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18 December 2003

The National Grid Company, BSC Signatories and
Other Interested Parties

Our Ref: MP No P144

Dear Colleague

Modification to the Balancing and Settlement Code (“BSC”) - Decision and Notice in relation to Modification Proposal P144: “Removal of CADL from the BSC”

The Gas and Electricity Markets Authority (the “Authority”)¹ has carefully considered the issues raised in the Modification Report² in respect of Modification Proposal P144, “Removal of CADL from the BSC”.

The BSC Panel (the “Panel”) recommended to the Authority that Proposed Modification P144 should not be made, but in the event that the Authority determines that the Proposed Modification should be made, the Implementation Date should be 5 Business Days after such an Authority determination.

Having carefully considered the Modification Report and the Panel’s recommendation and having regard to the Applicable BSC Objectives³, the Authority has decided not to direct a Modification to the BSC.

This letter explains the background and sets out the Authority’s reasons for its decision.

¹ Ofgem is the office of the Authority. The terms “Ofgem” and “the Authority” are used interchangeably in this letter.

² ELEXON document reference UMRP144, Version No. 1.0, dated 13 November 2003

³ The Applicable BSC Objectives, as contained in Standard Condition C3 (3) of National Grid Company’s (“NGC’s”) Transmission Licence, are:

- a) the efficient discharge by the licensee of the obligations imposed upon it by this licence;
- b) the efficient, economic and co-ordinated operation by the licensee of the licensee’s transmission system;
- c) promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity;
- d) promoting efficiency in the implementation and administration of the balancing and settlement arrangements
- e) the undertaking of work by BSCCo (as defined in the BSC) which is:
 - (i) necessary for the timely and effective implementation of the proposed British Electricity Trading and Transmission Arrangements (BETTA); and
 - (ii) relevant to the proposed GB wide balancing and settlement code;and does not prevent BSCCo performing its other functions under the BSC in accordance with its objectives.

Background

The Balancing Mechanism was designed to enable National Grid Company plc (“NGC”), as the System Operator (“SO”), amongst other things, to keep the transmission system (the “System”) in balance close to, and in, real time by adjusting levels of generation and demand via the Bids and Offers submitted to the Balancing Mechanism (“Electricity Balancing”). The SO also uses the Balancing Mechanism, amongst other things, to ensure that the System remains within safe operating limits⁴, and that the pattern of generation and demand is consistent with any System transmission constraints (“System Balancing”). System Balancing actions include, but are not limited to, frequency control and the alleviation of locational constraints. NGC, as SO, therefore incurs costs which can be approximately divided between costs associated with Electricity Balancing and costs associated with System Balancing.

Currently under the BSC, only the costs associated with Electricity Balancing actions are included in the calculation of Energy Imbalance Prices since these are the balancing actions taken by the SO to alleviate Electricity Imbalances directly attributable to Parties. In contrast, System Balancing actions are not included in the calculation of Energy Imbalance Prices. The costs associated with System Balancing are recovered from all users of NGC’s System through Balancing Services Use of System charges. Ensuring that only the costs incurred by the SO in Electricity Balancing are included in Energy Imbalance Prices minimises the potential for cross subsidies between participants, promoting effective competition in the generation and supply of electricity, and provides the SO with accurate signals of the costs of Electricity Balancing, promoting the efficient, economic and co-ordinated operation by the SO of the System.

There are two mechanisms included in the BSC for differentiating between those balancing actions taken for System Balancing reasons and those taken for Electricity Balancing reasons. First, Proposed Modification P18A (“Removing/Mitigating the effect of System Balancing Actions in the Imbalance Price Calculations”) sought to introduce a mechanism into the BSC to remove short duration Bid-Offer Acceptances (“BOAs”) associated with System Balancing actions, such as frequency control, from the calculation of Energy Imbalance Prices. The principle of Proposed Modification P18A was to exclude any BOA with a Continuous Acceptance Duration (“CAD”) of less than the value of the CAD limit (“CADL”) (initially set at 15 minutes) from the calculation of Energy Imbalance Prices on the basis that such acceptances were, in general, taken by the SO for System Balancing reasons. Under Proposed Modification P18A the BSC Panel may, from time to time, revise the value subject to approval by the Authority⁵. On 22 August 2001, the Authority decided to direct that Modification Proposal P18A should be made and implemented⁶. Hereafter this mechanism will be referred to as “CADL tagging”.

Second, Proposed Modification P78 (“Revised Definitions of System Buy Price and System Sell Price”) sought, in part, to introduce a further mechanism into the BSC to remove another category of acceptances taken for System Balancing reasons from the calculation of Energy Imbalance Prices. Under Proposed Modification P78 these acceptances were considered to be

⁴ As prescribed by The Electricity Supply Regulations 1988 (amended 1998) number 1057 and consistent with its statutory duties and licence conditions.

⁵ Section T3.1B of the BSC provides for the BSC Panel revise the value of CADL from time to time.

⁶ The Authority’s decision in respect of Approved Modification P18A can be found on the Elexon website: www.elexon.co.uk.

characterised by equal and opposite compensatory actions which, in general, are taken for System Balancing reasons, for instance, the alleviation of locational constraints. The principle of Proposed Modification P78 was to derive the Net Imbalance Volume (“NIV”) (defined as the volume of the overall System Energy Imbalance and determined as a net of all System Balancing and Electricity Balancing actions, including BSAD, taken by the SO in a particular Settlement Period) and calculate the main Energy Imbalance Price from only those BOAs taken to alleviate the Net Imbalance. On 9 September 2002, the Authority decided to direct that Modification Proposal P78 should be made and implemented⁷. Hereafter this mechanism will be referred to as “NIV tagging”.

During the assessment of Modification Proposal P144 the BSC Panel undertook a review of the value of CADL. At its meeting of 13 November 2003 the Panel recommended that CADL remain at 15 minutes and instructed ELEXON to carry out an industry consultation on the issue. The majority of respondents to the consultation and seven Panel Members agreed that 15 minutes remained the appropriate value of CADL. Following the consultation the Panel Chairman exercised his delegated authority under paragraph B4.4.6 of the BSC and agreed, on behalf of the Panel, that the value of CADL should remain at 15 minutes.

The Modification Proposal

In its Proposal, First Hydro Company, the Proposer of Modification Proposal P144, highlighted that Proposed Modification P18A was assessed over a short time period⁸ and noted that in the Authority’s decision document in respect of Modification Proposal P18A it was Ofgem’s view that there may be alternative methods of determining the duration of acceptances which could be developed over time and which may better facilitate achievement of the Applicable BSC Objectives than Proposed Modification P18A. It was the view of the Proposer of Modification Proposal P144 that NIV tagging represents such an alternative method and therefore it supersedes CADL tagging as it removes most of those acceptances removed by CADL tagging (i.e. short duration BOAs associated with System Balancing actions) since such acceptances are, in general, priced higher than longer duration BOAs and so are likely to be NIV tagged first. The Proposer therefore considered that CADL tagging was, in effect, “obsolete” and should be removed from the BSC.

Modification Proposal P144 was submitted on 10 October 2003 by First Hydro Company. NGC recommended that Modification Proposal P144 should be treated as an Urgent Modification Proposal for the purposes of Section F2.9 of the BSC and this recommendation was supported by the BSC Panel. On 14 October 2003 the Authority consented that Modification Proposal P144 should be treated as an Urgent Modification Proposal and agreed the proposed timetable and process for Modification Proposal P144.

It was the view of the Proposer that NIV tagging is intended to ensure that System Balancing and Electricity Balancing actions are properly identified and appropriately targeted onto Parties. The Proposer considered that including short duration trades in the calculation of Energy Imbalance

⁷ The Authority’s decision in respect of Approved Modification P78 can be found on the Elexon website: www.elexon.co.uk.

⁸ Modification Proposal P18A was submitted on 23 May 2001 and was subject to an Urgent timetable. The Modification Report in respect of Modification Proposal P18A was submitted to the Authority on 13 July 2001.

Prices would strengthen the signals to the market, in particular at times of system stress. It was the view of the Proposer that this would further incentivise market participants to balance their positions thereby reducing the actions that the SO must take to balance the System. The Proposer therefore considered that Proposed Modification P144 would better facilitate the achievement of Applicable BSC Objective C3 (b) for the efficient, economic and co-ordinated operation by NGC of the Transmission System. In addition the Proposer considered that Proposed Modification P144 would better facilitate the achievement of Applicable BSC Objective C3 (a) for the efficient discharge by the licensee of the obligations imposed upon it by the licence.

Further, it was the view of the Proposer that by improving the cost reflectivity of Energy Imbalance Prices and thereby removing the potential for cross subsidy associated with the defect in CADL tagging as perceived by the Proposer, the Proposed Modification would better facilitate achievement of Applicable BSC Objective C3 (c) for promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity.

Finally, it was the view of the Proposer that the CADL tagging methodology requires the Panel to define certain short duration trades as being for System Balancing reasons while others as being for Electricity Balancing reasons. The Proposer considered that this process is complex and cumbersome to manage and therefore, in the view of the Proposer, the removal of CADL tagging from the BSC would better facilitate achievement of Applicable BSC Objective C3 (d) for promoting efficiency in the implementation and administration of the balancing and settlement arrangements.

Pricing Issues Standing Modification Group considerations

The Pricing Issues Standing Modification Group ("PSMG") considered Proposed Modification P144 over the course of two meetings (17 October 2003 and 4 November 2003).

It was the view of the PSMG that the question of whether Proposed Modification P144 would better facilitate achievement of the Applicable BSC Objectives depended on the perception of whether the removal of CADL tagging from the BSC would result in a more cost reflective Energy Imbalance Price. It was the view of the PSMG that a more cost reflective Energy Imbalance Price can be considered to be one which is calculated, as far as is possible, from only Electricity Balancing actions, since it is these actions that are taken by the SO to alleviate Energy Imbalances caused by market participants. The PSMG considered that a more cost reflective Energy Imbalance Price would more appropriately target the costs of Electricity Balancing at those in imbalance, and thus reduce cross subsidies, and would create a more appropriate price signals to the Parties as to the costs of electricity balancing, thereby incentivising Parties to forward contract to reach an efficient level of balance.

A number of PSMG members considered that NIV tagging is a better mechanism for differentiating between System and Electricity Balancing actions than CADL tagging, since, in their view, CADL tagged short duration acceptances may be taken for Electricity Balancing reasons and that such acceptances should not be treated differently to any other acceptances for the purposes of NIV tagging, i.e. NIV tagging alone should make the differentiation between

System and Electricity Balancing actions. Thus, it was the view of these members that although CADL tagging was appropriate prior to Authority approval and implementation of Proposed Modification P78, CADL tagging has since been superseded by NIV tagging.

Further, a number of PSMG members noted that, under section T3.8A.1 of the BSC, longer duration trades (i.e. with a duration greater than the value of CADL) can be CADL tagged. For example, where an acceptance on a particular BM Unit in a particular Settlement Period has been CADL tagged (i.e. the duration of the individual acceptance [or series of related and continuous acceptances] is less than the value of CADL) then any other acceptance (or series of related and continuous acceptances) on that BMU in that same Settlement Period is also CADL tagged, regardless of its duration. These members therefore considered that CADL tagging thus has the potential to remove acceptances taken for Electricity Balancing reasons.

In addition, it was the view of a number of PSMG members that it was inappropriate to differentiate between acceptances taken for System Balancing reasons from those taken for Electricity Balancing reasons solely on the basis of the duration of each acceptance since it was feasible for short duration acceptances delivering large volumes of energy to have a more significant impact on Electricity Balancing than acceptances that last for an entire Settlement Periods but deliver only small volumes of energy. Under such circumstances, these members of the PSMG considered that it was inappropriate for the short duration acceptance to be CADL tagged.

In contrast, it was the view of a number of PSMG members that CADL tagging is still appropriate as it captures a different type of System Balancing action than NIV tagging. As stated previously, NIV tagging is intended to remove from the calculation of Energy Imbalance Prices those acceptances that are equal and opposite (i.e. compensatory) in nature. A number of PSMG members therefore considered that NIV tagging cannot capture System Balancing actions taken to address intra Settlement Period System related events, such as frequency control, since these short duration acceptances do not necessarily have an equal and opposite acceptance.

In addition, since energy trading and settlement is determined on an average basis over a whole Settlement Period, a number of PSMG members considered that it is important that Energy Imbalance Prices are set on a basis consistent with this and therefore the cost to the SO of taking balancing actions for very short durations in order to meet a dynamic profile of deliveries within a Settlement Period should not be borne by market participants. These PSMG members therefore considered that CADL tagging remains appropriate and complements NIV tagging in achieving the best differentiation between System Balancing and Electricity Balancing actions.

Further, a number of members of the PSMG considered that there is value in retaining the CADL mechanism within the BSC even if it was determined that CADL tagging was no longer necessary. Under such circumstances it was the view of these members that it would be better to lower the value of CADL from 15 minutes to zero rather than remove the mechanism entirely from the BSC since, in the opinion of these members, future changes to the calculation Energy Imbalance Prices could affect the need for, and significance of, CADL tagging in differentiating System Balancing and Electricity Balancing actions.

On balance, it was the view of the majority of PSMG members that Proposed Modification P144 would not result in a more cost reflective Energy Imbalance Price, and therefore would not better facilitate achievement of the Applicable BSC Objectives C3 (a), (b) and (c). However, a minority of PSMG members considered that a more cost reflective Energy Imbalance Price would arise from the removal of CADL, and as a consequence this would better facilitate achievement of Applicable BSC Objectives C3 (a), (b) and (c). In addition the majority of the PSMG considered that Proposed Modification P144 would not better facilitate achievement of Applicable BSC Objectives C3(d) since, even if it were appropriate for the value of CADL to be set to zero at the present time, it would be inefficient to remove CADL from the BSC in its entirety as it may be required in the future.

ELEXON published a consultation document in respect of Modification Proposal P144 on 23 October 2003, which invited respondents' views by 31 October 2003.

Respondents' views

Elxon received fourteen responses to the consultation on Proposed Modification P144. Two respondents (representing 10 Parties) supported the Proposed Modification; eleven respondents (representing 50 Parties and 1 non Party) did not support the Proposed Modification; and the remaining respondent (representing 1 Party) provided a "no comment" response. The original Proposer was amongst the respondents that considered that the Proposed Modification should be made.

In its response to the consultation, NGC expressed the view that it was appropriate to retain the CADL tagging mechanism in the BSC since, in its capacity as SO, it continues to accept short duration BOAs (less than 15 minutes) for System Balancing reasons, i.e. to manage within half-hour effects and control system frequency in real time. In its response NGC also expressed the view that the NIV tagging mechanism is based on the principle that System Balancing actions taken in the opposite direction to market length must be replaced by balancing actions in the same direction as market length and therefore that NIV tagging would not remove the System Balancing actions currently removed by CADL tagging. NGC expressed the view that the CADL tagging mechanism compliments the NIV tagging mechanism rather than NIV tagging rendering all other definitions of System Balancing actions redundant.

Several other respondents expressed the view that CADL and NIV tagging were complementary mechanisms designed to achieve different objectives. In addition, one respondent considered that retaining both tagging mechanisms in the BSC would make the tagging process more robust, reducing the likelihood of System Balancing actions polluting Energy Imbalance Prices. These respondents considered that CADL tagging was designed as the best practical method of removing short duration trades from cash-out. Some of these respondents also stated that NIV tagging did not directly address the differentiation of System Balancing actions from Energy Balancing actions for within-half-hour events where short duration acceptances are made that do not necessarily have an equal and opposite action. These respondents therefore considered it necessary to remove short duration actions from cash-out, citing the view that short duration actions were unlikely to be cost reflective or send consistent, economic Energy Imbalance Price signals to the forward markets. It was therefore the view of these respondents that CADL was not

made redundant by the implementation of NIV tagging, and its retention within the BSC was considered to be justified.

Several of these respondents also considered that the Proposed Modification was inconsistent with the interplay between CADL tagging and NIV tagging. One respondent suggested that the Modification Proposal stated that removing CADL tagging would improve cash-out price signals but also that NIV tagging would effectively remove the acceptances that CADL tagging currently removes. In the view of this respondent these views were inconsistent.

Two respondents considered that NIV tagging allowed for a consistent approach for differentiating between Energy Balancing and System Balancing actions. These respondents considered that CADL was an arbitrary mechanism that attempts to differentiate between System Balancing and Energy Balancing actions by assuming that all balancing actions with a duration less than CADL are taken for System Balancing reasons. CADL tagging was also considered by these respondents to tag out Energy Balancing actions, even though a substantial volume of energy may have been delivered. One of these respondents also stated that they did not consider that balancing actions of less than 15 minutes were a special case since short duration trades require the delivery of energy on to the System and as such there could be no justification for excluding such trades from the calculation of Energy Imbalance Prices.

Two respondents in favour of the Proposed Modification considered that the inclusion of short duration trades in the calculation of Energy Imbalance Prices would more appropriately target the cost of Electricity Balancing, thereby incentivising Parties to balance and strengthen the signals to the market particularly in times of stress. These respondents considered that this would improve the cost reflectivity of Energy Imbalance Prices and further encourage participants to avoid going short while reducing NGC balancing actions.

Several respondents stated that the BSC provides the BSC Panel flexibility to change the value of CADL (subject to Authority approval) in response to changes in the pattern of balancing actions. These respondents considered that it would be more cost effective to retain the CADL mechanism in the BSC but to set its value to zero. These respondents therefore considered that the Proposed Modification would not better facilitate achievement of Applicable BSC Objective C3 (d). One respondent highlighted the value in retaining the flexibility in setting the value of CADL in the light of the potential for changes to the calculation of Energy Imbalance Prices in the future, and also stated that the removal of CADL tagging would remove the flexibility to easily reintroduce CADL tagging should it turn out to be necessary in the future.

With regard to the Energy Imbalance Price analysis contained in the Modification Report, a number of respondents considered that the removal of CADL tagging would not improve incentives on market participants to contract ahead for this winter. These respondents stated that the signals provided by Energy Imbalance Prices would not be altered sufficiently by the removal of CADL, and where price would be altered respondents considered that removal of CADL tagging would dilute the current incentives to contract ahead of winter by lowering SBP and increasing SSP. The majority of these respondents did not consider that increasing the likelihood of allowing System Balancing actions to be fed into the calculation of Energy Imbalance Prices would provide a more appropriate price signal.

Several respondents also highlighted the fact that a full years worth of cash-out price data on the effect of CADL tagging under Proposed Modification P78 is not available as Proposed Modification P78 was implemented on 11 March 2003. These respondents therefore suggested that it would be premature to consider the removal of CADL tagging at this stage. These respondents considered that a more sensible approach would be to wait for the results of the periodic review of CADL as undertaken by the BSC Panel and, if appropriate, the value could be set to zero.

Panel's recommendation

The draft Urgent Modification Report in respect of Proposed Modification P144 was provided to the Panel for consideration at its meeting of 13 November 2003. The Panel considered the deliberations and recommendations of the PSMG and unanimously agreed with the recommendation of the PSMG that Proposed Modification P144 should not be made. In the event that the Authority determines that the Proposed Modification should be made, the Panel determined that the Implementation Date should be five Business Days after such an Authority determination.

Ofgem's view

Having carefully considered the Modification Report, the respondents' views and the Panel's recommendation, Ofgem, having regard to the Applicable BSC Objectives, agrees with the majority of respondents, the PSMG and the Panel that Proposed Modification P144 would not better facilitate achievement of the Applicable BSC Objectives. In addition, Ofgem considers that this decision is consistent with its wider statutory duties⁹.

Ofgem continues to be of the view that the costs of Electricity Balancing should be targeted onto those Parties that have caused Electricity Imbalances to occur (i.e. where Parties' notified generation/demand does not equal their actual generation/demand). In addition, Ofgem continues to consider that the costs of Electricity Balancing should reflect the prices at which the SO buys and sells energy to keep the System in Electricity Balance. Ofgem is of the view that the principles of cost-reflectivity and targeting which underpin the cash-out arrangements ensure that Parties face the appropriate level of exposure to Energy Imbalance regardless of the absolute level Energy Imbalance Prices. Ofgem consider, therefore, that there will be instances where Energy Imbalance Prices may rise to very high levels and that this is appropriate as prices should reflect underlying System conditions. In contrast, it is Ofgem's view that it is appropriate that System Balancing costs are targeted back to all users of NGC's System through Balancing Services Use of System charges since these costs cannot currently be attributed to particular users. Ofgem considers that these views are consistent with Applicable BSC Objective C3 (a) for the efficient discharge by the licensee of the obligations imposed upon it by the licence, Applicable BSC Objective (b) for the efficient, economic and co-ordinated operation by the licensee of the licensee's transmission system and Applicable BSC Objective C3 (c) for promoting effective competition in the generation and supply of electricity, and (so far as

⁹ Ofgem's statutory duties are wider than the matters the Panel must take into consideration and include amongst other things a duty to have regard to social and environmental guidance provided to Ofgem by the government.

consistent therewith) promoting such competition in the sale and purchase of electricity. In addition Ofgem considers that these views are also consistent with its wider statutory duties.

It is therefore Ofgem's view that the methodology for the calculation of Energy Imbalance Prices as set out in the BSC should be designed such that it best distinguishes, where practicable, between balancing actions taken for Electricity Balancing reasons and balancing actions taken for System Balancing reasons. Ofgem acknowledges that there are limitations to using 'static' mechanisms such as NIV and CADL tagging since such mechanisms can never perfectly distinguish between System and Electricity balancing actions in all circumstances. It is Ofgem's view, however, that in the absence of any more 'dynamic' mechanisms to distinguish balancing actions as either System or Electricity at the time of acceptance, static mechanism such as NIV and CADL tagging remain necessary.

CADL tagging was introduced into the BSC under Proposed Modification P18A. NGC, the Proposer of Proposed Modification P18A, considered that it was inappropriate for actions taken to address within-half-hour effects such as frequency control to be included in the calculation of Energy Imbalance Prices as these actions are taken for System Balancing reasons. In the Authority's decision letter in respect of Proposed Modification P18A, Ofgem agreed with NGC that the costs associated with these actions should not be included in the calculation of Energy Imbalance Prices.

In its response to the Assessment Consultation in respect of Proposed Modification P144, NGC expressed the view that short duration actions continue to be taken to manage within-half-hour effects and control system frequency in real time. Ofgem remains of the view that as actions taken to address within-half-hour effects such as frequency control continue to be taken by the SO for System Balancing reasons, these should continue to be excluded from the calculation of Energy Imbalance Prices.

The Proposer of Modification Proposal P144 considered that NIV tagging represents the most appropriate mechanism for distinguishing between balancing actions taken for Electricity Balancing reasons and balancing actions taken for System Balancing reasons, including those balancing actions taken to address within-half-hour effects such as frequency control. The Proposer considered that short duration acceptances currently removed by CADL tagging are, in general, priced higher than longer duration BOAs and so would be likely to be NIV tagged first were CADL tagging to be removed from BSC. The Proposer therefore considered that these acceptances would rarely be included in Energy Imbalance Prices.

Ofgem has not been persuaded by the arguments put forward by the Proposer of Proposed Modification P144 that NIV tagging alone is the most appropriate mechanism for distinguishing between System and Electricity balancing actions. It is Ofgem's view that NIV tagging is an appropriate mechanism for identifying equal and opposite compensatory actions which, in general, are taken for System Balancing reasons, for instance, the alleviation of locational constraints. Ofgem does not consider that balancing actions taken to address within-half-hour effects such as frequency control would necessarily exhibit equal and opposite characteristics and therefore it is Ofgem's view that NIV tagging is not the most appropriate mechanism for identifying these actions.

In contrast, it is Ofgem's view that CADL tagging is an appropriate mechanism for identifying balancing actions taken to address within-half-hour effects such as frequency control on the basis that such actions are likely to be of short duration (15 minutes or less as specified in the current version of the BSC). In addition, Ofgem considers that, in allowing the BSC Panel the discretion to review and revise the value of CADL, subject to approval by the Authority, the existing CADL tagging mechanism retains sufficient flexibility to allow its intended effect to be maintained in the future.

It is Ofgem's view, therefore, that it is appropriate to retain that CADL tagging mechanism in the BSC and that this mechanism complements the NIV tagging mechanism in achieving the best differentiation between System Balancing and Electricity Balancing actions. Ofgem therefore does not consider that removing CADL tagging from the BSC, as put forward by the Proposed Modification, would better facilitate achievement of Applicable BSC Objective C3 (a) for the efficient discharge by the licensee of the obligations imposed upon it by this licence, Applicable BSC Objective (b) for the efficient, economic and co-ordinated operation by the licensee of the licensee's transmission system or Applicable BSC Objective C3 (c) for promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity.

It is Ofgem's view that it is important to ensure that Energy Imbalance Prices provide appropriate cost-reflective signals to market participants. A number of PSMG members considered that CADL tagging was excluding Energy Balancing actions from the calculation of Energy Imbalance Prices as well as System Balancing actions. As highlighted previously, Ofgem acknowledges that it is difficult to establish a rule which clearly determines which acceptances are taken for System Balancing reasons and which are taken for Electricity Balancing reasons in all circumstances. However, Ofgem also considers that, where there are potential improvements to be made in respect of the Energy Imbalance Price calculations, it is important for the industry to address these issues in the appropriate forum and, if any serious defects are identified, for resolution of these defects to be progressed as quickly as possible.

Ofgem agrees with a number of PSMG members that, under section T3.8A.1 of the BSC, longer duration trades (i.e. with a duration greater than the value of CADL) can be CADL tagged. As stated previously, once an acceptance on a particular BM Unit in a particular Settlement Period has been CADL tagged (i.e. the duration of the individual acceptance [or series of related and continuous acceptances] is less than the value of CADL) then any other acceptance (or series of related and continuous acceptances) on that BMU in that same Settlement Period is also CADL tagged, regardless of its duration.

The Authority's decision

The Authority has therefore decided not to direct that the Proposed Modification P144, as set out in the Modification Report, should be made and implemented.

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

Please contact me on the above number if you have any queries in relation to the issues raised in this letter. Alternatively, contact Matthew Buffey on 020 7901 7088.

Yours sincerely

A handwritten signature in black ink, appearing to read "Sonia Brown". The signature is written in a cursive style with a large initial 'S'.

Sonia Brown

Director, Electricity Trading Arrangements

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