechanism Window".

The BSC Panel (the "Panel") recommended to the Authority that the Proposed Modification P59 should be rejected.

The Authority has decided not to direct a modification to the BSC. This letter explains the background to the Modification Proposal and sets out the Authority's reasons for its decision.

**Background to the proposal**

In accordance with the Grid Code, NGC are only able to issue Bid-Offer Acceptances ("BOAs") for periods up to the end of the Balancing Mechanism window (the "wall"). If no subsequent BOA is issued, then "beyond the wall", the Balancing Mechanism Unit ("BMU") can be left in imbalance if the BMU's physical parameters prevent it from returning to its Physical Notification ("PN") instantaneously.

The "beyond the wall" issue has existed since NETA Go-Live.<sup>1</sup> To address this issue and encourage participation in the Balancing Mechanism, NGC operated an informal agreement

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<sup>1</sup> NETA Go-Live was the 27 March 2001.

with BMUs. At the time that the BOA was issued, NGC agreed with the BMU that before the BMU reached the “wall”, NGC would issue a further BOA (consistent with submitted dynamic parameters) to return the BMU to its original PN level. This was provided that the BMU did not submit any revisions to its costs or other parameters in the meantime.

On 28 September 2001 NGC started a consultation process seeking views on the “beyond the wall” issue and how it should be addressed. With consideration to respondent’s views NGC believed that modifying the Balancing Principles Statement (“BPS”) to formalise how it currently deals with the situation was the appropriate solution. On the 12 February 2002 NGC initiated a further consultation with industry participants on a proposed revision to the BPS to include provisions for addressing the “beyond the wall” issue to which there was split support for and against the proposed revisions. On the 26 February 2002 the Authority approved NGC’s proposed revisions to the BPS to address the “beyond the wall” issue in a BPS Supplement. NGC proposed incorporating the BPS supplement within the BPS effective from 1 May 2002 as part of the annual review of the BPS. The Authority approved NGC’s proposed revisions to the BPS on the 1 May 2002.

On the 3 December 2001 Innogy raised Modification Proposal P59 “The Acceptance of Bids and Offers to Honour a BM Unit’s Dynamic Parameters Beyond the Balancing Mechanism Window”. The Proposer suggested that NGC is not obliged to return a Unit to its PN “beyond the wall” in accordance with its dynamic parameters and Parties are therefore discouraged from participating in the Balancing Mechanism due to the risk of being left out of balance “beyond the wall”. The Proposer suggests that formalising arrangements for BOAs that would extend “beyond the wall” within the BSC would remove this risk, improve transparency and encourage participation in the Balancing Mechanism.

### **The Modification Proposal**

Modification Proposal P59 seeks to further the achievement of the applicable BSC Objectives<sup>2</sup> (b) the efficient, economic and co-ordinated operation of the Transmission System by the Transmission Company and (c) of effective competition in the generation and supply of electricity. The modification proposes formalising the agreement that NGC will continue to accept Bids and Offers to honour a BMU’s dynamic parameters “beyond the wall” within the BSC. The Modification Proposal would require changes to NETA Central Systems to automatically calculate the BMU’s Cashflows, and subsequent Energy Imbalance Prices, using Bid-Offer Prices submitted for a prior Settlement Period.

During the Assessment Phase the Modification Group (the “Group”) considered that an automatic solution requiring changes to BSC Systems would create additional complexity and would not better facilitate the achievement of the applicable BSC Objectives. The Group

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<sup>2</sup> The relevant BSC Objectives are contained in Condition C3.3 of NGC’s Transmission Licence and are:

- (a) the efficient discharge by the licensee of the obligations imposed upon it by this licence;
- (b) the efficient, economic and co-ordinated operation by the licensee of the licensee’s transmission system;
- (c) promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity;
- (d) promoting efficiency in the implementation and administration of the balancing and settlement arrangements.

proposed a potential Alternative Modification which places an obligation in the BSC on NGC to formalise the informal agreement rather than implement major BSC Systems changes as per the Proposed Modification.

The effect of the potential Alternative Modification Proposal was judged to have the same effect as NGC's proposed revision to the BPS to formalise the informal agreement. However the Group felt there was merit in placing the obligation in the BSC for the reasons that:

- it is more transparent to have the obligation within the BSC;
- there is a material risk to Parties being left out of balance due to balancing actions taken by the System Operator;
- the BSC Modification process ensures that any further changes would better facilitate the achievement of the applicable BSC Objectives; and
- the process for disputing a BOA is clearer within the BSC and would allow Settlement rules to be amended if necessary.

At the Panel's meeting of the 14 February 2002 the Panel considered the Interim Report and the consultation document issued on 6 February 2002 as part of the Assessment Procedure for Modification Proposal P59. The Panel noted that the Group was progressing a potential Alternative Modification and that the effect was similar to NGC's proposed changes to the BPS. The Panel agreed to seek the Authority's provisional thinking on the governance structure proposed under the potential Alternative Modification and to postpone a decision on whether further work should be undertaken on the assessment of the Proposed Modification until after the provisional thinking had been received.

On the 26 February 2002 the Authority gave its provisional thinking on Modification Proposal P59. In the provisional thinking Ofgem<sup>3</sup> considered that on the basis of the analysis undertaken by the Group so far, the informal agreement should not be formalised in the BSC. Ofgem considered that the issue has been appropriately addressed by the implementation of NGC's proposed revisions to the BPS. Additionally, Ofgem considered that the proposed revisions to the BPS removes the risk of imbalance exposure should a BMU be out-of-balance at the "wall" and addresses concerns that this risk may have discouraged participation in the Balancing Mechanism.

The Panel considered Ofgem's provisional thinking at their meeting on the 14 March 2002. The Panel noted the Authority's provisional thinking, in particular, that the Authority believed that the "beyond the wall" issue has been addressed through NGC's BPS. The Panel agreed that Modification Proposal P59 should proceed to the Report Phase with a recommendation that the Proposed Modification should be rejected. ELEXON published a Draft Modification Report on 27 March 2002 which invited respondents' views by 9 April 2002.

### **Respondents' views**

In total, ELEXON received 14 responses on the Draft Modification Report. Of the responses, 7 supported the recommendations in the Modification Report, 6 did not and one did not comment.

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<sup>3</sup> Ofgem is the office of the Authority. The terms "Ofgem" and "the Authority" are used interchangeably in this letter.

Respondents did not support the original Modification Proposal with some respondents commenting that it would not be efficient to implement an automated solution.

The respondents that agreed with the Panels recommendation to reject the Modification Proposal considered that the formalisation of the issue in the BPS has the same effect as the potential Alternative Modification Proposal. Respondents also considered that although they would prefer to see an obligation in the BSC, they were supportive of avoiding further costs in assessing the Modification Proposal given that the Authority had already approved changes to the BPS.

The respondents who did not support the recommendations considered that it is more appropriate that the obligations sit within the BSC rather than the BPS as they felt this would provide greater transparency, clarity, efficiency and a clear process for dispute resolution. A minority of respondents considered that the Assessment Process should not have been curtailed.

### **Panel's Recommendation**

The Panel met on 18 April 2002 and considered the Draft Modification Report and the consultation responses received.

The BSC Panel (the "Panel") recommended to the Authority that the Proposed Modification P59 should be rejected.

### **Ofgem's view**

Ofgem considers, having had regard to its statutory duties, that the Proposed Modification does not better facilitate the achievement applicable BSC Objective (d) by promoting efficiency in the implementation and administration of the balancing and settlement arrangements.

Ofgem considers that neither the Proposed Modification, which involves an automatic solution that would require changes to BSC Systems, or the potential Alternative Modification would be efficient given that the "beyond the wall" issue has already been appropriately addressed in the BPS Supplement.

The purpose of the BPS is to set out the principles and criteria by which NGC uses Balancing Services and aims to assist BSC participants in understanding NGC's actions in achieving the efficient, economic and co-ordinated operation of the transmission system. Ofgem considers that incorporating the proposed changes into the BPS is appropriate, as it will ensure that a complete set of the principles and criteria used by NGC when selecting Balancing Services is included within this framework. Ofgem therefore considers that the "beyond the wall" issue is most appropriately addressed as part of the BPS.

Ofgem considers that the BPS Supplement effective from the 26 February 2002 removes the risk of imbalance exposure should a BMU be out-of-balance at the "wall" and addresses concerns that this risk may have discouraged participation in the Balancing Mechanism. Ofgem considers that formalising the informal agreement via the proposed changes to the BPS enhances the clarity of the BPS and improves transparency for BSC Parties.

Ofgem has noted that the Group believed that there might be inadequate arrangements to enable revisions to the BPS other than at the time of the annual review conducted in accordance with the Transmission Licence. However, licence amendments through Section 11(1) of the Electricity Act 1989 were implemented with effect from the 1 April 2002. The licence amendments to Special Condition AA4 of the Transmission Licence establish a governance structure that allows modifications to the BPS within year.

### **The Authority's decision**

The Authority has therefore decided not to direct that the Modification Proposal P59 as set out in the Modification Report dated be made or implemented.

Having regard to the above, the Authority, in accordance with Section F1.1.4 of the BSC, hereby notifies NGC that it does not intend to direct NGC to modify the BSC as set out in Modification Proposal P59.

Please do not hesitate to contact me on the above number if you have any queries in relation to the issues raised in this letter or alternatively contact Anthony Doherty on 020 7901 7159.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Sonia', with a stylized flourish at the end.

**Sonia Brown**

**Head of Electricity Trading Arrangements**

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