Responses from P212 Assessment Report Consultation

Consultation Issued on 15 August 2007

Representations were received from the following parties

No	Company	File number	No BSC Parties Represented	No Non-Parties Represented
1.	RWE Npower	P212_AR_01	11	0
2.	SmartestEnergy	P212_AR_02	1	0
3.	EDF Trading	P212_AR_03	1	0
4.	National Grid	P212_AR_04	0	0
5.	Centrica	P212_AR_05	9	0
6.	E.ON UK plc	P212_AR_06	7	0
7.	EDF Energy Plc	P212_AR_07	9	0
8.	Scottish and Southern Energy plc.	P212_AR_08	6	0
9.	Combined Heat and Power Association	P212_AR_09	0	0
10.	Scottish Power	P212_AR_10	7	0
11.	Uskmouth Power Limited	P212_AR_11	1	0
12.	Immingham CHP LLP	P212_AR_12	2	0
13.	APX	P212_AR_13	2	1
14.	Drax Power Limited	P212_AR_14	1	0
15.	Airtricity	P212_AR_15	1	0
16.	International Power	P212_AR_16	5	0
17.	InterGen (UK) Ltd	P212_AR_17	4	0
18.	E.ON UK Energy Services Limited	P212_AR_18	0	1
19.	The Renewable Energy Co Ltd	P212_AR_19	1	0
20.	BizzEnergy Ltd	P212_AR_20	1	0
21.	British Energy	P212_AR_21	5	0

P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	**Richard Jones**
Company Name:	**RWE Npower**
No. of BSC Parties Represented	**11**
Parties Represented	*Please list all BSC Party names of Parties responding on behalf of (including the respondent company if relevant).* **RWE Trading GmbH, RWE Npower plc, Great Yarmouth Power Ltd, Npower Cogen Trading Ltd, Npower Commercial Gas Ltd, Npower Direct Ltd, Npower Ltd, Npower Northern Ltd, Npower Northern Supply Ltd, Npower Yorkshire Ltd, Npower Yorkshire Supply Ltd**
No. of Non BSC Parties Represented (e.g. Agents)	**None**
Non Parties represented	*Please list all non Parties responding on behalf of (including the respondent company if relevant).*
Role of Respondent	*(Supplier/Generator/ Trader / Consolidator / Exemptable Generator / BSC Agent / Party Agent / Distributors / other – please state* [1]*)* **Supplier/Generator/ Trader / Consolidator / Exemptable Generator / Party Agent**
Does this response contain confidential information?	**No**

Q	Question	Response [1]	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	We believe the aim of imbalance prices under the BSC is to recover the costs incurred by the SO in balancing the system by reflecting those costs back onto the Parties that give rise to that imbalance.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	Cost reflective cash out prices should result in an economic and efficient outcome in terms of energy balancing (minimising BSUoS costs), in the marginal cost of energy in the forward market and the market signals for new entry (e.g. investment in new power stations).

[1] Delete as appropriate – please do not use strikeout, this is to make it easier to analyse the responses

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Q	Question	Response [1]	Rationale
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes/No	There is no doubt that cash out prices are influenced by activities other that straightforward energy balancing during certain settlement periods. However, the scale and extent of any problems in setting cash out prices is not immediately transparent to the market as a whole and further work may be required to demonstrate that the impact of these actions is significant.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	A more simplistic methodology for calculating cash out prices may be desirable. However, 'simplicity' should not be delivered at the expense of 'cost-reflectivity'. It is important that the costs associated with imbalance, are reflected on to those Parties who give rise to the imbalance.
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	We believe a fixed percentage (specifically 5%) will dampen cash out prices, making them benign and less cost reflective, resulting in weaker and less accurate signals to Parties than the current methodology, particular at times of system stress. Given our response to Question 1, and the fact that we believe imbalance prices should reflect the costs incurred by the SO (and not the short term market cost of electricity), applying a premium to the MIP is not necessarily accurate or reflective of imbalance prices and the true cost of balancing the system.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Although we note that Option 2 endeavours to improve on Option 1 by providing different percentages for different periods in an attempt to more accurately reflect times of system stress, this adds greater complexity to the methodology (something the Proposer is attempting to avoid). Also, the fundamental issue of applying a premium to the MIP as discussed above still exists.

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Q	Question	Response [1]	Rationale
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Option 3 suffers from the same issues described in our responses to Questions 5 and 6, plus; ▪ the concept of having a different percentage for each individual settlement period is incredibly complex (again something the Proposer is attempting to avoid) ▪ NIV is not necessarily related to system stress, therefore there is a significant risk in market participants receiving wrong or weak market signals We also note that no historical analysis has been carried out by the P212 Working Group in relation to Option 3 and that any historical analysis done would not be able to reflect changes in market participant behaviour.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: 2nd Preference: 3rd Preference: No Preference: Since we do not believe that any of the options provide an economic and efficient outcome we do not support implementation of any of them. However, a pragmatic solution could be option 1 if P212 is designed to deliver an incentive to trade ahead of gate closure.
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	We believe that market participants will be less incentivised to balance as cash out prices will be dampened in relation to current methodology and as a result far less penal. In turn this will put more pressure on the SO who will have to take more actions than it does currently. With cash out prices being more benign the SO will have to recover its costs elsewhere (BSUoS).
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	We expect that market participants would become more incentivised as the percentage premium increases and cash out prices become more penal.

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Q	Question	Response [1]	Rationale
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	As stated in our response to Question 9, our view is that the impact under all three Options is for the SO to face an increase in costs in balancing the system, as market participants will be less incentivised to balance their position compared to the current methodology.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	This is a pragmatic approach that, when relevant will allow debate and views from group members in relation to changes in the pricing value/methodology.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	
14.	Are there any further comments on P212 that you wish to make?	No	

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Colin Prestwich*
Company Name:	*SmartestEnergy*
No. of BSC Parties Represented	*1*
Parties Represented	*SmartestEnergy*
No. of Non BSC Parties Represented (e.g. Agents)	
Non Parties represented	
Role of Respondent	*Supplier/Trader / Consolidator*
Does this response contain confidential information?	*No*

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	Under NETA the aim of imbalance prices is to pass the costs of energy imbalance to those who cause the imbalance. We do not believe this principle has changed or should change. If the charging is suitably targeted, this should provide the correct incentive to balance, but this is secondary; if the costs are not high, the incentive should not be high i.e. there is no rationale for an incentive per se.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	The question should be one of whether you have achieved greater transparency whilst at the same time, not overly influenced the incentives to balance. This could be reported on by NGT.

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Q	Question	Response	Rationale
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	The extent of the "defect" was presented by NGT at the Ofgem industry meeting on 30th March as being, for the month of November 2006, SBP 9% higher than ideal and SSP 7% lower than ideal. This has led certain industry commentators to talk about "massive pollution." NGT, on the other hand, have since stated in the Modification Group that they think the answer is actually somewhere between the stated percentages and zero. In either event, we do not consider this to be massive pollution, especially when it is taken into account that the costs of reserve (which would not be necessary if everyone was in perfect balance) are not included in the current definition of energy costs. There is, however, no "correct answer" when trying to split out energy and system costs. The important thing here is to ensure that the monies changing hands are more or less reflective of the costs. We would say that at present they currently are; P78 introduced the most important change to make imbalance prices more realistic, but we also see the other pricing modifications over the years as good refinements which have brought about an overall satisfactory arrangement. The question we are faced with is whether this should be sacrificed for greater transparency/simplicity.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	Simplicity and cost reflectivity are both important desirable features of the arrangements. We believe that greater simplicity can be achieved so long as the costs are broadly in line with those being incurred by the system operator. This means that if the arrangements remove the link between imbalance prices and the costs it is extremely important to review whether the resulting prices are reflective of costs on a regular basis.

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	The fixed percentage of 5% quite clearly, in our view, will neither provide an adequate percentage, nor reflect the costs of imbalance especially at the appropriate times. No evidence has been provided which supports the use of this randomly low variable. There has been talk that 5% is a significant proportion of an energy cost which parties would wish to optimise. However, we are talking here of residual volumes of imbalance and not full contracted volumes. Taken across full contracted volumes the percentage would appear considerably smaller (and getting into the realms of not worth bothering with). This would lead to a lack of an incentive to balance and would throw the costs of energy balancing onto NGT and would then be smeared through BSUoS.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Potentially yes	We believe the profiled percentage approach, especially with the percentages given, would achieve imbalance prices of about the right order. It is important, however, to monitor the impact on behaviour if and when change is made so that percentages may be tweaked accordingly.
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Potentially yes	The dynamic approach is certainly worthy of further investigation. It does get round the problem of parties trading around a known price. (Although, this is less of an issue if the percentages are significantly greater than the 5%) However, we suspect that the average factor needs to be of the order of 20%, not the 5-10% which would be achieved by multiplying NIV/Dem by a factor of 10. We suspect this factor needs to be nearer 30
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: Option 2
			2nd Preference: Option 3
			3rd Preference: Option 1
			No Preference:

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Q	Question	Response	Rationale
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	As stated, the incentive to balance would virtually disappear and NGT would need to take more balancing actions which would feed through into BSUoS
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	There would be a greater incentive to balance the greater the percentage. This percentage should not be greater than that required to achieve a level of energy balancing broadly in line with that currently experienced. However, it is vital that the percentage varies such that it is greater at times of system stress.
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	As already stated Option 1 would increase the SO's costs of balancing the system. Options 2 and 3 may have the effect of increasing them slightly even if they were set at about the right level as there would not be a direct relationship to the costs incurred at exactly the right time. Option 4 (see below) would probably increase the SO's costs of balancing. However, we would question whether not increasing costs is compatible with the changes being proposed. It is inevitable in creating greater transparency and a division between system and energy actions that there would be an associated inefficiency. This may mean that the percentages may have to be higher than analysis of current behaviour would indicate.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	No	This process may need to be more dynamic and as such the Panel should be empowered to tweak the percentage.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	Yes	SmartestEnergy believes there is merit in further consideration of developing a market for energy imbalance within gate closure. For this to work correctly, however, NGT should not be allowed to trade energy imbalance in the APX.

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Q	Question	Response	Rationale
14.	Are there any further comments on P212 that you wish to make?	Yes	This is a finely balanced issue and it is difficult to come to any firm conclusions at this stage over whether it is worth sacrificing cost reflectivity for simplicity. To a certain extent, this modification needs to be seen in the context of other issues and we are also keen to see the results of other modelling before taking a firm view.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	Vincent Baslé
Company Name:	EDF Trading
No. of BSC Parties Represented	1
Parties Represented	EDF Trading Limited
No. of Non BSC Parties Represented (e.g. Agents)	0
Non Parties represented	N/A
Role of Respondent	Senior Analyst
Does this response contain confidential information?	No

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	Imbalance prices should provide parties with an incentive to trade ahead of gate closure and provide a reference price for energy balancing
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	There is a wealth of information available suggesting that imbalance price pollution is a significant problem, and that this is having the effect of sending inappropriate signals to the forward market. National Grid's analysis presented at the cash out working group meeting in March 2007 conclusively shows that the current cash out methodology is not producing anything close to a "clean" energy price. Similar analysis during the assessment of P205 showed similar results.

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Q	Question	Response	Rationale
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Real-time situations can occur that can be different from the initial guess made on day-ahead (which eventually helps form the reference price). The system can be longer or shorter than expected, and so imbalance prices should reveal this signal. There is no clear indication on how stressed the system is on a market based price.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	See answer to Question 5.
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	See answer to Question 5.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: 2nd Preference: 3rd Preference: No Preference:
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	See answer to question 5.

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Q	Question	Response	Rationale
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	No	
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	This is difficult to asses, but it should be noted that the modification is not proposing changes to the way that the SO balances the system so the effect should not be that significant.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	
14.	Are there any further comments on P212 that you wish to make?	No	

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	Rob Smith
Company Name:	National Grid
No. of BSC Parties Represented	
Parties Represented	
No. of Non BSC Parties Represented (e.g. Agents)	
Non Parties represented	
Role of Respondent	Transmission Company
Does this response contain confidential information?	

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	An efficient imbalance price should provide sufficient information to allow market participants to accurately economically determine whether they, or the system operator, can more efficiently resolve each MWh of the energy imbalance on the system in any settlement period

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Q	Question	Response	Rationale
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	We have concerns, as expressed in answers to the subsequent questions in this response, that the proposed imbalance price does not seek to better reflect the cash out aims as defined above. However we have tried to think about how to measure success in terms of our interpretation of the proposers perception of the aims of an imbalance price. This, by its very nature is a very difficult question and is unlikely to yield a completely accurate answer. Consequentially any method for measuring success will suffer from some degree of inaccuracy. However we believe the closest methodology for measuring the success of the aims stated by the proposer is to construct a unconstrained schedule that mimics the activity the activity the SO would have undertaken if it was in a fictitious position of only having to procure half hourly energy blocks up to the value of NIV. In constructing this unconstrained schedule, determinations would have to be taken on how much real world credibility should be included with the methodology. Considerations would have to include the incorporation of plant dynamics and inter half hours issue to determine how reflective this stack should be.
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	In order to answer this question it is necessary to understand what the proposer defines as a defect. If our understanding is correct then any action that does not mimic the procurement of a notional half hour aggregated volume of energy equivalent to the value of NIV is deemed to be pollution and should not be included in the imbalance price. If this definition is applied in assessing the activity undertaken to balance the system then a large proportion of the actions undertaken by the SO would fall into this category. Although not conclusive, analysis we have provided previously has estimated that in the year 06/07 approximately 70 percent of offers and 60 percent of bids that were used to resolve NIV were also used to manage other issues faced by the SO in balancing the system. Namely actions taken to create reserve, actions taken to create response provision, intra half hour demand shapes and actions taken to resolve constraint issues. However it is important to differentiate between the reasons activity was undertaken and the impact that activity had on altering the imbalance price. A large proportion of activity taken to resolve the issues indicated would be taken in cost order. Again although not conclusive, this is demonstrated in the analysis provided to the cash out review meeting in March 2007 that roughly estimated that in November 2006 the average differential in costs that this activity caused had in relation to resolving a notional half hourly demand position was somewhere between 0 and 9% difference in the cost of offers accepted and somewhere between 0 and 7% difference in the cost of bids accepted.

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Q	Question	Response	Rationale
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	We do not believe that simplicity by itself is a measure on which to base the appropriateness of an imbalance price. Fundamentally an imbalance price should strive to be reflective of a determined set of costs or create incentives to drive behaviour in a desired direction. If these objectives can be achieved through an imbalance price that is simple then this is a substantial extra benefit that is likely to aid access to the market. However we do not believe it should be adopted at the expense of an imbalance price methodology that appropriately incentives parties to act in a particular manner. If this happens it simply creates an inaccurate cross subsidy of costs with inappropriate winners and losers and ultimately an inefficient market.

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Whilst we understand that there are plans to progress further analysis on this proposal which may alter our position on this modification, we currently have some concerns relating to this modification that have not been allayed by the discussions or analysis noted in the consultation document. This modification makes two fundamental changes to the manner of the imbalance price calculation and it is the implications of this that must be understood. Firstly it effectively changes the imbalance price from being Ex-Post to Ex-Ante. Out concern is that Ex-Ante pricing may not reflect the characteristics of the system at real time. There can often be a considerable difference between the forecast position of NIV and the outturn level at real time as demonstrated by within gate plant loss and gain and supplier forecast error. This limits the ability of the forward price to mimic the real time characteristics of the system as it will not capture any within gate volatility and cost. This will in turn have an impact on the incentive to balance. The change in short term risk will impact on the risk mitigation strategies of participants. Given that likely imbalance exposure informs the appetite for participants to risk going short, a change in this risk may have implications for the level of imbalance that participants are willing to carry into the balancing mechanism. It will also fail to reflect the increase or decrease in costs that participants may cause the SO to incur by their behaviour post gate closure. This cost or benefit is, instead, socialised across the whole BSC participant community. This then raises questions regarding the incentive to invest in plant reliability. Secondly it decouples the link with setting the price on actions taken by or available to the System Operator. The forecast of imbalance prices are a strong driver in the risk management trading strategies of most market participants. In order that this “price to beat” is appropriate it needs to be a proxy for the opportunity cost participants would incur if they were able to resolve their contract positions post gate closure. The proposed P212 methodology divorces this link and relies on the fact that forward trades will also effectively act as the opportunity cost of itself. In such an event the incentive to trade switches from being related to the expectation of SO costs and associated energy scarcity. Instead it becomes dependent on a large number of interacting factors whose variability may not always correlate with the cost of energy scarcity. (Continued in Any other comments section 14)

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Q	Question	Response	Rationale
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Option 2, similarly to the original proposal, makes two fundamental changes to the imbalance price methodology. We recognise that option 2, unlike the original, provides a rationale for the percentage offsets to MIDP in that it attempts to reflect the aggregate cost differential between forward prices and imbalance prices. Unfortunately those values will be based on historic aggregated analysis and so will still suffer from an accuracy problem in attempting to reflect the level of energy scarcity and associated SO balancing costs that occur in any particular settlement period. In relation to the facilitation of the applicable BSC objectives our view is the same as in relation to the original

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Q	Question	Response	Rationale
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Unknown	The imbalance price proposed under Option C is derived Ex Post. This has the advantage of allowing the price to be reflective of the activity, or a proxy for the activity, that has been undertaken to enable the balancing of the system up to real time. This proposal also introduces a component that aims to incorporate the characteristics of the market in that particular settlement period by linking the premium or discount to the length of NIV. We have assumed that the rationale behind this methodology is that the forward market price, although cheaper than the cost of resolving NIV, will be correlated with that cost. The premium added will then reflect the differential between these two costs. This model presents us with two questions. Will this methodology prompt the forward market to respond to the relative scarcity in the market in any particular period? Secondly, can we construct a NIV size, percentage premium, ratio that can appropriately reflect the difference in these costs in each half hour? One point that we feel merits further investigation is the two opposing forces that forward trading exerts on this methodology. We would invite the modification group to consider the following scenario. A participant is short in a short market and is exposed to SBP. If the next MW being offered in the forward market is higher than current expectation of MIDP will that participant trade. By trading the participant raises the value of MIDP but reduces the value of NIV. In this scenario the participant must make a complex assessment to determine if trading is the correct economic move. As yet there is no analysis to help draw a conclusion on the likely behaviour in such scenarios and as such it is difficult for us draw a conclusion on how this methodology will drive behaviour and how it will perform in relation to facilitation of the applicable objectives. We would welcome some further exploration of this proposal to better understand it. At present we are unable to ascertain whether this will better facilitate the applicable objectives
8.	What is your order of preference of Options 1, 2 and 3 for forming	-	1st Preference: Further investigation of Option 3
			2nd Preference:
			3rd Preference:

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Q	Question	Response	Rationale
	the Proposed Solution? Please provide rationale.		No Preference: option 1 & option 2
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	As noted in our response to question 5 it is our initial view that the implementation of this modification could result in the incentive to balance changing. If the average price of imbalance is reduced as is suggested by the analysis provided then the economic incentive for participants to manage their energy position, and consequentially the behaviour of NIV will also change. However it is not certain how predictable such changes in NIV will be. We have concerns that P212 may bring more volatility in the value of NIV as much as significant change in its average length. As such it is difficult to predict how the SO will respond to such changes. However it is likely that if P212 leads to greater volatility and unpredictability then there will be an associated cost to the SO in resolving the energy imbalance on the system
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	As the percentage premium of and discount applied to P212 increases the opportunity cost of imbalance becomes greater. As such the incentive to balance also becomes greater. However this is not the same as an appropriate incentive to balance.

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Q	Question	Response	Rationale
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes/No	See response to question 5
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes/No	Yes – Changes to the values in the methodology would have a significant impact on BSc parties and there subsequent behaviour, As such any proposal to change it should be robustly assessed by the industry.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	We believe the most appropriate place to discuss the fundamental aims, objectives and necessary trade offs relating to imbalance price methodologies should be considered either at the OFGEM Cash Out review or at a BSC issue group. A more overarching discussion and assessment of what the imbalance price needs to, and can pragmatically, achieve would then allow the submission of more rounded, holistic, cash out methodology proposals.

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Q	Question	Response	Rationale
14.	Are there any further comments on P212 that you wish to make?	No Please note this text is a continuation to Question 5 and is not a response to question 14	In relation to the 5% specifically it is difficult to say whether this value has any greater or lesser validity than any other arbitrary percentage figure. In as much as the analysis carried out already can assist in our assessment of the appropriateness of this number it does not seem to reflect the differential between the cost of energy in the forward market and that procured by the SO even when comparing against the P211 price mechanism. Therefore we believe the P212 original will increase volatility at odds with market characteristics and this volatility will erode the efficiency of System Operation and so is detrimental to BSC objective B. This methodology is certainly simpler than the current methodology and it will not suffer from the perception that system actions are influencing the price. As such it may encourage market entry. However if the P212 price is not reflective of costs parties will not be made responsible for the costs they incur. In this scenario it is difficult to see how this better facilitates market competition. As such we do not believe it will better facilitates objective C. This price will be simpler to calculate and so, in terms of the administration surrounding the settlement process, it will better facilitate BSC objective D

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Dave Wilkerson*
Company Name:	*Centrica*
No. of BSC Parties Represented	*9*
Parties Represented	Accord Energy Ltd; British Gas Trading Ltd; Centrica Barry Ltd; Centrica Brigg Ltd; Centrica KL Ltd; Centrica KPS Ltd; Centrica PB Ltd; Centrica RPS Ltd; Centrica SHB Ltd
No. of Non BSC Parties Represented (e.g. Agents)	*-*
Non Parties represented	
Role of Respondent	*(Supplier/Generator/ Trader)*
Does this response contain confidential information?	*No*

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Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	The aim of cashout prices is to incentivise parties to balance their own position at gate closure. It is generally more efficient for parties to balance their own portfolio than for the SO to do it on their behalf. Therefore, the costs incurred by the SO on behalf of parties in imbalance should be reflected back on those parties causing the imbalance. The amount that is targeted back should be reflective of the actual costs that the SO had to incur as a result of those parties not managing to balance themselves. Ofgem summarised this succinctly in 2006, in their decision letter for P194: *"The cashout arrangements are designed to target the costs of energy balancing to the parties who create those costs. They do this by imposing imbalance charges on parties who are not in balance that reflect the costs incurred by the SO in rectifying the imbalance….* *"Generators and suppliers are not under obligations to balance and can choose to pay the cashout price. But the cashout price should correctly signal to them NGET's cost of balancing. In response to this signal, generators and suppliers should try to balance their own positions if they are able to do so at lower cost than NGET."* There are also wider incentives on security of supply, plant reliability and long-term investment, which all require a feedback loop to NGET's costs of balancing in order to operate successfully.

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Q	Question	Response	Rationale
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	1) The modification should seek to reflect NGET's costs of resolving imbalance on behalf of parties causing that imbalance. 2) The modification should reflect those costs as accurately as possible. 3) The modification should target those costs on the parties causing those imbalances. 4) The modification should maintain or improve the current incentives on balancing. While it is difficult to measure quantifiably these four measures of success, it is clear that P212 by definition fails on all four counts. Presumably, therefore, there is a more general and assumed criterion for success – namely that a modification should not by its own definition fail to meet any of the fundamental requirements of a cashout regime.
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	It seems clear that the same perceived defect is being addressed in P212 as in P211. We believe that it has been shown that at some times, in some periods, there are issues around either transparency of the actions that are being included in the cashout prices; or the inclusion of the actions themselves. If these are classed as the 'polluted' prices, we find it difficult, or even impossible, to quantify exactly how polluted those prices are.

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Q	Question	Response	Rationale
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	We do not believe that simplicity per se should be a criterion for setting imbalance prices. If a viable and cost-reflective methodology is developed that has the benefit of also being straightforward, then this would be an added bonus. As Ofgem stated in their decision letter for P194: "The cash out price should create incentives to balance based on a price that appropriately reflects the costs to the SO of resolving that imbalance. European legislation highlights the importance of appropriate signals to maintain the balance between generation and demand, and to ensure that imbalance rules are transparent, objective, non-discriminatory and cost-reflective." 'Transparent' is not synonymous with 'simple'. We believe that transparency could be improved in the market, and we agree with the proposer that there is scope for increased information provision from the SO. This will hopefully be resolved via NGET's work on information transparency and Ofgem's SO review. It would be dangerous to value simplicity over the 'best' solution, and to value change over the status quo for change's sake. The simplest solution would be to have an SBP of £40 for all periods, and an SSP of £20 – this is clearly absurd, and we believe the assertion that P212 is in any way better than the current arrangements due to its simplicity is equally absurd. In any case, despite its initial simplistic formula for calculation of the cashout price, we do not believe that P212 is as simple as it might first appear. The implications that it would have on traded markets, the SO, market participants, market behaviour, cashflows and so on would be so difficult to predict and manage that one could only call it highly complex.

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	We believe that P212 would be detrimental to the achievement of the relevant BSC Objectives. B: The removal of the feedback loop between cashout prices and the imbalance prices would lead to inappropriate incentives. NGET would undoubtedly be forced to take an increased number of actions at whatever cost was available, following entirely rational behaviour by parties. The only signal to parties is whether to take a trade on the exchange, or not - it has nothing at all to do with whether parties are balanced in their generation and demand or not. This proposal fundamentally changes the principles of cashout introduced with NETA (as described above), and we have seen no argument to explain either why this fundamental change needs to occur, or how it will be better than the current arrangements. C: We do not believe the assertions of the proposer either that volatility and unpredictability will be removed; nor that new entrants would be attracted by a simplistic methodology. Volatility will not be removed; it will simply be linked to the power exchange and unpredictability will be a function of behaviour of trading participants, rather than a function of participants' overall balancing and the SO's consequent actions. New entrants are likely to be attracted to a well-functioning market, where rational decisions have rational consequences. P212 does not deliver this. The appropriate targeting of costs on those parties who cause them is a fundamental aid to competition. P212 removes the link between participants and the NGET actions that resolve their imbalances, and so is detrimental to competition.

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Q	Question	Response	Rationale
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Option 2 shares all the same main features and problems as Option 1.
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Option 3 also shares the features and problems of Options 1&2. There is an improvement compared to the other two options, however, in that the price is not known ex-ante, and so is less prone to manipulation or adverse/bizarre yet rational behavioural consequences. However, we would see Option 3 as a tool for removing some of the problems of the initial modification, rather than a valid proposal in its own right.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference:
			2nd Preference:
			3rd Preference:
			No Preference: It is difficult to state preferences when all options are equally unpalatable (notwithstanding Option 3's attempt to improve on the other options)

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Q	Question	Response	Rationale
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	Firstly, a fixed percentage of 5% would mean that traders would stop trading if they saw the next trade available to be more than 5% higher than the current cashout price. Any other fixed percentage would mean exactly the same, just with a different integer. P212 has completely different incentives to those required for a successful cashout regime, and would lead to a loss in liquidity on the exchange. Secondly, the incentive for parties to invest in accurate demand forecasting tools would disappear. Thirdly, the incentive for parties to trade out a short position following a plant trip close to gate closure would completely disappear. For example, if a party is 20 minutes from gate closure with an short position and a major generator trips, the incentive currently is to try and trade out that imbalance as the party knows the cashout price will be high, based on the actions Grid will have to take in the BM to make up the shortfall at short notice. Under P212, however, the incentive on the same party would be not to trade at all, as any attempt to buy energy at short notice would send market prices up, and therefore imbalance prices. The incentive is to do nothing and keep a benign SBP in place Furthermore, if the party above is actually the generator who is doing the tripping, he has no incentive to invest in more reliable plant, as the full cost of that trip is not targeted at him and to the full extent necessary to incentivise investment in making sure it is not a regular occurrence. The general message is that parties would in some circumstances not bother to balance, in some instances take rational decisions not to balance, and generally force the SO to take many more actions on behalf of the parties in imbalance. These costs do not disappear – they are then smeared back to participants on a non-reflective basis, creating a cross-subsidy where one does not exist currently.

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Q	Question	Response	Rationale
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	See above – the traders would simply stop trading at different points. The perverse incentives not to trade out imbalances would still remain.
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	Please see response to Q10. By design, this modification increases costs for the SO and fails to accurately target them at the correct participants.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	-	Centrica strongly suspects that if this modification were to be approved, there would be a raft of further modifications which would be necessary to resolve the ensuing problems.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	
14.	Are there any further comments on P212 that you wish to make?	No	

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION

Respondent:	Paul Jones
Company Name:	E.ON UK plc
No. of BSC Parties Represented	7
Parties Represented	Citigen London Ltd, E.ON UK plc, Economy Power, Enfield Energy Centre Ltd, Powergen Retail Ltd, TXU Europe (AHGD) Ltd, TXU Europe (AHST) Ltd
No. of Non BSC Parties Represented (e.g. Agents)	0
Non Parties represented	-
Role of Respondent	Supplier, Generator, Trader, Consolidator, Exemptable Generator
Does this response contain confidential information?	No

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	We believe that the primary aim of imbalance prices is to accurately target the costs that the System Operator has incurred providing energy balancing, at those parties who contribute to the imbalance. If this cost reflectivity is achieved then other important aims are achieved also. For instance, if the costs are targeted at those who cause them, there cannot be undue discrimination. Additionally, this is an essential condition for effective competition. There is a trade off between cost reflectivity and simplicity. However, this does not mean that cost reflectivity should be abandoned to provide as simple a solution as possible.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	This cannot really be measured by undertaking a pure quantitative analysis. However, a qualitative assessment can be made of whether a methodology is capable of accurately reflecting the costs that the SO has incurred. The attached paper attempt to do this using stylised supply curves.

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Q	Question	Response	Rationale
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	The stated defect is that the current tagging rules "*are defective and are resulting in a high level of pollution of the energy price from costs that relate to maintaining the system balance*". This is quite a fundamental criticism of the present mechanism. Whilst we believe that the tagging rules do sometimes lead to situations where actions that were taken for system purposes contribute the main imbalance price, we are unconvinced that this is a wide spread issue that occurs regularly. We also do not believe that sufficient evidence of the materiality of the issue has been provided to suggest that change is necessary.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	There is definitely a trade off between these two aims. However, it should be borne in mind that it is also very difficult to define what a correct cost reflective price would actually look like. Theoretically, what the methodology should seek to do is to separate the costs of energy balancing from those of balancing the system, for example in order to overcome constraints. However, it is difficult to fully define the boundary between these two classes of balancing. Additionally, many actions that the SO takes can have a dual purpose. Therefore, these actions can legitimately be regarded as having an effect on energy balancing and should therefore be reflected in imbalance prices to some extent. We are not convinced that a different balance of cost reflectivity and simplicity is required from that provided by the current mechanism.

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	P212 does not seek to link imbalance prices to the cost of the actions that were or could have been taken to meet energy imbalance. Therefore, it is not at all cost reflective. It is indeed simple. However, cost reflectivity is by far a more important aim of the arrangements. To simply abandon it in this manner to achieve simplicity is inappropriate. What this option (at 5%) is likely to do is to understate the level of prices significantly. This dilution of the signal to balance will lead to an increase in the socialisation of energy balancing costs across all parties (through the combined effects of BSUoS and RCRC). In simple term, parties in energy imbalance will have too low a cost targeted at them, which will have to be made up by other parties. This will result in a cross subsidy to parties in imbalance. This would be detrimental to competition. Additionally, as the incentive to balance will be inappropriately reduced this will result in inefficient balancing decisions being made. This will also reduce the incentive to accurately forecast customer demand or to invest in the reliability of plant. This will reduce the efficiency of the arrangements and put up balancing costs. Therefore, this solution would undermine applicable objectives c) and b).
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	A similar rationale exists for not supporting this option. Simply observing a historic average ratio of imbalance prices to market prices under the existing methodology and using this to set imbalance prices in the future is not at all cost reflective. The difference between this option and the fixed percentage of 5% is that the cross subsidy could occur either way. If imbalance prices are overstated at times, this will result in cross subsidy from those parties in imbalance to others. The end result is the same: inefficient energy balancing and an undermining of competition.

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Q	Question	Response	Rationale
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Again, linking the dynamic percentage to a parameter such as NIV is inappropriate as a link between NIV, Market Price and Main Imbalance prices under the present mechanism has not been identified. It is likely that this proposal would have a similar effect to the second option. Prices may be understated or overstated as a result of the lack of cost reflectivity. Therefore, the results would be the same: inefficient energy balancing and an undermining of competition.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference:
			2nd Preference:
			3rd Preference:
			No Preference: All options would be detrimental in different ways. It is difficult to assess which would be worse than others or worst over all with any degree of certainty.
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	It would lead to a lower than efficient incentive to balance as described in 5, 6 and 7 above. The fixed percentage would result in participants not opting to trade in the market if the next price available was more than 5% higher than the level they expected market price to outturn at. This means that higher priced actions could be accepted under the balancing mechanism, but some of the cost of these would be smeared over other participants, rather than correctly targeted at those who caused them.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	The trade off described above would be made against a higher percentage. At some point this may result in imbalance prices <u>on average</u> overstating the costs compared with those actually incurred. However, this would only incur on average, not for periods or to the same extent, and could not be expected to persist for future years. The signals would still not be cost reflective and inappropriate balancing behaviour would continue to result from this.

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Q	Question	Response	Rationale
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	As stated in 5, 6 and 7 above, we would expect this to increase costs as inappropriate balancing decisions would be made.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	This would be a fundamental principle in the trading arrangements. As such it should only be open to change with the level of scrutiny and due process that the modification assessment procedures provide.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	
14.	Are there any further comments on P212 that you wish to make?	Yes	Please see the attached paper that seeks to further illustrate why we believe that the above options do not better meet the aim of cost reflectivity.

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An assessment of imbalance pricing and P212

The following is intended to support E.ON UKs' answers to the Assessment Consultation for P212. E.ON UK does not support P212 and believes that the following will illustrate P212's shortcomings as a concept. The following analysis uses stylised supply curves to show how a "perfect" energy price might be achieved. These curves are not intended to accurately illustrate the supply curve facing the UK market at any particular time or to fully describe the balancing mechanism's operation, but are designed to illustrate the basic intent of what an imbalance price should seek to do and show how the options for P212 compare.

The basic supply curve and pre and post gate closure transactions

Figure 1 below shows the basic supply curve that we will use for this illustration.

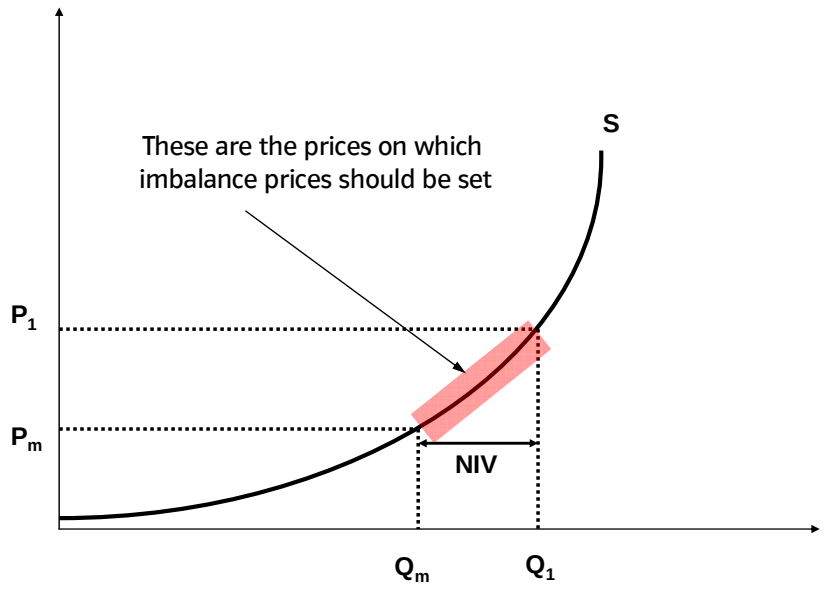

Figure 1: Stylised Supply Curve and a Short Market

In this example we assume that traders will initially buy lower priced offers in the market and that higher priced offers will be taken up as the market moves towards real time. Assume that up to gate closure a volume of Q_m of trades is made. The marginal price of these pre gate closure trades is P_m. After, gate closure as the market is short over all, the System Operator (SO) has a Net

Imbalance Volume (NIV) to meet up to the total demand of Q_1, at a corresponding marginal price of P_1. The part of the curve that imbalance prices should be calculated from is highlighted in red. Assuming an imbalance price calculated from the weighted average cost of these actions, the price would be somewhere between P_m and P_1.

Of course, this example above assumes that there are no constraints effective at the time. Figure 2 illustrates how the present tagging mechanism attempts to deal with these.

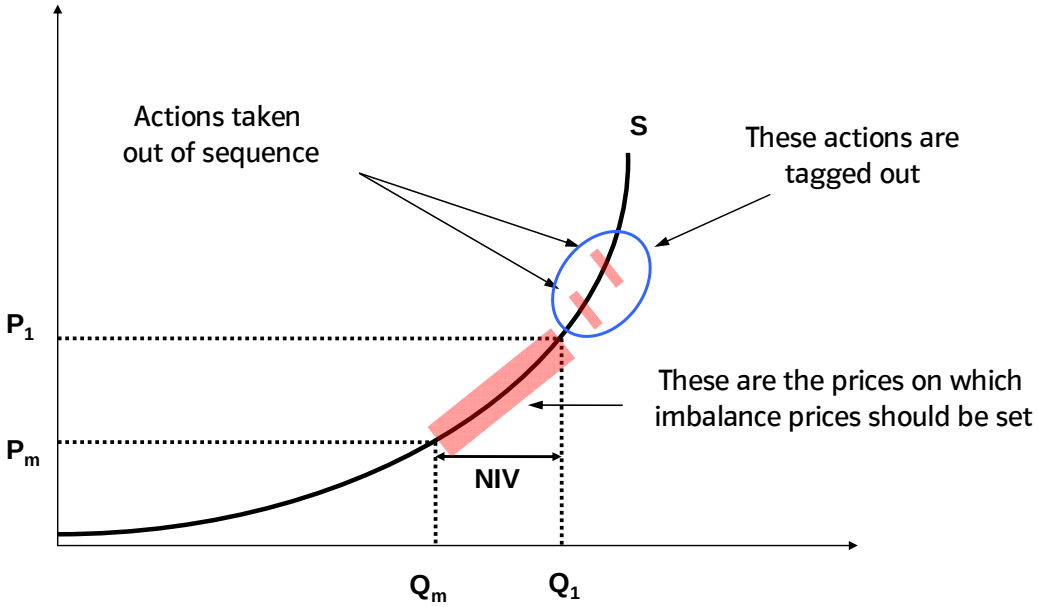

Figure 2: NIV tagging to remove constraint costs

In Figure 2 the actions that have been taken by the SO are illustrated by the red shaded areas. A block of actions have been taken to address the NIV. However, two other actions have been taken further up the curve out of sequence to meet constraints. It would be expected that equal and opposite actions are taken in the opposite direction (the bid curve) to bring the market back into energy balancing.

As it is the net imbalance of the market that should affect energy balancing costs, those actions that are required over and above those needed to meet the NIV are tagged out (by ignoring a volume of the most expensive offers equivalent to the total volume of offsetting bids accepted). Therefore, in the stylised example above the tagging ensures that the correct energy price is achieved.

However, there are circumstances when actions required for system balancing also meet an energy balancing purpose. For example, in a long market a bid accepted in the north of the country may relieve the north south

flow and also reduce the length of the market. In those circumstances, actions taken out of theoretical price order may end up in the imbalance price calculation. Figure 3 illustrates this.

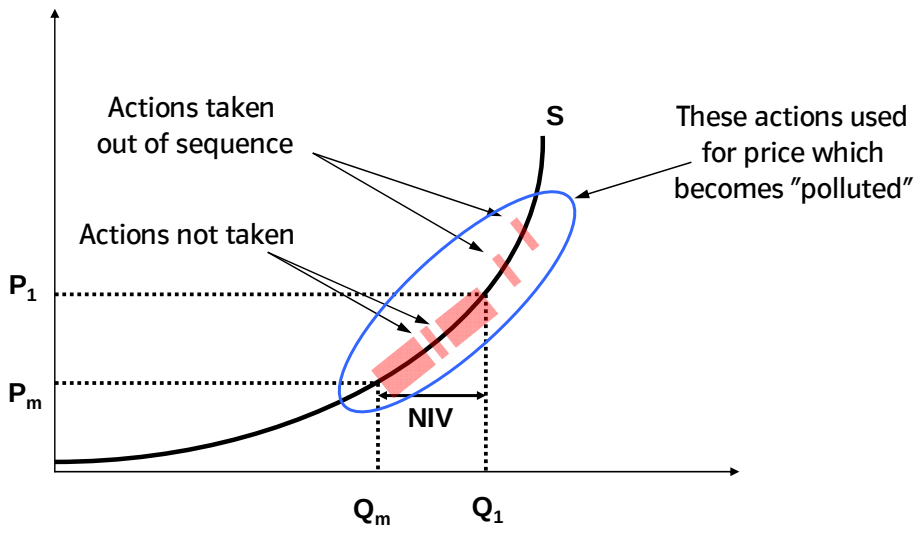

Figure 3: Prices accepted out of sequence

In Figure 3, the system operator has accepted prices out of sequence for system purposes. As these actions assist with energy balancing there is no need to take other actions that could theoretically have been taken. For illustrative purposes these "gaps" are shown in the middle of the block of energy actions that "should" have been taken, although in reality the SO is likely to have taken these and not taken more expensive actions in this block.

In these circumstances, the tagging rules include the higher priced actions in the calculation of the main imbalance price. This it could be argued sets an imbalance price that is higher than it ideally should be. This is what has been described as "pollution" of the energy price.

In reality, of course the situation is not as simple as this. The SO is taking actions over a longer period of time than just in gate closure, against a constantly changing view of the market, in order to resolve potential issues in more than one period. However, the above illustrates the basic issue that that has been raised as a reason for P212 and indeed P211.

Although, we do not actually believe that the extent of the potential defect has been illustrated to be sufficiently material or prevalent to warrant a change to the pricing mechanism, it is worth assessing whether the options under P212 would address the issue. Figure 4 below shows how the original proposal would work.

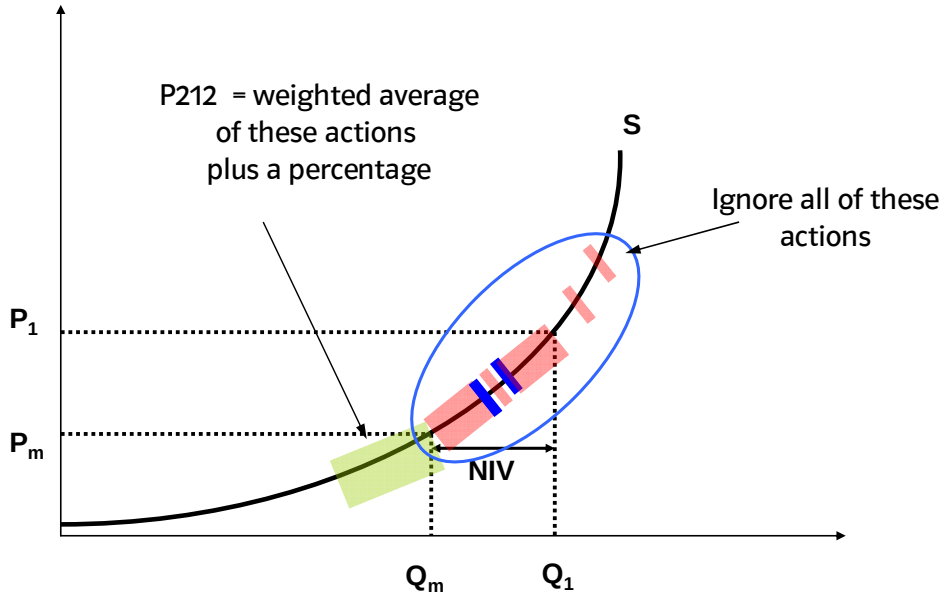

Figure 4: The basic P212 mechanism

As shown in Figure 4, the basic P212 mechanism simply adds a percentage on to the weighted average of certain trades made before gate closure to derive the main imbalance price. These trades are illustrated by the green shading on the curve. This mechanism cannot be a reliable proxy for the weighted average of prices between P_m and P_1 as the prices that are accepted pre gate closure cannot always be the same percentage difference from those prices accepted post gate closure.

For instance, in the example above if a larger NIV were to be met, then the relationship between pre and post gate closure prices would alter. Therefore, not only does the original fixed percentage solution for P212 fail to work, but the alternative solution which seeks to establish a historic relationship between pre and post gate closure prices also fails. Both these solutions would have derived the same imbalance price even though the costs caused by imbalance parties were very different.

The third option for P212 seeks to apply a different level of percentage uplift to market price dependent the level of a parameter such as NIV or a measure of system stress. However, this also cannot work as a proxy for costs the SO incurs in energy balancing. Figure 5 below illustrates why this is the case. Suppose from looking at the supply curve S it was possible to establish a relationship between NIV, market price and the correct energy imbalance price. That is for a certain NIV the energy price (P_{energy}) is X% higher than the market price (P_{market}). As soon as the shape of the curve changes, then this relationship will not hold. In Figure 5 this is illustrated by the different shaped

supply curves S_x and S_y that follow the same path as S up to a volume of Q_m and thereafter increase more steeply and more gradually respectively.

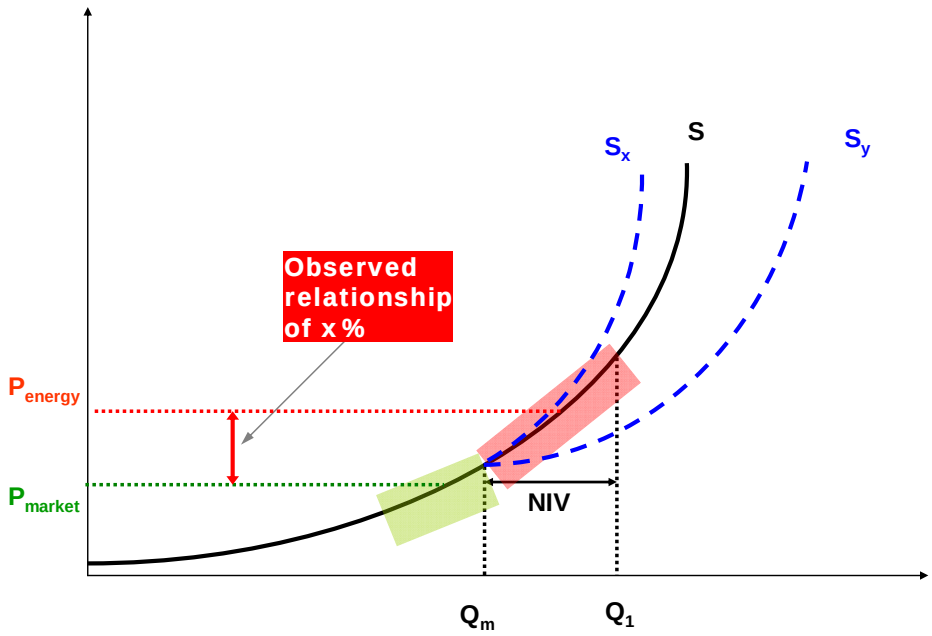

Figure 5: A link between market price, imbalance prices and NIV?

A percentage that changed in relation to NIV would calculate the same price for all three curves for the same level of NIV. However, it is clear that the costs that would be incurred with curve S_x would be higher than those incurred for curve S. Similarly, the costs incurred with curve S_y would be lower than those for curve S. Therefore, this approach cannot achieve a suitable proxy for the costs of energy imbalance either.

Conclusions

It is clear to us that P212 does not work. Even if you were to accept the extent of the stated defect, which we do not, the proposed solutions fail to solve the perceived problem. This is not surprising as all of the options for P212 fail to consider the costs that were or could have been taken to address the energy imbalance of the market and instead look at those trades that occurred outside of the balancing mechanism.

P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	David Lewis
Company Name:	EDF Energy Plc
No. of BSC Parties Represented	9
Parties Represented	EDF Energy Networks (EPN) plc; EDF Energy Networks (LPN) plc; EDF Energy Networks (SPN) plc; EDF Energy (Sutton Bridge Power); EDF Energy (Cottam Power) Ltd; EDF Energy (West Burton Power) Ltd; EDF Energy plc; EDF Energy Customers Plc; Seeboard Energy Limited
No. of Non BSC Parties Represented (e.g. Agents)	0
Non Parties represented	N/A
Role of Respondent	Supplier/Generator/Trader/Distributor
Does this response contain confidential information?	No

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Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	In a net mandatory pool such as NETA where most electricity is traded bi-laterally outside of the central arrangements, imbalance prices are designed to ensure that parties are incentivised to do just that (i.e. contract bi-laterally). We do not make the distinction between "incentive to contract" and "incentive to balance" as you are essentially contracting to balance, so both terms can be used interchangeably. It follows then that prices should be at a premium to the forward and short term markets to retain this incentive, and logically, this should be linked in some way to the cost that the residual balancer (i.e. National Grid as System Operator) has incurred through resolving this energy imbalance. The cost however should not be linked to "other actions" that the SO has to take to maintain system security such as the resolution of congestion on the system, the cost of dealing with short term fluctuations in demand and the cost related to reserve procurement, in particular, because this can be heavily influenced by constraints on the system (reserve can be made inaccessible by an export constraint and therefore may have to be purchased at a higher cost elsewhere). We would of course expect the relationship between primary fuel prices and imbalance costs to continue.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	Demonstrating that the incentive to contract/balance is working is relatively easy to measure ex-post by looking at the level of market imbalance in any settlement period (the "Net Imbalance Volume"), or simply comparing parties contracted positions to their outturn metered volumes. Market efficiency can be demonstrated by observing a narrow bid offer spread.
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	Please see our attachment to our P211 response entitled "EDF Energy P211 Defect Analysis Final".

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Q	Question	Response	Rationale
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	Both are important concepts in ensuring that the cash out arrangements are both transparent and accessible ("simplicity") whilst also appropriately targeting the cost of energy imbalance on to out of balance parties ("cost reflectivity"). Given the nature of the GB electricity system, it is recognised that there will always be a trade off between these two sometimes conflicting concepts, but it is clear that it is possible to achieve a better trade off than the arrangements that are currently in place. Given the wide range of actions that National Grid Electricity Transmission (NGET) as System Operator (SO) takes, to manage the system, it is impossible to calculate a cash out price that is cost reflective of energy imbalance, when it is based on actions that are not primarily for restoring the system imbalance. This is quite clearly shown in the analysis presented by National Grid at the cash out review meeting on the 30th March 2007 when they stated that 75% of Offers and 59% of Bids within NIV are polluted by other "non-energy" actions. It is clear that the P211 proposal will ensure cash out prices reflect energy imbalance, by basing the main imbalance price on actions that the SO could have taken on an unconstrained system. It is also clear that this approach moves towards a much simpler and transparent methodology for calculating the main imbalance price.

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Whilst we are sympathetic with what this (and options 2 and 3) are trying to achieve, we believe that there has to be some link to the actions that the SO takes, or could have taken, to resolve the energy imbalance of the system. We therefore believe that a price based purely on market trades with a fixed percentage of 5% would not provide a more cost reflective signal than the current baseline. We therefore believe that this would not better facilitate Objective B. In relation to Objective C, we agree that the modification will remove the impact of "other actions" on the main energy imbalance price and that the mechanism will be greatly simplified compared to the current arrangements. This could be likely to promote competition in the electricity market so we believe that it will better facilitate Objective C. In the round however, we do not believe that the proposed option 1 will better facilitate the BSC Objectives.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Please see our answer to Question 5.

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Q	Question	Response	Rationale
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Please see our answer to Question 5. We note however that one proposal under this option is to use a measure of system stress, and that some members believe that the difference between demand and sum of MEL is not a good proxy "because it does not take into account the volumes brought to the market by the System Operator". We would be grateful if those members could expand on this view which we find confusing, particularly given that sum of MEL minus demand is a well established measure of margin and a Grid Code defined term. Should the Modification group decide to use some measure of system stress then we would suggest that this is a much better approximation than CSOBM, which also includes the costs of "other actions" taken in the Balancing Mechanism. Section 4 of the note provided by RWE Trading to the P212 modification group illustrates this point very well.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: Whilst we do not support any of the options against the current baseline, we believe that option 1 should form the proposed solution for this modification. This maintains some sort of incentive to contract ahead of Gate Closure, whilst also retaining the simplicity that the proposal sought to introduce into the electricity trading arrangements.
			2nd Preference:
			3rd Preference:
			No Preference:

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Q	Question	Response	Rationale
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	It is likely that a move to a purely market based price will provide different signals than those provided by a mechanism which retains some sort of link to the actions taken by the SO in the Balancing Market, and it could be expected that parties behaviour will change accordingly in response to these different signals. However, any view on specifically how parties' behaviour might change will require some sort of subjective qualitative assessment which could hold little relevance to what actually happens. It is worth noting that applying any premium/discount to a price could be expected to retain some sort of incentive to contract, but the extent to which this changes party behaviour can only properly be understood if such a change is made.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	Please see our answer to Question 9 above.
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	Please see our answer to Question 9 above.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	Given the potential financial impact on parties from changes to the pricing value and/or the methodology, it is imperative that these can only be changed via a modification to the BSC and subject to a proper assessment.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	

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Q	Question	Response	Rationale
14.	Are there any further comments on P212 that you wish to make?	Yes	We would like to point out that the assessment procedure for P212 has been disrupted by the significant amount of time spent discussing what is a well recognised and proven defect within the trading arrangements.

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Andrew Colley*
Company Name:	*Scottish and Southern Energy plc.*
No. of BSC Parties Represented	*6*
Parties Represented	SSE Energy Supply Ltd., SSE Generation Ltd., Keadby Generation Ltd., Medway Power Ltd., Southern Electric Power Distribution plc., Scottish Hydro-Electric Power Distribution Ltd.
No. of Non BSC Parties Represented (e.g. Agents)	*0*
Non Parties represented	
Role of Respondent	*Supplier/Generator/Trader/Distributors*
Does this response contain confidential information?	*No*

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	To provide a sensible proxy of the short-term energy costs of the System Operator (SO) in balancing the system and reflect the opportunity costs of balancing; and to target those costs at those parties that impose the costs upon the SO, proportional to their share of total imbalances.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	

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Q	Question	Response	Rationale
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	Undoubtedly it has been proven that on occasion, "system" actions, or more precisely constraint actions, have affected energy imbalance prices and introduced costs that are not reflective of the short-term cost of energy balancing. SSE contends that constraint actions seem the most appropriate area to concentrate upon as these actions appear to be the principle cause of concern driving this proposal. This particular effect was prevalent in the months immediately following the introduction of BETTA, which also coincided with record wholesale gas prices. SSE do not accept the definition of "energy plus" as an appropriate definition in determining those actions that should or should not be included as part of short term energy balancing costs feeding into energy imbalance price equations. For example SSE firmly believe that intra half hour actions, such as TV pickups, are appropriate for inclusion in the price equation. SSE note the heavy caveats provided by the SO in presenting an "energy plus" analysis to industry at the Ofgem led workshop at the start of the year. Notwithstanding the above SSE remain concerned that the extent of the issue has not been proven, whilst accepting that providing such proof is very difficult to achieve. It is our view that, whilst always possible to highlight individual periods as anomalies, this does not prove that the issue is substantial. Our perception remains that actions taken by System Operator (SO) in the forward market have significantly helped in alleviating the inappropriate effects of Cheviot constraint costs within the imbalance price calculation. We do not perceive the current level of error that may be entering the imbalance price equation as significant and are prepared to continue to accept it as a reasonable and appropriate proxy of the short-term costs incurred by the SO to balance the system.

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Q	Question	Response	Rationale
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	SSE firmly believe that energy imbalance prices should continue to provide a proxy of the short-term costs of the SO in balancing the system and that cash-out should reflect the opportunity costs of balancing. As such it should reflect the real actions taken by the SO to resolve energy imbalance in the Balancing Mechanism and in forward markets through energy BSAD. Such costs should subsequently continue to be targeted upon those that impose them through being out of balance. These principles were a cornerstone of the NETA/BETTA arrangements and, given the features of NETA arrangements, continue to remain key concepts in our opinion. We note with interest that the Authority's response to virtually all pricing modification proposals since the implementation of NETA has reasserted these principles as key. SSE believe that the above principles are the simplest concepts of all to understand, in the context of economic efficiency, and that any deviation would in practice create a more artificial principle which could be argued to be more complex. We prefer simplicity of concept as opposed to simplicity of administration. Complexity in the administration of a simple concept is not in itself a barrier to competition as the rules governing the administrative arrangements are publicly available and accessible and can be assessed by new entrants.

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Objective (b). This proposal introduces the prospect of imbalance prices being derived that have no linkage to and may gear no resemblance to the actual costs incurred by the So to resolve imbalance. This would have the effect of softening imbalance prices, reducing SBP and increasing SSP. SSE would be concerned by that softening energy imbalance prices, unduly limiting price volatility and removing the link being prices and the actual costs faced by the SO to balance the system, traders may be presented with a reduced incentive to trade to minimise their imbalance exposure. An erosion in these incentives and the subsequent increased level of imbalance volume being held into the BM by traders likely to follow, would increase the costs to the SO to balance the system. Thus the modification acts counter to objective (b) in our view, by increasing the likelihood of greater costs being incurred by the SO to balance the system. Additionally SSE would be concerned that plant loss post Gate Closure and the potentially high cost incurred by the SO to cover this loss, would not be accommodated at all within the proposal. SSE would be concerned that dampened price signals for unreliable plant would reduce short-term incentives to trade out imbalances and reduce long-term incentives to invest in reliable plant technology, the second of these potentially creating a long-term threat to security of supply. To this extent, SSE believe that the modification acts counter to objectives (b) and (a) by increasing the likelihood of greater costs being incurred by the SO to balance the system and by creating a long-term threat to security of supply.

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Q	Question	Response	Rationale
			Objective (c). A fundamental principle of the NETA arrangements when first introduced was the desire to target the actual short-term energy balancing costs incurred by the SO upon those parties in imbalance, who had created the need for those costs to be incurred – a simple polluter pays concept. Parties were thus incentivised to invest in plant reliability and/or improved demand forecasting capability in order to minimise their exposure to these costs. This proposal moves too far away from that fundamental principle by removing the link to the actual costs borne by the SO and referencing a ex-ante market price which is likely to trade at a discount to the price that would be discovered through PAR500 methodology. This would have the effect of dampening the prices meaning that inappropriate prices would be passed through to those parties causing the imbalance on the system. This would penalise those parties that have been prepared to or are willing to invest in plant reliability and demand forecasting technology and creates an inappropriate cross-subsidy to those parties that have not made a similar investment. This distorts rather than promotes competition in our view and acts contrary to objective (c). SSE would also be concerned that the proposed modification would be more susceptible to single parties influencing prices to their own favour, particularly at times when the spot market is illiquid and small numbers of trades (possibly even a single trade) distort outturn prices. This would act contrary to objective (c).
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	See Q5 above.

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Q	Question	Response	Rationale
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	See Q5 above.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: 2nd Preference: 3rd Preference: No Preference: SSE have no preference. It is our view that the rationale supporting this change is so tenuous that we cannot support any change away from the current baseline. The premia and discount bands, and the premia and discount values themselves, have no economic basis to support their derivation; they are wholly arbitrary values; therefore SSE cannot state a preference for any of the options presented.
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	See Question 5. Above. To reiterate in summary :- SSE would be concerned that inappropriate price signals would be sent to the forward market to balance and trade out their positions. This would reduce trading activity and result in larger open positions being taken into the BM. This in turn would impose a greater cost upon the SO to balance the system and an inappropriate targeting and recovery of those costs.

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Q	Question	Response	Rationale
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	Market participants' balancing behaviour will be dictated by rational assessment of economic choices regardless of the percentage increase in premium and discount. The cost of buying forward in the spot market to cover imbalance exposure versus taking the imbalance price is one such rational assessment. Ex-ante setting of price premia and discounts would in our view lead to traders taking larger open positions into the BM, leading to a greater imbalance volume to resolve for the SO. Traders will have certainty of the imbalance price based on knowledge of the market price, plus the fixed adjustments suggested. Such prices are likely to be lower than the prices that would be taken in the BM (owing to the increasing value of real-time flexible generation as one gets closer to actual delivery), thus reducing the incentive to trade.
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	See Q5 above.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	Pricing values and methodologies are key commercial parameters that impact upon parties' profitability. Appropriate safeguards are required that ensure a full assessment is undertaken of any desired change to these parameters.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	
14.	Are there any further comments on P212 that you wish to make?	No	

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Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Graham Meeks*
Company Name:	*CHPA*
No. of BSC Parties Represented	
Parties Represented	
No. of Non BSC Parties Represented (e.g. Agents)	
Non Parties represented	
Role of Respondent	*Trade association*
Does this response contain confidential information?	*No*

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	The objective should be to provide a fair reflection of the cost of balancing energy for uncontracted trades, while embracing incentives to contract. In doing this cash-out must enable the SO to take actions efficiently and not distort competition between market participants by allocating system costs or costs that more appropriately should be socialised.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	Detailed examination of historic price stacks should help to better understand the derivation of the costs and assess the scale of the deficiencies, and in so doing provide a baseline against which rule changes can be properly assessed.
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	Ofgem's P205 decision letter and analysis presented by National Grid at the 30 March cash-out review industry meeting shows there is presently significant pollution in energy imbalance under current pricing rules, and thus a clear defect. The defect operates in such a way as to systematically disadvantage inflexible generators, including CHP plant which primarily tracks the heat load.

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Q	Question	Response	Rationale
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	Both are important.	The approach to cash-out should be transparent and comprehensible to the greatest extent possible and that prices can be verified where necessary. At present there is no ability to determine what the imbalance price might be in any particular imbalance period, and it is very difficult for a generator to manage the risk of plant failure. Ultimately there will always be judgments about what is cost-reflective, but it is clear that there are real distortions under the current cash-out rules with system costs being mis-targeted.
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	It would guarantee a price that was higher than the market reference price, which in turn would reflect the market price for short-term energy. By avoiding use of the current tagging rules it would nullify the competitive distortions inherent in the current arrangements.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	While in principle the concept of a profiled percentage has merit, the proposed approach represented by option 2 is penal in its effect.
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	As with option 1 it would guarantee a price that was higher than the market reference price, which in turn would reflect the market price for short-term energy. Again by avoiding use of the current tagging rules, it would nullify the competitive distortions inherent in the current arrangements.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: Option 3, assuming it can be linked to NIV. 2nd Preference: Option 1.

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Q	Question	Response	Rationale
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	The imbalance price under all the P212 options will preserve a strong incentive to contract because it will produce above-market prices. Logically "fear of cash-out" should increase in this situation as generators compete to avoid the premia.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	A 5% uplift is sufficient to create a strong incentive to avoid imbalance in most instances. During periods of system stress the increment would be from a much higher base increasing the absolute cost incentive to contract.
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	There is an argument that the incentive to contract is sufficient and should not greatly impact on participants' decisions. Perversely the higher the cost premium the more likely parties are to over-contract, thereby increasing the SO's costs.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	No	Option 2—it is important that the rules can be applied flexibly. An approach analogous to other key parameters such as CADL where the rule can be reviewed by the panel following consultation with the added surety of an Ofgem veto would seem appropriate.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	Yes	There is a range of possible options for setting the premium/discount, which seem not to have been tested.

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Q	Question	Response	Rationale
14.	Are there any further comments on P212 that you wish to make?	Yes	A key impediment to proper assessment of P212 is the failure of the group to identify a benchmark for the optimal imbalance price. The report notes (p17) that as a result the group could not conclude whether the proposed solutions was a better estimate of the true energy costs of the SO's balancing actions. The reluctance of the modification group to tackle the details of a suitable arrangement and carry out an appropriate level of analysis should not obscure the basic principles and merits of a market reference price approach.

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	Man Kwong Liu
Company Name:	*Scottish Power*
No. of BSC Parties Represented	7
Parties Represented	*Please list all BSC Party names of Parties responding on behalf of (including the respondent company if relevant).* ScottishPower Energy Management Ltd, ScottishPower Generation Ltd, ScottishPower Energy Retail Ltd, SP Transmission Ltd, SP Manweb plc, SP Distribution Ltd, CRE Energy Limited
No. of Non BSC Parties Represented (e.g. Agents)	0
Non Parties represented	*Please list all non Parties responding on behalf of (including the respondent company if relevant).*
Role of Respondent	*(Supplier/Generator/ Trader / Consolidator / Exemptable Generator / BSC Agent / Party Agent / Distributors / other – please state* [1]*)* Supplier/Generator/ Trader / Consolidator / Exemptable Generator /distributors
Does this response contain confidential information?	No

Q	Question	Response [1]	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	ScottishPower believe the principle of main imbalance price should be to reflect SO actions for that particular period to resolve energy imbalances. This price should then be applied to those parties who are out of balance. Imbalance prices should therefore provide the necessary incentive for parties to ensure a balanced position (as much as possible) to avoid higher imbalance charges.

[1] Delete as appropriate – please do not use strikeout, this is to make it easier to analyse the responses

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Q	Question	Response [1]	Rationale
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	ScottishPower suggest one way of measure of success would be that all parties approach gate closure with a balanced position and SO carry out minimal residual energy balancing actions at minimal costs. All energy imbalance costs would be recharged against those whose are out of balance.
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	**Yes**	ScottishPower acknowledge that there is a defect relating to imbalance price impact due to transmission constraints. However, We do believe that after 6 years of NETA/BETTA operation, the current cash out pricing arrangement is now well proven, reasonably reflective of SO actions and provide an appropriate incentive to balance. While there were some examples of particular problems during the BETTA transition period, our understanding is that the frequency and impact from any subsequent similar occurrence were minimal and cannot justify such wholesale change of arrangement as proposed by this Modification and its alternatives. The defect defined in P212 appears to be more significant comparing to P211. This has not shown to be the case in the modification analysis.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	ScottishPower accept that a solution and mechanism to fulfil the principle of imbalance pricing should be simple. We do not think the current arrangement to be overly complicated or a barrier to entry. Electricity is not a simple business. Rules have to be reflective of the principles. The new arrangement as proposed by this modification and its alternatives while simple on the surface may not be any more efficient to operate and are difficult to determine,

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Q	Question	Response [1]	Rationale
5.	Whether the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	**No**	ScottishPower believe this Proposed modification creates prices that are arbitrary and would not better facilitate the achievement of the Applicable BSC Objective (b) – efficient operation of the transmission system or (c) – promote competition, when compared with the current baseline. In approving P194, the Authority argued that the averaged cash out prices were not as reflective of SO actions and therefore did not give sufficient incentive to balance. As analysis showed, this modification will be even less reflective than the averaged pricing arrangement. This means that it will give even less incentive to balance which could give rise to greater SO actions and costs. Furthermore, as the Mod Group has suggested, the reduced penalty on imbalance potentially could mean less concern to ensure plant reliability which could give rise to potential supply security issue. These would be detrimental to Objective (b). With its less cost reflectivity, this modification gives rise to cross subsidies with imbalanced parties not paying the appropriate costs due to their imbalances. Also, while the modification attempts to eliminate 'pollution' from the current arrangement, it creates an environment for potential price manipulation (within the rules) as well as reactive behaviour and resulting in other potential price distortions. We are also concerned that for a low materiality defect, the industry could change the arrangement so fundamentally that could undermine a lot of investments by existing participants. Such situation gives uncertain signal to the market. These factors do not promote Objective (c). On Objective (d) – efficient administration, while ScottishPower accept this arrangement is simpler to operate, the above disbenefits outweight any potential efficiency saving in administration.

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Q	Question	Response [1]	Rationale
6.	Whether the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	**No**	Same rationale and objectives as the Proposed above. While it attempts to produce prices that are more reflective than the Proposed, the same issues as discussed above remain that are detrimental to the Applicable BSC Objectives. There also remains an issue with the difficulty in determining the appropriate % values.
7.	Whether the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	**No**	Same rationale and objectives as the Proposed above. While it attempts to produce prices that are more reflective and less manipulative than the other options, the same issues as discussed above remain that are detrimental to the Applicable BSC Objectives. Furthermore, On Objective (d) – efficient administration, ScottishPower do not believe that this option is any more efficient to administrate and operate. There also remains an issue with the difficulty in determining the appropriate % values.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	**-**	Not withstanding the fact that ScottishPower do not believe any of these options would better facilitate the achievement of the Applicable BSC Objectives comparing with the current baseline, we think Option 3 would give better cost reflectivity and be less prone to market influence when comparing with each other. However, it would depend on the cost of implementation and the % values used. 1st Preference: Option 3
			2nd Preference: Option 2
			3rd Preference: Option 1
			No Preference:

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Q	Question	Response [1]	Rationale
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	**Yes**	ScottishPower believe that at times there will be no incentive to balance. This would increase SO actions and costs. We are also concerned that liquidity in the forward market would suffer give rise to more opportunities for market influence by large traders. The fixed 5% would exacerbate the above situation.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	**Yes**	The greater the % increase from 5%, the greater would be the incentive to balance. However, participants' behaviour would remain reactive to the market prices and their abilities to influence the market rather than proactively ensuring a balanced position at gate closure.
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	**Yes**	Irrespective of which option is used, the impact on SO costs of balancing the system would depend on the values (%) used and the incentive to balance. However, as has shown in numerous Mod Group meetings, there is no 'one sure way' in determining what the values should be, apart from arbitrary suggestions and subjective views of individuals.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	**Yes**	ScottishPower agree with the Mod Group's view that due to the difficulty in defining a methodology and with no particular saving, and for such potential significant impact to the industry, wider industry and Ofgem participation would be necessary to ensure confidence in and transparency to the market governance.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	**Yes**	As the main issue of the current pricing arrangement appears to be the 'pollution' of transmission constraints, ScottishPower believe that the process of tagging out system actions including transmission constraints should be reviewed.

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Q	Question	Response [1]	Rationale
14.	Are there any further comments on P212 that you wish to make?	**Yes**	ScottishPower find that the pursuance of this modification and indeed P211 significantly diverged from previous Authority views on pricing modifications (P194 and P205). While we believe P194 did not better the applicable BSC objectives due to its penal nature, this modification appears to go to the other extreme at the expense of incentive to balance and cost reflectivity. Existing participants have already made significant investment to ensure good balancing operation. Such change in principles and arrangement could undermine their position, creating significant uncertainty in the industry and detrimental to competition. We are also concerned that as with any new arrangement, anomalies could exist (as shown by some analysis) which may not have been envisaged at the outset. This could lead to uncertainty and further development. We suggest such a departure in the pricing arrangement should be developed with more timescale and stress testing. Furthermore, with such a fundamental change in pricing arrangement, the values of parties' existing energy contracts could be significantly eroded which could have knock-on effects. This should be considered when determining the implementation timescale.

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **12:00 on 28 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	Rebecca Williams
Company Name:	Uskmouth Power Limited
No. of BSC Parties Represented	1
Parties Represented	Uskmouth Power
No. of Non BSC Parties Represented (e.g. Agents)	none
Non Parties represented	
Role of Respondent	Generator
Does this response contain confidential information?	No

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	The aim of the imbalance prices is to reflect the energy cost of being out of balance. These costs relate to the energy cost the SO has incurred for correcting your imbalance position. Imbalance prices should therefore reflect costs, be charged on a polluter pays basis and be transparent.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	Analysis that shows whether the methodology for calculating the imbalance price does achieve an energy imbalance price, removing all system costs, but taking account of the actual costs to the SO. This means that the prices must remain linked to the energy sold in the very short term which may be different from that sold in forward markets, or even under the same system position on a different day – i.e. different plant being used to balance.

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Q	Question	Response	Rationale
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	YES	Uskmouth has some sympathy with the view that the separating energy costs from system costs is difficult. There have been times when system actions, such as for constraints, can get caught in the cash out calculations. However, Uskmouth feels that where this "pollution" of prices does occur that better tagging would provide a more robust solution.

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Q	Question	Response	Rationale
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	Uskmouth would like to see cost reflective pricing as it is important to encourage plant to be available in the short term and for new plant to be built in the longer term. We feel that changes to cash out that reduce cost reflectivity will impact the forward market to such an extent as to risk security of supply. Changes that artificially suppress any prices will be detrimental to the economically efficient development of the market as a whole. It is also important that suppliers continue to look to buy their energy in the pre-gate closure markets, where power would reasonably be expected to be cheaper due to the costs associated with near real time delivery. The idea of a "simple" price is attractive, but the modification groups' discussions around P211 and P212 have only served to demonstrate that there is no simple solution. A simple mechanism is likely to result in an imbalance price that does not reflect what could or would actually be delivered and therefore cannot be reflective of prices. Any changes that focuses on simplicity is therefore likely to create problems somewhere in the market, such as not encouraging new build, or leading to increased smearing of costs. There seems to be a view that it things were simpler it would be easier to manage risks. What seems more important is that the prices are not extreme and remain reflective of the costs the SO faces in real time. If cash out becomes simpler and therefore non-cost reflective, suppliers may find that it is easier to take cash-out rather than correctly forecast and contract in advance. This could reduce liquidity, push up RCRC costs, etc, simply moving the costs of supply to other areas.

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	The principle of the proposal itself is flawed, through removing the link of the costs of the balancing actions undertaken by the SO from the main imbalance price calculation. In addition to this disconnect between the costs incurred by the SO and the energy imbalance price, option 1, further discourages participants to balance, the fixed 5% provides a much weaker incentive to balance than the current arrangements. Uskmouth also notes that the 5% is random and could turn out to be the wrong random number.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	As explained above, the principle of the proposal is flawed. Option 2, variable percentage, introduces an additional level of complexity without necessarily encouraging market participants to balance. The current arrangements reflect the costs of SO balancing actions and these are targeted onto parties contributing to the imbalance, therefore better facilitating the achievement of Applicable BSC Objectives.
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Option 3, dynamic percentage determined ex-post, introduces the same concept of disconnecting the costs incurred by the SO and the energy imbalance price. Option 3 is more complex than Option 1 and 2, in particular the methodology to calculate the initial % value is difficult to determine, creating greater unnecessary. Uskmouth does acknowledge what the group was trying to achieve in suggesting links to system stress, etc but we do not feel that the outcome would necessarily be robust.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference:
			2nd Preference:
			3rd Preference:
			No Preference: All 3 options are disliked in comparison to the current Code baseline.

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Q	Question	Response	Rationale
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	A participant's view on whether to balance its position, prior to gate closure, is dependent upon the expected imbalance price. Option 1, a fixed 5%, provides a much weaker incentive to balance than the current arrangements, hence the SO becoming responsible for the majority of participant's balancing. This would then have impacts on other parts of the market, none of which we could consider are likely to be positive when considering the development of a competitive market for generation and supply.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	No	
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	If the imbalance price is no longer going to reflect the balancing costs undertaken by the SO, and is likely to be at a discount, then you could expect SO costs of balancing the system to increase. In aggregate, larger actions by the SO are required in real time.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	Any changes to the pricing value/methodology need to go through the BSC modification process and be evaluated against the BSC Objectives.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	
14.	Are there any further comments on P212 that you wish to make?	No	

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Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Kirsten Elliott-Smith*
Company Name:	*Immingham CHP LLP*
No. of BSC Parties Represented	*2*
Parties Represented	*Immingham CHP LLP, ConocoPhillips UK Ltd*
No. of Non BSC Parties Represented (e.g. Agents)	
Non Parties represented	
Role of Respondent	*Trading party, trader*
Does this response contain confidential information?	*No*

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	The objective should be to provide a fair reflection of the cost of balancing energy for uncontracted trades, while embracing incentives to contract. In doing this cash-out must enable the SO to take actions efficiently and not distort competition between market participants by allocating system costs or costs that more appropriately should be socialised. The arrangements should also facilitate transparency and simplicity.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	Hard analysis should be utilised to guide informed decisions on these matters. Detailed examination of historic price stacks should also help to better understand the derivation of the costs and assess the scale of the deficiencies, and in so doing provide a baseline against which rule changes can be properly assessed.

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Q	Question	Response	Rationale
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	Ofgem's P205 decision letter and analysis presented by National Grid at the 30 March cash-out review industry meeting shows there is presently significant pollution in energy imbalance under current pricing rules, and thus a clear defect. The defect operates in such a way as to systematically disadvantage smaller parties and non-portfolio players.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	Both are important.	The approach to cash-out should be transparent and comprehensible to the greatest extent possible and that prices can be verified where necessary. Smaller parties will naturally have a preference for simplicity. At present there is no ability to determine what the imbalance price might be in any particular imbalance period, and it is very difficult for a generator to manage the risk of plant failure. Ultimately there will always be judgments about what is cost-reflective, but it is clear that there are real distortions under the current cash-out rules with system costs being mis-targeted. If the design principle is to be causer pays, it is obviously important that only energy imbalance costs are allocated to the causer otherwise the charging mechanism will remain penal and discriminatory.
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	It would guarantee a price that was higher than the market reference price, which in turn would reflect the market price for short-term energy. By avoiding use of the current tagging rules it would nullify the competitive distortions inherent in the current arrangements. It should also reduce current incentives on parties to over-contract, and which creates an avoidable cost for the SO and ultimately consumers.

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Q	Question	Response	Rationale
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	While in principle the concept of a profiled percentage has merit, the proposed approach represented by option 2 is penal in its effect. Option 2 also draws on an assumption about RCRC, which is misplaced. RCRC is a by-product of the cash-out rules, and realised values have been inflated by the operation of the current cash-out rules. Setting out to preserve the overall surpluses by adding inflated premia entrenches an unwarranted cost on imbalance parties, and is arguably more discriminatory than the current baseline.
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	As with option 1 it would guarantee a price that was higher than the market reference price, which in turn would reflect the market price for short-term energy. Again by avoiding use of the current tagging rules, it would nullify the competitive distortions inherent in the current arrangements. Such an approach would also have merit in that it provides a linkage to the state of the physical imbalance on the system varying the incentive to contract during periods of system stress.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: Option 3, assuming it can be linked to NIV. Utilisation of the ratio of NIV to demand also warrants further assessment. See response to Q7.
			2nd Preference: Option 1. See also response to Q5.
			3rd Preference: Variant on option may also have merit, with premia of 10, 15% and 20%. See also response to Q13 below.

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Q	Question	Response	Rationale
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	The imbalance price under all the P212 options will preserve a strong incentive to contract because it will produce above-market prices. If it were considered—after suitable analysis—that there might be occasions on which parties were electing to avoid contracting because of an expectation that they would face a higher price then option 3 is to be preferred. The argument put forward in the assessment report that parties would be more inclined to resort to imbalance exposure to avoid expensive trades is a spurious one. Where a trade was declined but the system were short, the incremental energy would still be taken after Gate Closure and the costs levied on imbalance parties who were short together with the premium applied by P212. Logically "fear of cash-out" should increase in this situation as generators compete to avoid the premia.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	A 5% uplift is sufficient to create a strong incentive to avoid imbalance in most instances. During periods of system stress the increment would be from a much higher base increasing the absolute cost incentive to contract.
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	It is difficult to anticipate behavioural change. There is an argument that the incentive to contract is sufficient and should not greatly impact on participants' decisions. Perversely the higher the cost premium the more likely parties are to over-contract, thereby increasing the SO's costs. We have noted above a situation where a party might avoid to trade out its imbalance, but pointed out that the costs of the shortfall would still be realised and targeted on short parties. It is acknowledged that in such instances the SO's costs could be greater but the cost to the system as a whole (and therefore to consumers) may be less. The probability of this outcome is likely to be reinforced because the SO may well hold options over flexible generation and demand which many participants cannot ordinarily access and possibly at better prices.

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Q	Question	Response	Rationale
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	No	It is important that the rules can be applied flexibly. Any requirement for a rule change will mean the revised mechanism would be cumbersome. An approach analogous to other key parameters such as CADL where the rule can be reviewed by the panel following consultation with the added surety of an Ofgem veto would seem appropriate (option 2 of the three governance options listed).
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	Yes	There is a range of possible options for setting the premium/discount, which seem not to have been tested. The degree of rigour applied in other review processes (e.g. CADL where a range of definitions ranging from +/- 5% in 1% steps over the current arrangements were examined) has not been applied by the P212 modification group. According we would have expected to see analysis and comment on the effect of applying a 10%, then 15% and perhaps a 20% adjustment, before defaulting to an alternative (option 2) that seems designed to maintain RCRC levels (which itself is a distortion of cash-out and gives rise to a cross-subsidy).

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Q	Question	Response	Rationale
14.	Are there any further comments on P212 that you wish to make?	Yes	A key impediment to proper assessment of P212 is the failure of the group to identify a benchmark for the optimal imbalance price. The report notes (p17) that as a result the group could not conclude whether the proposed solutions was a better estimate of the true energy costs of the SO's balancing actions. Use of the market based reference price in any of its formulation has merit because: +it removes arbitrary distortions arsing from the tagging rules under the current methodology, which is having major competitive distortions and which is operating as a barrier to entry +it has the considerable advantage of simplicity and transparency Again, by eliminating the tagging rules a major cause of complexity—in effect a barrier to entry—would be removed. A market-based reference price would reflect the value of short-term energy trades, which is a key design objective of cash-out. It may also reduce the volatility and improve the predictability of the main imbalance price. It should reduce the tendency for parties to over-contract, improving the efficiency of the actions taken by the system operator. The reluctance of the modification group to tackle the details of a suitable arrangement and carry out an appropriate level of analysis should not obscure these basic principles.

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Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Ian Moss*
Company Name:	*APX*
No. of BSC Parties Represented	*2*
Parties Represented	*APX Power Ltd, APX Commodities Ltd.*
No. of Non BSC Parties Represented (e.g. Agents)	*1*
Non Parties represented	*APXMIDP (Market Index Data Provider)*
Role of Respondent	*Trader (non-physical)*
Does this response contain confidential information?	*No*

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	To provide a fair price for the Half Hourly Energy that is required to resolve parties' imbalances. The price should be reflective of the cost of sourcing short term half hourly energy, which is not usually the same costs as faced by the SO in the balancing mechanism. Prices as submitted into the balancing mechanism are for services required by the SO, which are more than HH energy, hence any price derived from the BM prices will contain a 'system' element. If the price of HH energy rises the closer you get to delivery, then the imbalance price will be at a premium to the market price, hence providing an incentive to balance.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	System actions not influencing energy imbalance price; improvements in liquidity of markets.

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Q	Question	Response	Rationale
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	The analysis has identified periods when system actions have affected the imbalance prices. The frequency in which this occurs is less clear, however, as stated above, the prices submitted into the BM are influenced by the product the SO is buying, (not simply HH energy), hence it is possible to argue that system actions influence the price in every period.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	Simple does not have to mean 'not cost-reflective', neither is complexity necessarily a problem provided it is transparent and based on understood actions. The biggest problem with the current arrangements is that the imbalance prices are based on actions taken by the SO to resolve more than HH energy imbalances. The current arrangements are complex as they are trying to de-gut SO actions into system and energy actions, which is nigh on impossible, yet over time, more 'refinements' have been added to the rules to try and improve the 'accuracy'.
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	An ex-ante price is likely to lead to a change in the behaviour of trading parties to influence the market price and hence the imbalance price. This may have adverse consequences – further analysis should be undertaken to investigate the drivers on parties and likely behaviour.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	An ex-ante price is likely to lead to a change in the behaviour of trading parties to influence the market price and hence the imbalance price. This may have adverse consequences – further analysis should be undertaken to investigate the drivers on parties and likely behaviour.

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Q	Question	Response	Rationale
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	A dynamic ex-post percentage is certainly an improvement to options 1 & 2 as parties do not know exactly what the price will be and are less likely to alter their behaviour post market close to take advantage of a favourable price, as this is likely to be counter-productive. A link to NIV has the advantage of introducing some price elasticity, if more HH energy is required, the more it is likely to cost. This option has the potential to be an improvement on the current baseline, but further detail is required on the rules/methodology of the price setting mechanism.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: 3
			2nd Preference: 2
			3rd Preference: 1
			No Preference:
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	A fixed percentage is may lead to some parties trading on the market to influence the imbalance cash-out price, rather than resolve their imbalances, which may leave the SO with the task of resolving larger imbalance positions. The first trade could be crucial in setting the trading pattern, and subsequent trades may well sit within the +/- 5% tolerance. This may have an effect on market liquidity, leading to an erosion in the confidence of the settlement arrangements.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	The analysis shows that currently cash-out prices are more than 5% higher than the market price, (but the current cash-out prices do include the system pollution), therefore a higher premium may well be justified. A higher premium may be a stronger incentive to balance, or may be a stronger incentive to 'influence' the market price. A larger percentage will constrain less the prices at which participants will be willing to trade on the market.

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Q	Question	Response	Rationale
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	An ex-ante price setting mechanism may encourage parties to 'adjust' their position post market close, (currently 30 minutes prior to gate closure), to take advantage of a favourable imbalance price, which may lead to an increase in SO costs. This effect could be ameliorated by changing the rules on contract notification to allow the spot market to remain open until gate closure. Grid Code obligations could minimise post gate closure position changes.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	As a key part of the pricing mechanism, changes to the premium should follow a robust consultation and approval process, which the modification process provides.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	Yes	Investigating whether the SO should trade to explicitly resolve half hourly energy imbalances, (and transacting in the BM to ensure system is in balance moment by moment and resolve constraints etc.).

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Q	Question	Response	Rationale
14.	Are there any further comments on P212 that you wish to make?	Yes	Since the introduction of the Market Index Price in setting the reverse price, the market price has proved itself to be a reliable index to base the cash-out prices on. APX would be concerned if any modification were to be approved that would materially change the rationale that parties had for trading on the APX exchange e.g. from a market place for willing buyers and sellers, into an arena for price manipulation. The APX price currently reflects a fair price for short term half hourly energy and as such is suitable as a base for calculating imbalance cash-out prices and which should reflect the cost of HH energy. Trades undertaken in the BM are for the SO to balance the system moment by moment, irrespective if a party is contractually out of balance or not on an aggregated half hour basis. A cash-out solution that is based on market prices, has more merit in setting a half hour energy price, rather than trying to de-gut SO actions, who is necessarily trading a different product. Therefore APX supports the principle of using the spot market price as a basis for setting imbalance prices, but we feel that options 1 & 2 may change the nature of parties behaviour on the exchange. Option 3, being ex-post, has greater merits but would need further definition before it were to receive our support.

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	Stuart Cotten
Company Name:	Drax Power Limited
No. of BSC Parties Represented	1
Parties Represented	Drax Power Limited
No. of Non BSC Parties Represented (e.g. Agents)	0
Non Parties represented	n/a
Role of Respondent	Generator
Does this response contain confidential information?	No

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	The aim of imbalance prices under the BSC should be to recover the costs of the System Operator to balance the system, based upon the Bid / Offer acceptances that the System Operator was required to take in a given settlement period. The price should reflect the balancing of energy on the system, excluding, where possible, 'energy plus' balancing actions. The volatility of such prices, due to the unpredictable nature of imbalances in a given settlement period, also act as an incentive for Parties to balance their position prior to Gate Closure.

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Q	Question	Response	Rationale
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	The Modification would calculate a Main Imbalance Price that better reflects the actions that the System Operator had to take for purely energy balancing reasons. The modification should demonstrate that the proposed solution would make improvements over the status quo.
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	At present, we share the view of the Modification Group that a sufficient level of materiality is yet to be established. It would appear that P211 and P212 seek to address the same perceived defect, which is the inclusion of 'energy plus' actions in the determination of the main imbalance price.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	We believe it is important to maintain cost reflectivity in the determination of the main imbalance price. In addition, the System Operator should have an incentive to choose the most cost efficient actions. P212 does not seek to establish this. A further consideration when developing a solution is that creating overly complex solutions may increase barriers to new entrants.

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Our main concerns are: • The decrease in volatility of the Main Imbalance Price will mean there is less incentive for Parties to balance (Objective B); • An increase in SO actions would increase costs and produce a less efficient system (Objective B); • Using an arbitrary number to determine the increase/decrease of imbalance prices would make such pricing less cost reflective of the SO actions in a given period. This would mean the costs incurred by the SO are less likely to be covered by the imbalanced Parties, with the whole industry being liable for the increased shortfall (Objective C).
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Same as above.
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Same as above, although there is more scope to make this option more cost reflective.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	No Preference: We believe that all three proposals involve an arbitrary figure that bares no resemblance to the true energy balancing costs incurred by the System Operator. Further development of Option 3 may help to create more cost reflective option.

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Q	Question	Response	Rationale
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	The volatility of the prices provides an incentive to market participants to aim to balance. The dampening of this incentive may lead to the need for more balancing transactions by the SO. This would result in a less efficient system and increased work load for the SO.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	The higher the percentage, the greater the incentive to balance. However, this does not make the imbalance price more cost reflective, it just produces a larger figure (increasing 'fear' of imbalance). In the case of Option 3 (where the percentage is dynamic), it would depend on the chosen structure. If the percentage was linked to the stress of the system, or the actions taken by/available to the SO, then this would add a degree of reflectivity.
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	We believe that the arbitrary nature of the three options will lead to an increase in SO costs. The modification will also lead to increased costs for all participants. As mentioned above, any decrease in incentive to balance will increase the volume of balancing transactions required by the SO, therefore increasing the cost to balance the system. The current system aims to retrieve costs from the parties that place the system in imbalance, whereas the loss of cost reflectivity under P212 may create a larger mismatch between the cost of SO actions and the recovery of costs from imbalance prices. Any shortfall in recovered costs would have to be recouped from all parties, including those that balanced their position.

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Q	Question	Response	Rationale
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	We believe that any changes to pricing value/methodology should only be undertaken after an appropriate assessment and consultation process.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	–
14.	Are there any further comments on P212 that you wish to make?	Yes	Although the modification seeks to address a defect in the calculation of the Main Imbalance Price, P212 does not (a) establish sufficient materiality of the defect to warrant such a change, and (b) uses an arbitrary figure as a basis to create a Main Imbalance Price that bares no resemblance to the true energy balancing costs incurred by the System Operator. We welcome the decision by the Modification Group to recommend further analysis of P212. We look forward to an opportunity to revise our comments once P212 has been developed further.

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Robert Longden*
Company Name:	*Airtricity*
No. of BSC Parties Represented	*1*
Parties Represented	Airtricity
No. of Non BSC Parties Represented (e.g. Agents)	
Non Parties represented	
Role of Respondent	*Trading Party Interconnector User*
Does this response contain confidential information?	*No*

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Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	Imbalance prices should act to provide: • An appropriate, but not **penal**, incentive to contract, for market participants • A reasonable reflection of the costs involved in performing **efficient** energy balancing actions for uncontracted trades. The process should not be distorted by actions taken by the SO for system reasons. It should allow and incentivise the SO to take actions in a timely efficient and economic manner. Where these actions have a distorting effect on energy markets, and compromise the ability of market participants to secure balancing trades themselves, market participants should not be exposed to the resultant increased imbalance costs. The arrangements should be as transparent and simple as possible, consistent with the need to facilitate and appropriately incentivise efficient balancing.

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Q	Question	Response	Rationale
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	Fully transparent and auditable records of the actions and cost allocations performed by the system operator. Analysis of imbalance volumes in the market against factors such as: • the ability to access appropriate traded mechanisms to achieve balance • inherent limitations on the ability of participants to balance • the costs of energy balancing • for those participants who are able to more easily balance, balancing "performance" over time, assessed on a consistent basis • the ability and performance of the SO in undertaking the necessary residual balancing of the system Assessment of performance, identification of deficiencies and development of proposed modifications or remedies, should be on the basis of sufficient hard data and full analysis of actual and prospective effects.
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	Both Ofgem's P205 decision letter and analysis presented by National Grid at the 30 March cash-out review industry meeting demonstrates that the present arrangements are both flawed and discriminatory. There is currently significant "pollution" in energy imbalance under current pricing rules, and thus a major defect. The defect operates in such a way as to systematically disadvantage smaller parties and non-portfolio players. Given the unequivocal evidence above, it is unclear why the modification process is asking this question. Effort should be focussed on addressing the clear defect in the current arrangements.

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Q	Question	Response	Rationale
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	Both are important.	Both are important. The pursuit of cost reflectivity for its own sake, without due regard to the complexities and sufficiencies of any incentives involved, is of little value. Complexity tends to promote obfuscation and the more complex the arrangements, the more time and effort that has to be devoted to understanding and verifying their outcomes. This results in arrangements being virtually impenetrable for all but the largest market participants. Provided that certain safeguards are in place, arrangements should be as simple and transparent as possible, whilst providing adequate and proportionate incentives. Provided that the objectives and incentives of any revised arrangements are aligned, then the desired behaviour will be facilitated There currently exist substantial distortions under the current cash-out rules with system costs being mis-allocated. Unless this is properly addressed, the charging mechanism will remain penal and discriminatory.
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	It would ensure the use of a price that was higher than the market reference price. This in turn would provide an effective proxy for a short-term energy market price. By moving away from the current tagging rules it would avoid the competitive distortions in the current arrangements, which have been noted by National Grid and Ofgem.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	The approach represented by option 2 is penal in its effect and should not be pursued.

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Q	Question	Response	Rationale
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	Similarly, option 3 would ensure the use of a price that was higher than the market reference price. This in turn would provide an effective proxy for a short-term energy market price. Option 3 would provide a dynamic linkage to the state of the physical system imbalance. This would sharpen the incentive to contract during periods of system stress.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	1, followed by 3.	Option 1 followed by option 3 Use of a market based reference price is preferable to the current situation: • it removes the major distortions arising from the tagging rules under the current methodology • it is both simple and transparent, thus reducing barriers to market entry A market-based reference price would more appropriately reflect the value of short-term energy trades, for which cash-out is supposed to act as a proxy. It should reduce the incentive on market participants to over-contract, improving both the efficiency of the actions taken by the system operator and overall market dynamics.

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Q	Question	Response	Rationale
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	The resulting imbalance price under P212 will continue to provide a strong incentive to contract, due to its linkage with "above-market" prices. If experience and suitable analysis confirmed that the incentive needed to be further strengthened, option 3 would be appropriate. The assessment report suggests that parties may have an incentive to "avoid" an expensive trade and elect to be exposed to imbalance costs. This is highly unlikely to be the case. A party electing to do this when the system was short, would be exposed to higher costs. The system operator would use available incremental energy, post gate closure and levy the cost, *plus P212 margin*, on out of balance parties.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	A 5% premium is material and provides a strong incentive to avoid imbalance. As the percentage rose, particularly at times of high cost/ system stress the resulting incentive would be sharpened significantly. Care needs to be taken to consider the impact of such a large absolute cost on those market participants who are unavoidably out of balance, such as renewable generation to avoid an incentive turning into a penalty.

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Q	Question	Response	Rationale
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	If the proposed options provide appropriate and sufficient incentives on market participants to achieve balance, then the costs of the SO should tend to reduce. By increasing transparency for both market participants and the SO, more efficient decisions should be expected, better balancing strategies developed and costs reduced. In common with a consideration of the incentives on market participants, a full examination should be made of the strategies used by the SO in performing its balancing role. The SO has a wider suite of options available, [including generation and demand side options over various timescales] than the majority of market participants and the exercise of these options will have a material impact on the ability of smaller non-integrated players to secure effective balancing services.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	No	Of the change control methods discussed, Option Two is preferred. Other key parameters such as CADL can be reviewed by the BSC panel following consultation – this would appear to be a similar process. The use of an Ofgem review and acceptance/veto gives added confidence.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	Yes	There is merit in a more rigorous approach to analysing the range of potential discount/premium. The modification group does not appear to have given sufficient detailed consideration to this area. The use of market based references is not confined to the UK. Insufficient consideration has been given to the experience and features associated with overseas markets which employ a market based element in their “cash-out” arrangements.
14.	Are there any further comments on P212 that you wish	Yes	The assessment report does not contain sufficient rigorous analysis

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Q	Question	Response	Rationale
	to make?		for many of the statements made within it. We have noted above, that imbalance prices should provide a sufficient incentive for parties to contract, where they are able, but not result in excessive, unreflective prices which constitute a penal regime. A fundamental component of the consideration of imbalance pricing is thus what constitutes a sufficient incentive. The P212 Modification Group does not appear to have given this issue proper consideration. The establishment of any imbalance pricing methodology requires this element to be properly established, prior to a discussion of the merits of any particular process for derivation. We have also noted that, in common with a consideration of the incentives on market participants, a full examination should be made of the strategies used by the SO in performing its balancing role. The SO has a wider suite of options available, [including generation and demand side options over various timescales] than the majority of market participants and the exercise of these options will have a material impact on the ability of smaller non-integrated players to secure effective balancing services. There is no quantitative assessment of changes in SO costs. Without this, as the group has noted, the assessment of the impact of any changes on the *true* energy costs of the SO's balancing actions will necessarily be compromised. The level and quantity of analysis appears inadequate. Given the importance of the issues involved, thorough and complete numerical analysis is required. Trades undertaken on power exchanges feed into market prices provided by Market Index Data Providers (or a single provider, as it currently stands). However, this needs to be expanded to examine

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Q	Question	Response	Rationale
			how the price formation process actually works in the short term forward market. There appears to be concern expressed with regard to the ability of participants to use a price known ahead of despatch but after gate closure in an anti-competitive manner – there is no supporting evidence or analysis to explain or support this contention. Given the high level of data capture in the market, it is difficult to understand how such actions might be achieved, or if undertaken, remain outside the scope of various remedial actions and safeguards which already exist.

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Libby Glazebrook*
Company Name:	*International Power*
No. of BSC Parties Represented	*Five*
Parties Represented	*First Hydro Company, Rugeley Power Generation Ltd., Saltend Co-generation Limited, Deeside Power Development Company Ltd, Indian Queens Power Ltd.*
No. of Non BSC Parties Represented (e.g. Agents)	*None*
Non Parties represented	*None*
Role of Respondent	*Generator*
Does this response contain confidential information?	*No*

Q	Question	Response Error! Bookmark not defined.	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	To charge parties that fail to balance their contract positions at gate closure with the costs that the SO incurs in balancing on their behalf.

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Q	Question	Response Error! Bookmark not defined.	Rationale
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	Primarily by ensuring that the costs that the SO incurs are being targeted on Parties accurately, by examining these costs against imbalance prices. By implication, cashout prices not derived from actual bid/offer activity (as under P212.) would be unlikely to achieve this aim. Disconnecting cashout prices from the balancing mechanism activity would be detrimental to market efficiency, and this important link must be maintained. International Power believes that the current mechanism performs well in targeting the costs of balancing actions on those that cause them; the analysis presented by the SO has demonstrated that they are within around 8% of the 'ideal' which suggests an excellent degree of cost reflectivity. P212 represents a significant departure from the current arrangements – therefore it should be noted that any comparison of price impacts become less reliable due to the potential for changes in market behaviour where incentives are shifted. Care therefore needs to be taken in using any results to determine whether either mod is better than the current arrangements. However, in terms of the key aim set out in our answer to Q1, it is clear that P212 will result in a significant deterioration of cost-reflectivity.

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Q	Question	Response Error! Bookmark not defined.	Rationale
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	The analysis presented by National Grid at the 30 March CORWG meeting suggested that for the month of November 2006, the SBP was 7% too high and the SSP 9% too low as a result of non energy related actions feeding into cashout prices. Subsequent to the 30 March meeting, National Grid placed numerous caveats on their analysis (it ignored dynamics, ignored the actual value of NDZ when it was less than 89mins, was based on one month's worth of data etc.). National Grid opined that the level of sub optimality lay somewhere between 0 and 7%. The NG analysis seems to have been taken out of context by the Proposer and used to justify a modification that will severely dampen cashout prices The modification describes the perceived defect as follows: "the current rules are not producing a clean energy price. This arises because the current tagging rules that seek to remove certain balancing actions … are defective and are resulting in a high level of pollution of the energy price". Our view is that this perception is misplaced, and overstates the impact of system balancing actions on cashout prices Just looking at constraints, whilst they do still occur, this is not to the extent immediately post BETTA both in quantity and cost to manage. There have been very few recent examples of constraints resulting in any change to cashout prices, and if they have, this impact has been negligible. Scottish bid prices are now usually close to or at the top of the bid merit order and so cannot be having much of an impact on lowering the SSP. When constraints have been apparent, these have been managed through the use of system PGBTs which do not affect the SSP. Of the other actions taken to balance that are not purely for energy ('energy plus' actions), these actions could still be in merit. Just because they contain 'energy plus' elements, it does not necessarily mean they are wrong or that they pollute the energy price. We conclude that the extent of the defect has been exaggerated. Cost reflectivity is more important than the removal of a small degree of system pollution in cashout prices, especially where this removal is being proposed through radical, and disproportionate overhaul of the regime.

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Q	Question	Response Error! Bookmark not defined.	Rationale

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Q	Question	Response Error! Bookmark not defined.	Rationale
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	Ideally both are desirable, and it is possible to achieve aspects of both. However, of the two, cost reflectivity is more important. Some level of complexity is necessary, and, especially when coupled with transparency, entirely appropriate. Cost reflective cashout prices encourage parties to take rational trading decisions. Currently, if a 'short' party sees, for example, a strong signal of need for additional generation (e.g oil plant warmed by the SO for potential use over peak), it will react to avoid the potential consequences of being exposed to this price via SBP either by bringing on its own plant or buying MW from another party in the short term markets. If the party does neither of these, it will face the imbalance price. P212 will tend to weaken this signal as there will be no direct connection between cashout prices and actions taken to balance - instead there is a direct link between market price and the outturn cashout price. Parties will make a rational decision to only trade in the forward market if the price at which they expect to be able to transact is lower than the imbalance price they expect to face at that point in time. We anticipate the impact of P212 to be detrimental to short term market liquidity – the link to market prices will mean that parties will be reticent about covering short positions so as not to increase SBP exposure through their actions. This will also lead to a *widening* gap between cashout prices and balancing costs, even in the event that some indirect link is initially established through, for example, profiled percentage premia. Liquidity in half-hourly contracts is already fragile and patchy. Any deterioration in short term market activity will be damaging to competition. A cost reflective mechanism is not a barrier to entry for small players provided they are able to trade and balance their positions. Any difficulties with trading or balancing (e.g. lack of liquidity for small volumes) will still remain (unless there is no cashout price) regardless of the cashout mechanism. Market rule changes may in fact create a barrier to entry for smaller players as P212 is a significant departure from the current arrangements (and any previous version of the current arrangements). Companies will have to undertake completely new analysis and historic data will be worthless, especially given that participant behaviour will change if P212 is implemented.

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Q	Question	Response Error! Bookmark not defined.	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Whilst we do not support this modification whatever the percentage, setting it at 5% will discourage contracting where the next available price in the PX is more than 5% of the weighted average of the MIDP to that point. Parties will choose to pay the imbalance price rather than trade in the PX. The SO will have to take more actions to balance the system which will increase balancing costs and BSUoS charges. These costs will then be socialised across the market rather than targeted on those who cause the actions to be taken. This is neither efficient nor economic, and the resulting cross subsidy is detrimental to competition. In any case, it is patently clear that a fixed 5% in no way reflects historic balancing costs.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	To come up with a variable percentage that has any justification, there has to be a baseline against which to measure it. The current cashout prices cannot in the context of this mod provide the baseline as they are perceived to be "wrong". Other than the analysis presented by National Grid, we have no feel for the precise extent of system pollution (however as discussed above we do not believe it is a significant factor.) Even if a baseline were to be agreed using current data, the variable percentages would have to be revisited periodically to ensure they were still appropriate. Following implementation of P212, cashout prices will change in response to the new incentives; pre P212 analysis would then be meaningless. If the percentages did need to be changed, how would such a change be assessed? Proposed option 2 suggests using an idealised RCRC using the National Grid analysis referred to in Q3 and then recreating the RCRC by varying the day and night percentages. Any number of combinations of the four percentages might get to the same value of RCRC. Without a baseline, how can the right combination be determined? We do not view this proposal as being workable, and can be expected to have an adverse impact - it cannot therefore better facilitate the BSC objectives.

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Q	Question	Response Error! Bookmark not defined.	Rationale
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	All of the options considered by the mod group for a dynamic percentage have their limitations. Using demand as an indicator will require a definition of demand and will either not be real time and hence a good indicator of system stress or if it is real time, will not be available to allow prompt price reporting. The extent of NIV is a poor indicator of the cost to balance the system as a NIV of 500MW off peak will cost far less to manage than one in period 35 in winter. MELNGC less demand is a poor indicator of system tightness as MELNGC ignores feasibility of delivery. Since none of these would work, they cannot better facilitate the BSC objectives.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: Option 2 provided the variable percentage has some link to reality and a baseline against which to compare it can be agreed. If this is not possible, Option 1 is our fisrt preference.
			2nd Preference: Option 1 - this is the only workable option but the proposed percentages would not incetivise parties to balance.
			3rd Preference: Option 3 – in its current state it is unworkable
			No Preference:

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Q	Question	Response Error! Bookmark not defined.	Rationale
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes/No	See answer given to Q4. We believe that the use of a fixed 5% adjustment will reduce market liquidity, widen the gap between market and balancing activity, and increase residual balancing costs for the SO. Using any of the alternative methodologies, but particularly in the case of the fixed 5% proposal, the percentage adjustment prevailing in any specific half hour is very unlikely to reflect the true costs of the marginal plant required to balance the system. This will deter participants from taking trading actions to balance. This is even more pertinent at times of peak demand where the generating supply curve may be at its steepest. For instance, if a settlement period has traded around £30, but the only offers left available (reflecting higher priced peaking plant) are, say £100/MWh , a market participant that suffers some generation loss, will never, under P212, seek to lift this offer. It will have a high degree of confidence that SBP will outturn at £31.50/MWh. In the balancing mechanism of course the unit offered at £100/MWh is likely to be utilised to help balance the system on its behalf.

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Q	Question	Response Error! Bookmark not defined.	Rationale
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	As described above, under a low percentage P212, we would expect stifled liquidity in the short term markets as participants withhold from trading in order not to influence imbalance prices to which they may be exposed on residual volumes. Clearly as the % increases, the incentive to avoid trading will reduce. However, other (perverse) incentives might be created. For instance, where a party is short, and in periods of low liquidity, it may be incentivised to actually sell volume in order to push the market price down, thereby reducing its overall imbalance exposure. Even if the percentage was set at a level that bore some relationships to historic cashout prices (analysis by ELEXON shows that on average the SBP is around 1.8 times the market price and SSP around 0.8 times the market price) it would still not be appropriate at times of system stress. Taking a very recent example of Friday 24 August 2007. Day Ahead, the peak period (7am – 7pm) traded at £38.05/MWh on the broker screens. The power exchange was showing prices typically at around £40/MWh over this period although at this point it had not traded. An oil plant was warmed on 12 hours notice and synchronised at 9:30am. Because of the higher offer price on the oil plant (£290/MWh) and the expectation that this would increase the SBP, the power exchange price started to increase throughout the early hours of 24 August, and traded for period 23 (11-11:30am) at a peak of £170/MWh. Had P212 been in place, even with a cashout price that was 1.8 times the market price, the market would have continued to trade around the £40/MWh mark because there would be no reason for it to go higher (other than a step change in fuel costs or a perception of an increased value to reflect that the system was short). Even if prices did increase in a P212 world, they would increase at a much slower rate rather than the step change seen under the current arrangements on 24 August. Under P212, PX prices will not move to reflect the actions that the SO is taking, they will only change in response to activity in the PX. Furthermore, as noted in Q6, no percentage can be justified since there is no ideal price against which to compare a P212 type price to establish if the percentage is correct.

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Q	Question	Response Error! Bookmark not defined.	Rationale
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	We would expect SO costs to increase if the percentage is set less than that implied by the current arrangements, as the SO will have to take more actions to balance to compensate for reduced trading actions. Conversely, SO costs could fall if the percentage was set higher.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	It is vital that any change is discussed and debated in detail by industry experts in this complicated area. Therefore we agree that the modification route should be used.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	We do not believe that basing cashout prices on trades undertaken in the forward market is appropriate as these trades do not (and cannot) take account of the actions taken by the SO to balance the system post gate closure.
14.	Are there any further comments on P212 that you wish to make?	Yes / No	The Proposer has provided no justification for the +/-5% value. Because of this, it has been very difficult for the mod group to assess whether P212 mod better facilitates the BSC objectives. Parties will make a rational decision to only trade in the forward market if the price they see is lower than the imbalance price they would face. Currently, there is already declining liquidity in the power exchange. As outlined in various answers above, we have serious concerns about the impact that P212 will have on liquidity in the short term markets, and on the efficiency of market operation.

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment

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Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	**Scott Keen**
Company Name:	**InterGen (UK) Ltd**
No. of BSC Parties Represented	**4**
Parties Represented	**RPCL, SPAL, CECL, IETS**
No. of Non BSC Parties Represented (e.g. Agents)	**0**
Non Parties represented	
Role of Respondent	**Generator**
Does this response contain confidential information?	**N**

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	The aim of imbalance prices under the BSC is to provide sufficient incentive to market participants to balance to their contracted positions where they are able to do so. Imbalance prices do not need to be punitive to achieve this outcome. Punitive prices simply punish unnecessarily those parties who are unable to balance their position.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	Imbalance prices reflect the costs incurred by the SO in balancing the system from an energy perspective and are not influenced by the resolution of transmission constraints.

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Q	Question	Response	Rationale
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	The defect identified under P212 impacts market participants by inflating the punitive nature of system cash out prices so that they are over and above a level needed to incentivise participants to balance where they are able to do so. The 'polluting' of the energy price by inclusion of 'energy plus' actions exacerbates the punitive nature of cash out prices. This is highly detrimental in nature to smaller market participants in particular.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	Whilst cost-reflectivity is desirable, simplicity should be sought where it will assist in the transparency of actions or calculations and reduce admin costs.
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	The fixed percentage of 5% premium / discount on Market Reference Price option would facilitate more accurate and reliable forecasting of potential cash out values and greatly increase the transparency of the price calculations. It would also make system prices less punitive when compared to the current Code baseline which would encourage new entrants into the market so *promoting effective competition in the generation and supply of electricity and promoting such competition in the sale and purchase of electricity.*
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	The variable percentage option would also facilitate more accurate and reliable forecasting of potential cash out values although reduce the simplicity and transparency of the price calculations compared to a fixed percentage. It would also make system prices less punitive when compared to the current Code baseline which would encourage new entrants into the market so *promoting effective competition in the generation and supply of electricity and promoting such competition in the sale and purchase of electricity.*

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Q	Question	Response	Rationale
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	The dynamic percentage ex-post option would again facilitate more accurate and reliable forecasting of potential cash out values although to a lesser extent than a fixed or variable percentage. It would also reduce the simplicity and transparency of the price calculations compared to these options. However, it would also make system prices less punitive when compared to the current Code baseline which would encourage new entrants into the market so *promoting effective competition in the generation and supply of electricity and promoting such competition in the sale and purchase of electricity.*
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: 1
			2nd Preference: 2
			3rd Preference: 3
			No Preference: Rationale as per answers to Q5 to Q7.
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	The 5% premium / discount on Market Reference Price is sufficient incentive to balance for market participants so little change would be seen in market behaviour and there would be minimal impact on the SO.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	The 5% premium / discount on Market Reference Price is sufficient incentive so market participants would continue to balance where they are able to do so as the percentage increases.

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Q	Question	Response	Rationale
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	Since the 5% premium / discount provides sufficient incentive for market participants to balance where they are able to do so, there should be minimal change to the SO costs of balancing the system.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	This would increase the simplicity of the calculations and reduce the number of changes to the pricing value / methodology, reducing the requirement of IT system modifications and providing long term stability.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	
14.	Are there any further comments on P212 that you wish to make?	Yes	We fully support modifications which aim to reduce the unnecessarily punitive nature of system prices, which are detrimental to smaller market participants and new entrants in particular.

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Alastair Barnsley*
Company Name:	*E.ON UK Energy Services Limited*
No. of BSC Parties Represented	*0*
Parties Represented	
No. of Non BSC Parties Represented (e.g. Agents)	*1*
Non Parties represented	*E.ON UK Energy Services Limited*
Role of Respondent	*Party Agent*
Does this response contain confidential information?	*No*

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	We would like to make a neutral return to this consultation as the proposed modification will have no direct impact on our systems & processes.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	Please see response to question 1
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	No	
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	Please see response to question 1

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.		Please see response to question 1
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes/ No	Please see response to question 1
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes/ No	Please see response to question 1
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference: 2nd Preference: 3rd Preference: No Preference:
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	No	

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Q	Question	Response	Rationale
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	No	
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	No	
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes/No	Please see response to question 1
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	
14.	Are there any further comments on P212 that you wish to make?	No	

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Philip Catherall*
Company Name:	*The Renewable Energy Co Ltd*
No. of BSC Parties Represented	*1*
Parties Represented	ECOT
No. of Non BSC Parties Represented (e.g. Agents)	
Non Parties represented	
Role of Respondent	*Company Secretary*
Does this response contain confidential information?	*No*

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	The aim should be to fairly reflect the costs to the system of parties being out of balance.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	The system operator should be able to provide analysis to do this.
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	Ofgem have provided documented evidence that there is significant distortion in the calculation of SBP and SSP caused by unidentified system operator balancing actions.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	Simplicty over cost reflectivity	The simpler the better as everyone can then understand what is going on and make informed decisions on cash out.

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	A rational business will always try to minimise costs. The only question is how much the incentive to contract should be.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	This adds unnecessary complexity
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.		
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	1, followed by 3.	A market based price is a solution to avoiding the problem of system operator pollution.
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	See answer above point 5

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Q	Question	Response	Rationale
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	A 5% uplift is material and sufficient to create a strong incentive to avoid imbalance in most instances. During periods of system stress the increment would be from a much higher base increasing the absolute cost incentive to contract.
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	No	
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	No	
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	Yes	Discussions on cash out methodology have been ongoing for many years without a perfect solution appearing.
14.	Are there any further comments on P212 that you wish to make?	No	

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

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Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Keith Munday*
Company Name:	*BizzEnergy Ltd*
No. of BSC Parties Represented	*1*
Parties Represented	BizzEnergy Ltd
No. of Non BSC Parties Represented (e.g. Agents)	
Non Parties represented	
Role of Respondent	*Supplier*
Does this response contain confidential information?	*No*

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	The objective should be to provide a fair reflection of the cost of balancing energy for uncontracted trades, while embracing incentives to contract. It should fit with the principle of polluter pays and costs only targeted at those who have directly caused them. The arrangements should also facilitate transparency and simplicity.

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Q	Question	Response	Rationale
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	The level of NIV on a comparable basis should not be materially worse than historic levels. Imbalance costs should more closely reflect the energy trading costs of the MIP. There should not be distortions in terms of level or volatility due to system related actions. The mechanism should be simple and transparent such that more than a few people in the industry can understand how it works with confidence. Fear of cash out should not be a reason held by many for not entering the market. Participants only pay for the block energy cost of their imbalance and can have confidence that this has not been distorted by action from the system operator to manage the system. (Currently the other way around).

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Q	Question	Response	Rationale
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	Ofgem's P205 decision letter and analysis presented by National Grid at the 30 March cash-out review industry meeting shows there is presently significant pollution in energy imbalance under current pricing rules, and thus a clear defect. The defect operates in such a way as to systematically disadvantage smaller parties and non-portfolio players. The onus should be on the modification group to explain why it believes this analysis is flawed or incomplete, and it is not obvious why the report does not reprise this analysis before noting unsubstantiated opinions of modification group members that they doubt there is a deficiency. One aspect of the defect is that parties who are energy balanced over the settlement period but who within the period have caused the system operator to take actions bear no imbalance costs and their costs are carried by those out of balance. The group needs to demonstrate that this cannot happen in order to prove that a defect does not exist. The impact of this is that imbalance costs of smaller new suppliers who have less predictable load patterns are higher than they should be, as they are subsidising others.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	Both are important.	It is crucial that the basic approach to cash-out is transparent and comprehensible to the greatest extent possible and that prices can be verified where necessary. Smaller parties will naturally have a preference for simplicity. Ultimately there will always be judgments about what is cost-reflective, but it is clear that there are real distortions under the current cash-out rules with system costs being mis-targeted. If the design principle is to be causer pays, it is obviously important that only energy imbalance costs are allocated to the causer otherwise the charging mechanism will remain penal and discriminatory.

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Q	Question	Response	Rationale
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	It would guarantee a price that was higher than the market reference price (which the baseline does not do), which in turn would reflect the market price for short-term energy. By avoiding use of the current tagging rules it would nullify the competitive distortions inherent in the current arrangements.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	In principle the concept of a profiled percentage has merit, but the proposed approach represented by option 2 is penal in its effect. Setting out to preserve the overall surpluses from RCRC by adding inflated premia entrenches an unwarranted cost on imbalance parties, and is arguably more discriminatory than the current baseline.
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	Yes	Again it would guarantee a price that was higher than the market reference price, which in turn would reflect the market price for short-term energy. Such an approach would also have merit in that it provides a linkage to the state of the physical imbalance on the system varying the incentive to contract during periods of system stress. It is also an unknown until after the event and is therefore makes the imbalance price less predictable, which will encourage contracting.
8.	What is your order of preference of Options 1, 2 and 3	3, followed by 1.	1st Preference: Option 3, assuming it can be linked to NIV. 2nd Preference: Option 1.

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Q	Question	Response	Rationale
	for forming the Proposed Solution? Please provide rationale.		Use of the market based reference price in any of its formulation has merit because: +it removes arbitrary distortions arsing from the tagging rules under the current methodology, which is having major competitive distortions and which is operating as a barrier to entry +it has the considerable advantage of simplicity and transparency Again, by eliminating the tagging rules a major cause of complexity—in effect a barrier to entry—would be removed. Increases confidence in the market as it will be simple transparent and auditable and thus should encourage competition. A market-based reference price would reflect the value of short-term energy trades, which is a key design objective of cash-out. It may also reduce the volatility and improve the predictability of the main imbalance price, facilitating the greater adoption of more innovative tariffs. It should reduce the tendency for parties to over-contract, improving the efficiency of the actions taken by the system operator.
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour? Please provide rationale.	Yes	The imbalance price under all the options will preserve a strong incentive to contract because it will produce above-market prices. If it were considered after suitable analysis that there might be occasions on which parties were electing to avoid contracting because of an expectation that they would face a higher price then option 3 is to be preferred. The argument put forward in the assessment report that parties would be more inclined to resort to imbalance exposure to avoid expensive trades is flawed. As only the last executed trade can reasonably guess where outturn MIP prices will be.

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Q	Question	Response	Rationale
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	A 5% uplift is material and sufficient to create a strong incentive to avoid imbalance in most instances. During periods of system stress the increment would be from a much higher base increasing the absolute cost incentive to contract. No conclusive evidence has been produced to prove that 5% is too low or high, therefore it cannot be that unreasonable.
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	It is difficult to anticipate behavioural change. There is an argument that the incentive to contract is sufficient and should not greatly impact on participants' decisions. Perversely the higher the cost premium the more likely parties are to over-contract, thereby increasing the SO's costs. We have noted above a situation where a party might avoid to trade out its imbalance, but pointed out that the costs of the shortfall would still be realised and targeted on short parties. It is acknowledged that in such instances the SO's costs could be greater but the cost to the system as a whole (and therefore to consumers) may be less. The probability of this outcome is likely to be reinforced because the SO may well hold options over flexible generation and demand which many participants cannot ordinarily access and possibly at better prices.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a modification? (Section 2.3 final paragraph) Please provide rationale.	Yes	During its initial phase a full and open review of the mod should be carried out. A further modification could be raised to allow changes to the parameters in the light of market experience.
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	Yes	

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Q	Question	Response	Rationale
14.	Are there any further comments on P212 that you wish to make?	Yes	The group has failed to explore the merits of the proposal as an alternative method of formulating cash out prices. It has been taken as read that the current mechanism works and provides all the correct incentives. The nature of the analysis has been based on comparison of P212 against existing prices or P211 prices, rather than go back to fundamentals and seek to design a new mechanism and criticise it for its merits and faults. The data set for analysis is too restricted. Nine settlement periods should, as a minimum, be nine days (3 stress, 3 benign and 3 random). The volume of analysis made available to the group is in extreme contrast to other pricing mods such as P194, where the active engagement of parties in the assessment process enabled extensive quantitative analysis to be carried out. There is no quantitative assessment of changes in SO costs.

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P212 ASSESSMENT PROCEDURE CONSULTATION QUESTIONS

BSC Parties ("Parties") and other interested parties are invited to respond to this consultation expressing their views or provide any further evidence on any of the matters contained within this document. In particular views are sought in respect of the following questions. Parties are invited to supply the rationale for their responses.

Respondent:	*Martin Mate, Rob Rome*
Company Name:	*British Energy*
No. of BSC Parties Represented	*5*
Parties Represented	*British Energy Power & Energy Trading Ltd, British Energy Generation Ltd, Eggborough Power Ltd, British Energy Direct Ltd, British Energy Generation (UK) Ltd*
No. of Non BSC Parties Represented (e.g. Agents)	*-*
Non Parties represented	*-*
Role of Respondent	*Supplier/Generator/Trader/Consolidator/Exemptable Generator/Party Agent*
Does this response contain confidential information?	*No*

Q	Question	Response	Rationale
1.	What do you believe is the aim of imbalance prices under the BSC?	-	We believe that imbalance prices under the BSC should (1) be cost-reflective; (2) meet BSC objectives and (3) be transparent. Imbalance prices should have the effect of encouraging parties to balance prior to gate closure. Imbalance parties should be charged for the actions taken on their behalf collectively by the System Operator to balance the system. The BSC Objectives do not mention simplicity and therefore for the calculation of the main imbalance price, simplicity (alone and above all) is not an essential driver for change. If an appropriate mechanism can be simple as well as cost-reflective then that is naturally desirable, however the electricity trading arrangements are not simple so we doubt if it is a realistic and achievable target.

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Q	Question	Response	Rationale
			The reverse price assumes that parties whose outturn volume reduces the level of system imbalance do not impose additional balancing costs, and should face the price which prevailed in the forward markets as if they had forward traded that volume. Any effect they would have had on forward prices is ignored, as is the requirement on the System Operator to hold reserve to manage unbalanced positions.
2.	How could you demonstrate a measure of success that a Modification has better achieved the aim you have identified in Question 1?	-	There is no convenient measure of what is the most efficient level of System Operator costs. Low SO costs could be achieved at the expense of higher than efficient party costs or vice versa. However, by exposing individual imbalance parties to the cost of actions taken by the SO to resolve imbalance, participants – 'the market' – will make choices which will give an efficient outcome. If imbalance prices underestimate the costs of SO balancing, parties will not have incentive to manage their own imbalance and competitive advantage is gained by being the worst balancer (with costs borne by someone else). Conversely, if imbalance prices overestimate the costs of SO balancing, competitive advantage is gained by balancing well, and parties will trade with each other to avoid the cost. Incentives to balance well should be retained in this case.
3.	Do you have a view of the extent/impact of the perceived defect identified under P212 (and any link to the defect under P211)?	Yes	The proposer appears to envisage three defects: 1. Complexity. We do not view this as a defect. The aim of imbalance charges should be to reflect the costs of balancing actions as part of what is a very complex issue. Simplifications should only be considered where unavoidable or where the consequent inaccuracy is immaterial. If an appropriate mechanism can be simple as well as cost-reflective then that is naturally desirable, however the electricity trading arrangements are not simple so we doubt if simplicity alone is a realistic and achievable target.

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Q	Question	Response	Rationale
			2. Influence on imbalance prices of actions taken because of transmission constraints. We agree that it would be preferable if such actions did not influence imbalance prices, as individual parties have no control over them. However, there is very limited evidence of the extent of the problem, and we do not believe it to be significant at present. 3. Influence on imbalance prices of actions taken for what has been termed 'Energy Balancing Plus'. Many if not all actions classed as 'Energy plus' are taken solely for the purpose of efficiently balancing energy. It seems entirely rational that parties in imbalance should face those costs. There is an issue that the cost of such actions may not be correlated with the actual half-hourly imbalance in a given settlement period, but that does not mean they should be ignored in cashout. We do not consider that sharing these costs between all parties is a desirable or efficient objective. Linking back to P211, it is unclear to BE of the extent /impact of the perceived defect identified and that is due to the limited snapshot analysis upon which it has been based. New terms have been introduced to describe certain National Grid actions, such as "Energy Balancing Plus" which has not been defined clearly enough and is perhaps being used in the wrong context as these actions <u>do not</u> solely consist of transmission constraints or actions taken for system reasons.
4.	What are your views on 'simplicity' versus 'cost-reflectivity' on the calculation of the main imbalance price?	-	As described above, we believe that any cashout mechanism should (1) be cost-reflective; (2) meet BSC objectives and (3) be transparent. The BSC Objectives do not mention simplicity and therefore for the calculation of the main imbalance price, simplicity (alone and above all) is not an essential driver for change. If an appropriate mechanism can be simple as well as cost-reflective then that is naturally desirable, however the electricity trading arrangements are not simple so we doubt if it is a

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Q	Question	Response	Rationale
			realistic and achievable target. The aim of imbalance charges should be to reflect the costs of balancing actions. Simplifications should only be considered where unavoidable or where the consequent inaccuracy is immaterial. Simplicity in itself should not be an objective. Parties face a choice between the costs of trading energy and related products bilaterally to meet their individual energy requirements, and the cost of being exposed to imbalance. Unless the imbalance price to which a party is exposed is equivalent to, or reflective of, the price it would have faced bilaterally to trade the same energy **at the same time as the SO**, it will not make efficient decisions. When the imbalance price is reflective of costs faced by the SO, the market will decide the level at which it is more efficient for the System Operator to balance collectively: parties will trade forward where it is more cost-effective, and otherwise leave balancing to the SO. If the imbalance price is more expensive than the actual price of actions taken by the SO, parties will inefficiently spend too much bilaterally avoiding imbalance. If it is too cheap, then some parties will spend too little, the SO will spend more, which is inefficient, and the actual cost must be made up by others. Determination of a cost-reflective price is a pre-requisite to achieving efficient overall balancing (assuming the cost of such determination is much less than cost of balancing energy itself, which all evidence suggests is the case). Simplicity is desirable provided the cost of inefficiencies due to approximations inherent in simplicity are not significant. In this case: a. We do not consider the non-quantified and subjective benefits of simplicity outweigh the obvious inaccuracy in cost-reflectivity of ignoring the real constraints of plant dynamics and lack of perfect foresight. This is particularly true in a wholesale market where

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Q	Question	Response	Rationale
			achievement of energy requirements should be the core activity. b. We believe the current arrangements are simple in principle: the costs of actions actually taken by the system operator on behalf of parties which are in imbalance are used to determine the imbalance price. This is at least as simple as the proposed method of using hypothetical volumes which meet essentially arbitrary criteria relating to apparent availability.
5.	Do you believe the fixed percentage (Proposed Option 1 - specifically a fixed percentage of 5%) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	It is clear from analysis performed that a fixed premium/discount to short term forward market prices would not be in any way reflective of the costs of actions taken by the System Operator to resolve short term imbalances up to real time. It would vastly underestimate the costs. Therefore: (a) If individual parties face lower costs than those of the balancing actions taken on their behalf, there must be a risk either to (i) security of supply because they won't procure enough energy for all situations or (ii) to efficient balancing activity because the System Operator will have to procure actions which parties could have procured more cheaply themselves. Therefore BSC Objective A relating to System Operator licence conditions would not be better met. (b) If individual parties face lower costs than those of the balancing actions taken on their behalf, the System Operator will have to procure actions which parties could have procured more cheaply themselves. Also, if parties have less incentive to balance, the uncertainty and cost of actions required to be taken by the SO would increase. This would not be efficient. Therefore BSC Objective B relating to efficient system operation would not be better met. (c) If individual parties face lower costs than those of the balancing actions taken on their behalf, and the additional cost of actions taken by the System Operator are shared amongst all parties, then some parties must be subsidising others. Therefore BSC Objective C relating to competition would not be better met. (d) The cost of implementing this proposal or its alternative would be

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Q	Question	Response	Rationale
			considerable and no benefit in terms of ongoing administration of BSC activities is envisaged. Therefore BSC Objective D relating to administrative efficiency of would not be better met.
6.	Do you believe the variable percentage (proposed option 2) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	Again, prices would not track actual imbalance costs and the proposal is far inferior to the present arrangements for reflecting costs of SO actions.
7.	Do you believe the dynamic percentage determined ex-post (proposed option 3) would better facilitate the achievement of the Applicable BSC Objectives when compared to the current Code baseline. Please provide rationale.	No	A dynamic percentage would have potential to reflect costs more closely than option 1 (fixed 5%) or 2 (variable percentage), given that some correlation between system net imbalance or system margin and imbalance costs is likely. However, the correlation is likely to be poor and prices would not track actual imbalance costs, and the proposal is far inferior to the present arrangements for reflecting costs of SO actions. Again, why use a proxy for costs rather than the costs themselves? Any variable percentage used as a proxy for System Operator costs would be ludicrous when the System Operator costs are known.
8.	What is your order of preference of Options 1, 2 and 3 for forming the Proposed Solution? Please provide rationale.	-	1st Preference:
			2nd Preference:
			3rd Preference:
			No Preference: None of the options would be reflective of real outturn costs. Indicating a preference would suggest a degree of support which we cannot give.
9.	Do you have any views on how these solutions will influence market participants' balancing behaviours and any subsequent impact on the SO? Specifically, how would a fixed percentage of 5% affect behaviour?	Yes	If individual parties faced lower costs than those of the balancing actions taken on their behalf, there would be a tendency for parties to balance less accurately. This would increase the cost of actions required to be taken by the System Operator, even though many parties could balance their own position more cheaply. Since the additional cost would be less well

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Q	Question	Response	Rationale
	Please provide rationale.		reflected on those responsible, it would be shared amongst all parties, including those which balanced accurately. A fixed percentage of 5% would clearly vastly underestimate the cost of balancing actions taken by the System Operator to balance the system. Benefit would be gained by being the worst at balancing, as the true cost would be shared with all other participants. One scenario could be all parties trading only a proportion of their requirements, with all uncertainty and reserve being managed at great cost by the System Operator.
10.	Do you have any views on how market participants' balancing behaviours would adjust as the percentage increases from 5%? Please provide rationale.	Yes	If the price were set systematically below the cost of actions taken by the SO, the behaviour indicated in response to question 9 is likely: inefficient costs incurred by the System Operator. If and only if the level were set sufficiently high, then incentives to balance could be retained in most periods, though probably not in the most extreme conditions. However, without cost reflectivity there would be no confidence that efficient outcomes were being achieved. With a crude estimation of costs such as this, balancing incentives would not be matched to the periods where balancing costs are greatest (or least).
11.	Do you have a view on the impact of the three identified Proposed Options with regards to whether these will lead to an increase or decrease in the SO costs of balancing the system? Please provide rationale.	Yes	As described previously, the effect on SO costs would depend on the extent to which the resulting prices reflect the SO costs. If it is cheaper for participants to cash out and let everyone share the true costs of balancing actions incurred by the SO, then SO costs would increase. Conversely, if imbalances prices more than reflected SO costs, parties would take more measures to avoid imbalance and SO costs would reduce. None of the proposed approaches reflect real SO costs accurately. A very high premium/discount would be necessary to provide the correct incentives at times of 'system stress', but would not provide efficient incentives at other times.
12.	Do you agree with the Groups view that the pricing value/methodology should only be changed by a	Yes	A parameter or methodology having such significant influence on imbalance prices should only be changed with the full notice, assessment and consultation associated with a modification.

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Q	Question	Response	Rationale
	modification? (Section 2.3 final paragraph) Please provide rationale.		
13.	Do you believe there are any other solutions that the Modification Group has not identified and that should be considered? Please provide rationale.	No	Imbalance prices should reflect the cost of balancing actions taken by the System Operator. Market prices of trades made in advance take no account of the costs associated with resolving imbalance efficiently at short notice while allowing for dynamic constraints. Therefore it is difficult to see how any method using forward prices as a measure of balancing costs can provide better incentives for efficient balancing to all concerned.
14.	Are there any further comments on P212 that you wish to make?	Yes	This proposal and its variants fundamentally undermine the principle of cost reflective balancing on which the NETA arrangements are based. A proxy for SO costs should not be used in preference to SO costs themselves. Any de-linking of SO costs and cashout arrangements should be avoided in order for them to be cost-reflective in meeting BSC objectives.

Parties are encouraged to provide financial information with regard to either the costs or benefits of the Modification Proposal to support the Assessment Procedure. Where requested this information can be treated as confidential, although all information will be provided to the Authority.

Please send your responses by **17:00 on 29 August 2007** to modification.consultations@elexon.co.uk and please entitle your email 'P212 **Assessment Consultation**'. Please note that any responses received after the deadline may not receive due consideration by the Modification Group.

Any queries on the content of the consultation pro-forma should be addressed to Chris Stewart on 020 7380 4309, email address chris.stewart@elexon.co.uk.

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