

## P314 'Reduction in PAR from 500MWh to 350MWh'

This Modification proposes a reduction in the Price Average Reference value from 500MWh to 350MWh. This will improve the strength of imbalance price signals during winter 2014/15.

This Assessment Procedure Consultation for P314 closes:

**5pm on Tuesday 30 September 2014**

The Workgroup may not be able to consider late responses.



The P314 Workgroup initially recommends **approval** of the P314 Alternative Modification and **rejection** of the P314 Proposed Modification

This Modification is expected to impact:

- ELEXON
- BSC Parties

**ELEXON**

What stage is this document in the process?

**01** Initial Written Assessment

**02** Definition Procedure

**03** Assessment Procedure

**04** Report Phase

P314  
Assessment Procedure  
Consultation

16 September 2014

Version 1.0

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## Any questions?

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## About This Document

The purpose of this P314 Assessment Procedure Consultation is to invite BSC Parties and other interested parties to provide their views on the impacts and merits of P314. The P314 Workgroup will then discuss the consultation responses, before making a recommendation to the BSC Panel at its meeting on 9 October 2014 on whether or not to approve P314.

Attachments from documentation relating to Modification [P304 'Reduction in PAR from 500MWh to 250MWh'](#) are included for reference; as set out in this consultation, P314 is closely related to P304.

There are six parts to this document:

- This is the main document. It provides details of the solution, impacts, costs, benefits, drawbacks and proposed implementation approach. It also summarises the Workgroup's key views on the areas set by the Panel in its Terms of Reference, and contains details of the Workgroup's membership and full Terms of Reference.
- Attachment A contains the draft redlined changes to the BSC for both the proposed and alternative Modifications under P314.
- Attachment B contains the P304 Workgroup's analysis on a PAR value of 100MWh.
- Attachment C contains the P304 Workgroup's analysis on a PAR value of 250MWh.
- Attachment D contains the P304 Workgroup's analysis on a PAR value of 350MWh.
- Attachment E contains the specific questions on which the Workgroup seeks your views. Please use this form to provide your response to these questions, and to record any further views or comments you wish the Workgroup to consider.

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### Why Change?

The existing imbalance arrangements have the effect of dampening imbalance price signals, meaning that they do not provide sufficient indication to the market of the value of flexible capacity when margins are tight. A potential cause of this price dampening is the level of the Price Average Reversion (PAR), which is currently set at 500MWh. Deriving a weighted average from a volume of 500MWh creates an imbalance price which does not reflect the marginal cost of balancing energy for a given Settlement Period.

P314 contends that a reduction to 350MWh is more appropriate than a reduction to 250MWh, as proposed by Modification P304 and that Parties should be given more time to prepare for a change to PAR.

### Proposed Solution

The P314 proposed solution seeks to introduce a reduction in the PAR volume from 500MWh to 350MWh and gives Parties approximately 2½ months' notice of this reduction, with an Implementation Date of:

- **2 January 2015** if an Authority decision is received on or before 17 October 2014; or
- **52 Working Days** following an Authority decision, if it is received after 17 October 2014.

### Alternative Solution

The Workgroup's alternative solution also proposes a reduction in PAR to 350MWh but with an alternative Implementation Date (matching that of P304) of:

- **31 October 2014** if an Authority decision is received on or before 17 October 2014; or
- **10 Working Days** following an Authority decision, if it is received after 17 October 2014.

### Impacts & Costs

We do not anticipate any direct impacts on BSC Parties due to the implementation of P314. BSC Parties may be indirectly impacted by the effects of the reduced PAR value on imbalance prices.

### Recommendation

The majority Workgroup view is that both the P314 proposed and alternative solutions better facilitate Objectives (b) and (c) compared to the baseline, and that the P314 alternative solution better facilitates the Objectives compared to the proposed solution, and therefore recommends that the P314 alternative solution is approved.

### What are imbalance prices?

Imbalance prices, which are known as 'cash-out' prices, are a key part of the wholesale electricity trading arrangements in Great Britain.

Under the current arrangements, market participants that require electricity for their customers (Suppliers) enter into contracts with organisations that produce electricity (generators). However, contracts between these participants are not always exactly delivered in real time causing an imbalance between energy generation and demand on the Transmission System. This can cause problems as electricity cannot easily be stored economically in large quantities and generation must always match consumer demand in real time if a stable system is to be maintained.

For any given Settlement Period (each half hour), Parties may trade with each other up to Gate Closure, which occurs one hour prior to the start of that Settlement Period. Parties aim to balance their position for a given Settlement Period by Gate Closure to ensure that the amount of energy generated and bought matches the amount of energy consumed and sold. However, there are circumstances where this does not happen. For example, if a generator experiences an unexpected outage that does not allow them to generate their projected amount of energy, or if a Supplier over or under estimates the amount of energy their customers actually use. This leaves the Party in an imbalanced position for that Settlement Period.

To balance energy on the Transmission System the Transmission Company, acting as System Operator (SO), assesses the amount of generation and the amount of demand expected for each Settlement Period. If required, the SO will take balancing actions<sup>1</sup> to balance the system so that the total amount generated matches the total amount consumed. The SO does this by issuing Bids and Offers via the Balancing Mechanism or Balancing Service Adjustment Actions (BSAA)<sup>2</sup> to participants (usually generators) to increase or decrease the amount of energy they need to produce (or consume) to ensure the system is balanced. The SO will do this prior to and throughout the Settlement Period to ensure the system is balanced at all times.

Following the end of a Settlement Period, ELEXON (using the BSC Systems) will compare the amount of energy each Party contracted with its metered volumes for the Settlement Period, accounting for any accepted Bids and Offers and other applicable balancing service volumes. Any surplus or shortfall that the Party has is called the imbalance volume and is paid for using the relevant imbalance price:

- If the Party is **short** (it consumed more energy than it had bought or sold more energy than it had generated) then it pays for its shortfall at the **System Buy Price** (SBP).
- If the Party is **long** (it generated more energy than it had sold or bought more energy than it had consumed) then it is paid for its surplus at the **System Sell Price** (SSP).

<sup>1</sup> A balancing action is an instruction to a Party, in accordance with agreed rules, to either increase or decrease generation, or increase or decrease demand. Parties must also submit details of their contracts to the BSC Systems.

<sup>2</sup> Balancing Service Adjustment Actions (BSAA) are the technical services that the System Operator purchases outside the Balancing Mechanism. This is described in [Balancing Services Adjustment Data \(BSAD\) Methodology Statement](#).

There are two methods for calculating the imbalance price:

- The **Main Price** is based on the costs of energy balancing actions incurred to the Transmission Company for that Settlement Period.
- The **Reverse Price** is based on the short term market price of wholesale electricity traded on the power exchanges for that Settlement Period.

The method (Main Price or Reverse Price) which is to be applied to an imbalance price (SBP or SSP) for each Settlement Period is determined by whether the system as a whole was long (Net Imbalance Volume (NIV) is zero or negative) or short (NIV is positive) for that Settlement Period:

- If the system is long, the SSP will be the Main Price and the SBP will be the Reverse Price.
- If the system is short, the SBP will be the Main Price and the SSP will be the Reverse Price.

As a result, the Main Price is applied to any Party whose imbalance was in the same direction to, and is considered to have contributed to the overall system imbalance. These Parties will therefore face the costs of the balancing actions accepted by the SO to resolve energy imbalance on the system. Conversely, the Reverse Price is applied to any Party whose imbalance was in the opposite direction to the net imbalance, and is considered to have helped to reduce the overall system imbalance. Therefore, these Parties might face the costs they would have incurred had they traded out their imbalance position on the power exchanges near Gate Closure.

Further information on imbalance prices can be found on the [imbalance pricing page](#) of our website.

## What is the Price Average Reference volume?

The PAR volume is used in the Main Price calculation. It is a volume of actions in the dominant direction from which a weighted average is calculated.

PAR captures the most expensive actions remaining after a series of “tagging” operations have been conducted by the SO. The tagging process eliminates the most expensive actions in the dominant direction that have a matching volume to any in the reverse direction. The PAR volume (MWh) for the most expensive energy balancing actions remaining is the volume used to set the Main Price.

Originally under the current arrangements, imbalance prices were calculated as an average of all actions taken by the SO to balance the system. This was subsequently changed to the most expensive 500MWh of actions under [P205 'Increase in PAR level from 100MWh to 500MWh'](#) in November 2006. This level of 500MWh has since been maintained.

Further information on PAR can be found on the [imbalance pricing page](#) of our website.

## What is the Electricity Balancing Significant Code Review?

In August 2012, Ofgem launched the [Electricity Balancing Significant Code Review](#) (EBSCR) to address long-standing concerns on electricity balancing arrangements raised in its 2010 [Project Discovery Report](#). In particular, Ofgem expressed concerns that imbalance

prices are not creating the correct signals to allow the market to balance, leading to increased risks to future security of supply.

Ofgem completed its review of the electricity balancing arrangements and published its [Final Policy Decision](#) on 15 May 2014. The final decision document lays out Ofgem's conclusions and builds on the extensive analysis and stakeholder engagement conducted during the EBSCR.

## P304 and P305

Ofgem published its [Final Policy Decision](#) on the EBSCR on 15 May 2014 and directed National Grid (as the Transmission Company) to raise the relevant Modifications to put the package of reforms in place.

National Grid raised [P304 'Reduction in PAR from 500MWh to 250MWh'](#) and [P305 'Electricity Balancing Significant Code Review Developments'](#) to progress a package of changes that came out of the EBSCR, as follows:

- Initial reduction in the PAR value to 250MWh (under P304)
- Further reduction in the PAR value following P304 (50MWh from winter 2015/16, then 1MWh from winter 2018/19) and changes to the Replacement PAR (RPAR) volume which is currently set at 100MWh;
- A single imbalance price, calculated using the main price calculation;
- The introduction of Reserve Scarcity Pricing (RSP); and
- The introduction of Value of Lost Load (VoLL) pricing for Demand Control actions.

## What is the issue?

The Proposer considers that the existing imbalance arrangements have the effect of dampening imbalance price signals, meaning that they do not provide sufficient indication to the market of the value of flexible capacity when margins are tight. As a result, imbalance price signals may have failed to create appropriate incentives for investment in flexible capacity (such as flexible generation, Demand Side Response (DSR) services and storage).

A potential cause of this price dampening is the level of PAR, which is currently set at 500MWh. Deriving a weighted average from a volume of 500MWh creates an imbalance price which does not reflect the marginal cost of balancing energy for a given Settlement Period. This is especially true at times of system stress when differences between the costs of accepted balancing actions are greatest.

P304 was also raised to address this issue, but the Proposer of P314 believes that a more modest reduction of PAR to 350MWh would be a more appropriate first step, and that Parties should be given more notice of the reduction in PAR to allow more time to prepare.

## Request for Urgency

### Interactions with P304

In order to assess whether a PAR value of 250MWh was the most appropriate value, the P304 Workgroup completed analysis on PAR values of 100MWh, 250MWh and 350MWh. This analysis indicated that, under the current arrangements, there would be some adverse impacts across different types of industry participant, in particular independent Suppliers (i.e. Suppliers who were not part of a vertically integrated Party). This analysis also showed that the higher the PAR value the smaller the impact on industry participants.

There is no alternative solution under P304. Though, at the final Workgroup meeting a member suggested a possible alternative solution for consideration by the Workgroup that was similar to the P314 proposed solution, as detailed below:

- A reduction in PAR to 375MWh (as the higher the PAR value the smaller the impact)
- PAR reverting back to 500MWh at the end of 2015
- Suggested implementation in January 2015 (to allow the industry more time to assess the effects of a lower PAR value)

The Workgroup did not take this potential solution forward as the majority of members did not support a PAR value of 375MWh and were uncomfortable with the idea of PAR reverting back to a value of 500MWh as it could create uncertainty under the current arrangements.

Full details of the P304 Workgroup discussions can be found in the Assessment Report published on the [P304 page](#) of the ELEXON website. The analysis completed under P304 can be found in Attachment B (100MWh), Attachment C (250MWh) and Attachment D (350MWh).

### Proposer's rationale for Urgency

The Proposer requested that P314 be treated as an Urgent Modification Proposal to allow the Authority to make a decision on both P314 and P304 at the same time.

The Proposer also requested urgency due to potential negative commercial impacts to the industry following the announcement that a large nuclear generation plant will be taken offline during winter 2014/15.

### Panel's views

The Panel considered the Proposer's request for Urgent status on 8 September 2014. Following its consideration, the Panel unanimously agreed that P314 should be treated as an Urgent Modification Proposal due to potential significant commercial impacts (as noted by the Proposer, above) and to allow the Authority to consider P314 alongside P304.

### Authority's decision

The Authority consented to P314 being treated as an Urgent Modification Proposal on 10 September 2014. The Authority's decision on Urgency for P314 can be found on the [P314 page](#) of the ELEXON website.



### Proposed Solution

First Utility raised [P314 'Reduction in PAR from 500MWh to 350MWh'](#) on 4 September 2014. This Modification proposes a reduction in the PAR volume to 350MWh. The Proposer contends that reducing PAR to a value of 350MWh will improve the strength of imbalance price signals during winter 2014/15. The Proposer also contends that Parties should be given appropriate notice of this reduction so they can better understand the effects of a lower PAR value and prepare for any impacts.

[P304](#) was raised by National Grid on 30 May 2014 and is currently in the Report Phase of its progression. P304 proposes a reduction in the PAR volume from 500MWh to 250MWh on 31 October 2014. The P304 Workgroup's analysis confirmed that a reduced PAR value under the current dual priced regime does have some adverse distributional effects on different types of industry participant. This is especially the case at times of system scarcity and potentially adversely affects competition in the market.

The P314 Proposer believes that a reduction in PAR to a value of 350MWh with an Implementation Date of 2 January 2015 will help prepare the market for a move towards a more marginal price and provide an increased signal of scarcity on the system (but limit the adverse impacts under the current dual priced market). The Proposer contends that the P314 proposed solution allows the objectives of the ESBCR to be achieved but at a reduced risk to market participants.

The P314 proposal originally included a 'sunset clause' so that PAR would revert back to 500MWh on 5 November 2015. However, the Proposer decided to remove this aspect from the proposed solution following the initial discussions of the P314 Workgroup.

In summary, the P314 proposed solution is to:

- Reduce the PAR volume from 500MWh to 350MWh; and
- Implement this change on 2 January 2014, giving Parties approximately 2½ months' notice of the reduction.

### Alternative solution

The majority of the Workgroup did not agree with an implementation date for P314 of 2 January 2015, but acknowledged that the implementation lead time that drives this date reflects that the Proposer believes Parties should be given time to prepare for the PAR reduction; which is integral to the P314 proposed solution.

The Workgroup therefore developed an alternative solution that would introduce the same reduction in PAR, from 500MWh to 350MWh, but with an implementation date of 31 October 2014. This is because a reduction in PAR could have more of an effect over winter 2014/15 and provide Ofgem with an option that more closely reflects P304 (which proposes the Implementation Date).

In summary, the P314 alternative solution is to:

- Reduce the PAR volume from 500MWh to 350MWh; and
- Implement this change on 31 October 2014, giving Parties 10 Working Days' notice.



Full details of the Workgroup's development of these solutions, and on the proposed Implementation Dates, can be found in Sections 5 and 6.

## Proposed draft legal text changes

This Modification proposes changes to BSC [Section T 'Settlement and Trading Charges'](#) to introduce a reduction in the PAR volume from 500MWh to 350MWh, as shown in Attachment A.

Please note that the draft legal text changes are the same for both the proposed and alternative solutions, as the only difference between the two is the recommended Implementation Date and implementation lead times from the point of approval.

### Estimated central implementation costs of P314

The estimated central implementation costs associated with P314 (for both the proposed and alternative solutions) are minimal. It will take approximately one ELEXON man day (equating to £240) to implement changes to the BSC and to change a central system parameter as part of business-as-usual operations to reduce the PAR value to 350MWh.

### Indicative industry costs of P314

We do not anticipate any direct implementation impacts on BSC Parties or Party Agents for either the P314 proposed or alternative solution. However, if industry participants have elected to store or use the value of PAR in their systems there may be a cost associated with changing the value.

### P304 impacts

#### Impact on BSC Parties and Party Agents

We do not anticipate direct implementation impacts on participants as the imbalance prices, in which PAR is used, are calculated centrally. Participants systems will only be impacted if they have elected to store or use the value of PAR within their systems (e.g. to calculate the system prices themselves) which they would do voluntarily. Participants may also be indirectly impacted by the effects of the reduced PAR value on imbalance prices.

#### Impact on Transmission Company

We do not anticipate there to be an impact on the Transmission Company.

#### Impact on BSC Agent/service provider contractual arrangements

BSC Agent/service provider contract	Potential Impact
SAA	The SAA will set the value of PAR within central systems to 350MWh effective from the P314 Implementation Date. This value will apply to all Settlement Days from this date onwards.

#### Impact on Code

Code Section	Potential Impact
Section T	Changes will be required to implement this Modification, as detailed in Attachment A.

### Recommended Implementation Date

#### Proposed solution

The Workgroup recommends an Implementation Date for the P314 proposed solution of:

- **2 January 2015** if an Authority decision is received on or before 17 October 2014; or
- **52 Working Days** following an Authority decision, if it is received after 17 October 2014.

The Proposer contends that a lower PAR value may require indirectly impacted BSC Parties to alter their strategies and commercial positions in order to prepare for the change. They also believe that the expected reduction in nuclear capacity over part of winter 2014/15 will add to the risk of scarcity events occurring. If a scarcity event does occur during this period it may result in higher imbalance prices which could be exacerbated by the implementation of a reduced PAR value, further impacting the industry. The Proposer therefore recommends that P314 is implemented on 2 January 2015 to help mitigate the risks to the industry of introducing the required reduction in PAR.

Whilst the majority of the Workgroup did not agree with this rationale they acknowledged that it is an integral aspect of the proposed solution.

#### Alternative solution

The Workgroup recommends an Implementation Date for the P314 alternative solution of:

- **31 October 2014** if an Authority decision is received on or before 17 October 2014; or
- **10 Working Days** following an Authority decision, if it is received after 17 October 2014.

The Workgroup considered the potential commercial impacts on industry participants if P314 were to be implemented ahead of winter 2014/15. Some members indicated a clear steer from Ofgem and the Transmission Company that there will be issues with scarcity on the Transmission System this coming winter. It was also noted that the Implementation Date for P314 should be aligned with P304 so that Ofgem have a clear decision between a PAR value of 250MWh (under P304) and 350MWh (under P314). Ofgem can then determine the best solution based on the value of PAR only, without a different Implementation Date (and the P314 proposed solution is available if Ofgem accept the rationale for a later Implementation Date).

A majority of the Workgroup believe that P314 should be implemented ahead of winter 2014/15 to enable the benefits of providing a better signal to the market when System margins are tight to be realised. It is therefore the majority view of the Workgroup that a solution be put forward with an alternative Implementation Date of 31 October 2014.

### Workgroup's initial discussions

#### Consideration of a 'sunset clause'

In addition to a reduction in PAR from 500MWh to 350MWh, the Proposer raised P314 with the inclusion of a 'sunset clause'. It was the Proposer's original intention for PAR to revert back to 500MWh on 5 November 2015.

A Workgroup member questioned how the inclusion of a 'sunset clause' (seeing the PAR value revert back to 500MWh) would better facilitate the Applicable BSC Objectives if the reduction in PAR proposed under P314 would also better facilitate the Objectives. The member questioned whether it would be more pragmatic to just raise a Modification should there be an issue with a reduction in PAR in the future.

It was noted that the idea of P314 was to change the incentives and behaviours of industry participants. A member contended that the inclusion of a 'sunset clause' may result in such behaviours not being realised given that the reduction in PAR would be temporary. They added that the forward modelling suggested that the margins for next winter will be even tighter than this winter.

The Proposer advised that a number of respondents to the P304 Assessment Consultation indicated that a reduction in PAR should only be progressed under a single priced regime. The Proposer believed that a reduction in PAR will result in more accurate signals of scarcity but could cause a long term issue for smaller Parties in a dual priced market. They considered that P305 (which seeks to introduce a single price, amongst other things) is targeted for implementation in November 2015, but if the introduction of a single price were to be delayed it could adversely impact smaller Parties. The Proposer believed that it would be more efficient to include a 'sunset clause' rather than raise a new Modification to put the PAR value back up to 500MWh should a single priced market not be introduced (under P305 or any other Modification).

It was noted by a member that there needs to be clear rationale as to why the PAR value reverting back to 500MWh would better facilitate the applicable BSC Objectives.

It was suggested by a member that the 'sunset clause' be removed as, if there is an issue with the approval or implementation of P305 (or the introduction of a single priced market), there will be plenty of time to consider raising a Modification to either put PAR back to 500MWh or introduce a single price. They could not see how a 'sunset clause' could be justified against the Objectives. The Proposer noted that there is no guarantee that such a Modification(s) would be approved.

The Proposer considered the Workgroup's views and decided not to take the inclusion of a 'sunset clause' forward under the P314 proposed solution.

#### What is the most appropriate implementation date?

The Proposer explained that implementing P314 in January 2015 will allow for the expected nuclear plant outage (announced in September 2014) to end (i.e. give time for the plant to come back online). They added that their intention is to miss out any scarcity event during the outage period (which is expected to end in December 2014) as it may result in exceptionally high imbalance prices which could be exacerbated by a lower PAR value. It will also allow the industry more time to react to a lower PAR value overall.

A member noted they believed the purpose of reducing PAR was to provide a better signal of scarcity in the market for winter 2014/15, so by implementing in January you may lose some of the benefit (i.e. by missing a period of scarcity when such signals would be beneficial). Another member added that the introduction of Demand Side Balancing Reserve (DSBR) and Supplementary Balancing Reserve (SBR) will further dampen price signals if either of the services are used, meaning the market will become even shorter. Some members therefore suggested that P314 be implemented on 31 October 2014, to ensure a reduction in PAR is implemented ahead of winter 2014/15. This date will also align P314 with P304, which will be considered by the Authority at the same time.

The Workgroup considered the date of the 'start of winter', as P304 proposes an implementation date of 31 October 2014 but winter under the BSC is defined as starting on 1 December. A member believed that a date of 1 December 2014 would be a better reflection of the start of the winter period and would allow the industry a bit of extra time to react to a lower PAR value, compared with a 31 October Implementation Date. The P304 Workgroup looked to get a reduction in PAR in prior to winter 2014/15 which is why they opted for implementation on 31 October 2014.

The Workgroup therefore considered three Implementation Dates for P314:

- 31 October 2014;
- 1 December 2014; or
- 2 January 2015.

The Proposer advised the Workgroup that they still believe an Implementation Date of 2 January 2015 is the most appropriate for the reasons previously given. A minority of the Workgroup supported this view.

A majority of Workgroup members did not agree with the Proposer's view and preferred an Implementation Date of 31 October 2014. It was therefore suggested that an alternative solution be put forward which would see reduction in PAR to 350MWh but with an Implementation Date of 31 October 2014.

One Workgroup member did not agree with the Proposer or the majority view and believed that a 1 December 2014 Implementation date would be more appropriate. The Workgroup agreed that this date should be consulted upon as it represented a compromise between the other options.

## Workgroup's alternative solution

It was the majority view of the Workgroup that an alternative solution should be put forward under P314. The Workgroup's alternative is identical to the proposed, in that it seeks to reduce the PAR value from 500MWh to 350MWh, with the only difference being an Implementation Date of 31 October 2014 (i.e. a shorter associated implementation lead time).

Some Workgroup members believed that, in order for the industry to realise the benefits of a reduced PAR value, and see a better reflection of scarcity in the market, a reduction in PAR needs to be made ahead of winter 2014/15.

Some members believed that, given part of the Authority's rationale for granting urgency was based on submitting both P314 and P304 to the Authority at the same time, it would be pragmatic to align the proposed Implementation Dates for both Modifications. This

means that the Authority will, in essence, have a choice between a reduction in PAR on 31 October to either 250MWh (under P304) or 350MWh (under P314 alternative).

## Other alternatives considered by the Workgroup

### Introduction of a single price with a reduction in PAR to 350MWh

A Workgroup member questioned why a single price was not considered under P304 as it seems the Assessment Consultation respondents were in favour of a reduction in PAR in a single priced market, and suggested that this might be considered under P314. The Workgroup noted that the introduction of a single price was considered. However, due to the time it would take to assess such an introduction (in the context of the timetable for the assessment of P314) and the scope of P304 it was not taken forward.

It was noted that Ofgem's EBSCR considered a reduction in PAR with in a single priced market. A member added that P304 was raised with the expectation that the system margins would tighten regardless of the recent developments. The Ofgem representative indicated that a PAR value of 250MWh was seen to be a suitable stepping stone towards a move to a more marginal price.

The P314 Proposer believed that it may not have been quite so evident during Ofgem's EBSCR that independent Suppliers would be adversely impacted in the current dual priced market. They also believed that there is potential for larger Parties to benefit from a lower PAR value.

It was noted that, due to the 'missing money' issue in the imbalance price, a lower PAR value will benefit generators in addressing the issue. Suppliers have all hedged already for this winter and will therefore be more adversely affected by a change. A Workgroup member added that this is a market for generation as well as supply. They accept the arguments about reducing PAR in a single priced market having less of an impact than under the current arrangements. However, they believe that a reduction in PAR for winter 2014/15 will benefit the market overall, even taking into account potential adverse impacts on small Suppliers.

A member recognised that there will be winners and losers amongst even amongst Suppliers; on average, vertically integrated Suppliers will benefit marginally whilst small Suppliers will have a small disadvantage, but questioned whether this was simply the nature of competition. Another member added that the analysis conducted as part of P304 indicated a range of impacts across different types of Supplier. However, it needs to be recognised that there were limitations to this analysis as the Workgroup and ELEXON were not able to take into account prospective behaviour changes (i.e. the analysis was based on applying a different PAR value to past data and didn't take into account behavioural changes). Another member believed that the overall impact of a reduced PAR value is unknown, especially at times of system scarcity. The member was therefore concerned that the impacts could be unmanageable. It was noted that extrapolating the 5 Settlement Periods of scarcity identified by ELEXON could have a considerable adverse distributional impact on industry participants.

The Proposer advised the Workgroup that they conducted analysis on the data published by ELEXON, under P304, in order to determine how a PAR value of 250MWh may affect the industry at a time of scarcity (as a result of higher demand). The Proposer filtered the data provided by ELEXON on the 20 December 2010. The Proposer noted that this was not a scarcity event as such but a very cold day during the winter period. The idea of filtering the data was so the impacts and benefits across the industry could be better understood.

Their results indicated that, during December 2010, a single company could benefit by approximately £2 million.

With respect to the suggestion that the Workgroup consider the introduction of a single priced market regime under P314, a member commented that such a change would be quite material to the industry. It may not be a difficult change to central systems or Party systems but the industry have already hedged for this winter based on a dual priced market. Therefore, there is not sufficient time for either ELEXON or the industry to properly assess the impacts of a reduced PAR value with the introduction of a single price market regime, given the P314 timetable.

It was considered that, if the Workgroup were to propose the introduction of a single priced market but there was not sufficient analysis on the impacts of a single price, Ofgem would most likely send P314 back to the Workgroup. A member added that a reduction in PAR under a single priced market appears very different to the Modification the Authority granted Urgent status for. The member did not think the Authority would have treated this Modification as urgent if it included a move to a single priced market. They suggested that, notwithstanding the introduction of a single price (which has its merits), the Workgroup needed to look at what it can do for this winter.

It was the unanimous view of the Workgroup that, taking the above discussions into consideration, it would not be appropriate to include the introduction of a single priced market regime under the P314 proposed or alternative solution.

## **Views on reduction of PAR to 350MWh compared with 250MWh**

Whilst recognising that P314 and P304 are separate Modifications and must be assessed on their own merits against the Applicable BSC Objectives, the Workgroup considered that it would be helpful to industry participants, the Panel and Ofgem for it to give its views on the different PAR values proposed by the two Modifications, i.e. 350MWh for P314 and 250MWh for P304.

The Workgroup noted that a PAR value of 250MWh (under P304) would give the market an increased signal of scarcity when system margins are tight. However, they also note the potential for adverse distributional impacts on smaller parties, due to reducing PAR too much under the current arrangements. A majority of the Workgroup therefore believed that a reduction in PAR to 350MWh would be more appropriate as it will provide the market with an increased signal of scarcity but limit the adverse impacts to the industry.



## Summary of initial views against the Applicable BSC Objectives

### Proposed and Alternative solutions compared with the baseline

The majority Workgroup view is that both the P314 proposed solution and the P314 alternative solution do better facilitate Objectives (b) and (c).

The following table summarises the Workgroup and the Proposer's views of both the P314 proposed and alternative solutions compared with the existing baseline against the Applicable BSC Objectives:

Does P314 better facilitate the Applicable BSC Objectives?		
Obj	Proposer's Views	Other Workgroup Members' Views <sup>3</sup>
(a)	<ul style="list-style-type: none"> <li>Neutral</li> </ul>	<ul style="list-style-type: none"> <li>Neutral</li> </ul>
(b)	<ul style="list-style-type: none"> <li><b>Yes</b> - making the main imbalance price signal more cost reflective strengthens the incentive on market participants to balance their positions ahead of Gate Closure, reducing the number of balancing actions required by the SO.</li> <li>A sharper imbalance price will signal the commencement of reforms designed to better reflect the value of flexible plant in the balancing arrangements. It may therefore contribute to deferring the mothballing of flexible plant and help counteract potential tightening of margins.</li> <li>Making the imbalance price sharper though a step change, starting with PAR350 this mid-winter, provides parties with the time required to get used to lower PAR values and to change behaviours accordingly.</li> </ul>	<ul style="list-style-type: none"> <li><b>Yes (majority)</b> – agree with Proposer</li> <li><b>Yes (minority)</b> – only a marginal benefit; a step in the right direction to help incentivise forward contracting resulting in a more efficiently run market.</li> <li><b>No (minority)</b> – a lower PAR value will more likely encourage Parties to take a long position, increasing the number of SO actions required.</li> <li><b>No (minority)</b> – it would have an adverse impact on liquidity as parties may hold their options until the last few seconds before Gate Closure.</li> </ul>
(c)	<ul style="list-style-type: none"> <li><b>Yes</b> - Strengthening the energy imbalance price signal should incentivise market participants to trade to balance their positions ahead of Gate Closure, increasing liquidity in the forward market and benefitting competition by encouraging investment in flexible capacity (flexible generation, demand participation and other technologies).</li> </ul>	<ul style="list-style-type: none"> <li><b>Yes (majority)</b> – agree with Proposer but believe benefit is marginal.</li> <li><b>Yes (minority)</b> – addresses the recognised defect in the market that there needs to be a better signal of scarcity on the system.</li> <li><b>No (minority)</b> – reduction in PAR under the current dual priced market would not better facilitate competition.</li> <li><b>No (minority)</b> – adverse distributional impacts and increased uncertainty will</li> </ul>



### What are the Applicable BSC Objectives?

(a) The efficient discharge by the Transmission Company of the obligations imposed upon it by the Transmission Licence

(b) The efficient, economic and co-ordinated operation of the National Electricity 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 of the balancing and settlement arrangements

(e) Compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency [for the Co-operation of Energy Regulators]

(f) Implementing and administering the arrangements for the operation of contracts for difference and arrangements that facilitate the operation of a capacity market pursuant to EMR legislation

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<sup>3</sup> Shows the different views expressed by the other Workgroup members – not all members necessarily agree with all of these views.

Does P314 better facilitate the Applicable BSC Objectives?		
Obj	Proposer's Views	Other Workgroup Members' Views <sup>3</sup>
		<p>mean Parties might change tactics and may hinder small suppliers competing for customers.</p> <ul style="list-style-type: none"> <li>• <b>No</b> (<i>minority</i>) – as the higher the imbalance prices the more credit cover Parties may need.</li> </ul>
(d)	<ul style="list-style-type: none"> <li>• Neutral</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Neutral</b> (<i>majority</i>)</li> <li>• <b>No</b> (<i>minority</i>) – inefficient to have what is considered a temporary reduction in PAR progressed knowing that another Modification (P305) has been raised to further reduce the value of PAR. Potentially inefficient and contradictory to propose a reduction in the PAR value for one winter whilst putting in place balancing actions (SBR and DSBR) that will further dilute the imbalance price.</li> </ul>
(e)	<ul style="list-style-type: none"> <li>• Neutral</li> </ul>	<ul style="list-style-type: none"> <li>• Neutral</li> </ul>
(f)	<ul style="list-style-type: none"> <li>• Neutral</li> </ul>	<ul style="list-style-type: none"> <li>• Neutral</li> </ul>

Because the Workgroup's alternative solution is identical to the proposed, in that it seeks to introduce a reduction in PAR to 350MWh, with the only difference between the two being the Implementation Dates, the Workgroup's views against the Objective for both the proposed solution and the alternative solution were the same.

### Proposed solution compared with the Alternative solution

The majority of the Workgroup believed that the P314 alternative solution would better facilitate the Applicable BSC Objectives compared with the proposed solution because implementation ahead of winter 2014/15 would enable the benefits of a reduced PAR value to be more fully realised.

A minority of the Workgroup believed that the P314 proposed solution would better facilitate the Applicable BSC Objectives compared with the alternative solution. This was because the later implementation date would enable Parties to better prepare for a PAR reduction, even though the later implementation would reduce the extent to which the benefits of a reduced PAR could be realised over for winter 2013/14 (i.e. they believed a later date represented a reasonable compromise between realising benefits and avoiding unjustified adverse impacts on Parties).

It is therefore the initial majority recommendation of the Workgroup that:

- the P314 alternative modification **should** be approved; and
- the P314 proposed solution **should not** be approved.

## Appendix 1: Workgroup Details

### Urgent Modification timetable

P314 Assessment Timetable	
Event	Date
Urgent Panel Meeting	8 Sep 14
Workgroup Meeting 1	15 Sep 14
Assessment Procedure Consultation	16 – 30 Sep 14
Workgroup Meeting 2	1 or 2 Oct 14
Panel considers Draft Modification Report	9 Oct 14
Issue Final Modification Report to Authority	10 Oct 14

### Workgroup membership and attendance

P314 Workgroup Attendance		
Name	Organisation	15 Sep 14
Members		
Dean Riddell	ELEXON ( <i>Chair</i> )	✓
Talia Addy	ELEXON ( <i>Lead Analyst</i> )	✓
Jeremy Guard	First Utility ( <i>Proposer</i> )	✓
Martin Mate	EDF Energy	✓
Esther Sutton	E.ON	✓
Sarah Owen	Centrica	✓
Tom Edwards	Cornwall Energy	✓
Cem Suleyman	Drax	✓
Libby Glazebrook	GDF Suez	☎
Andrew Colley	SSE	✓
Olaf Islei	APX Commodities	✓
Bill Reed	RWE	✓
Chris Elder	INTERGEN	☎
Keith Munday	Independent Consultant	☎
Sally Lewis	National Grid	✓
Lisa Waters	Waters & Wye	✓
Nick Haines	Good Energy	✓
Hannah McKinney	Dong Energy	✓
Ian Tanner	UK Power Reserve	✓
Graham Wilcox	EnDCo	☎

P314 Workgroup Attendance		
Name	Organisation	15 Sep 14
Attendees		
Oliver Xing	ELEXON ( <i>Design Authority</i> )	✓
Nick Brown	ELEXON ( <i>Lead Lawyer</i> )	✓
Dominic Scott	Ofgem	✓
David Beaumont	Ofgem	✓
Steve Bradford	Flow Energy	✓

## Appendix 2: Glossary & References

### Acronyms

Acronyms used in this document are listed in the table below.

Glossary of Defined Terms	
Acronym	Definition
BSAA	Balancing Services Adjustment Actions
BSAD	Balancing Services Adjustment Data
DSBR	Demand Side Balancing Reserve
DSR	Demand Side Response
EBSCR	Electricity Balancing Significant Code Review
NIV	Net Imbalance Volume
PAR	Price Average Reference
RSP	Reverse Scarcity Price
SBP	System Buy Price
SBR	Supplementary Balancing Reserve
SO	System Operator
SSP	System Sell Price
VoLL	Value of Lost Load

### External links

A summary of all hyperlinks used in this document are listed in the table below.

All external documents and URL links listed are correct as of the date of this document.

External Links		
Page(s)	Description	URL
2	P304 page of ELEXON Website	<a href="http://www.elexon.co.uk/mod-proposal/p304/">http://www.elexon.co.uk/mod-proposal/p304/</a>
4	P305 page of ELEXON website	<a href="http://www.elexon.co.uk/mod-proposal/p305/">http://www.elexon.co.uk/mod-proposal/p305/</a>
4	BSAD Methodology Statement	<a href="http://www2.nationalgrid.com/UK/Industry-information/Electricity-transmission-operational-data/Codes-principles-methodologies/Methodologies/">http://www2.nationalgrid.com/UK/Industry-information/Electricity-transmission-operational-data/Codes-principles-methodologies/Methodologies/</a>
5	Imbalance pricing information webpage	<a href="http://www.elexon.co.uk/reference/credit-pricing/imbalance-pricing/">http://www.elexon.co.uk/reference/credit-pricing/imbalance-pricing/</a>
5	P205 page of ELEXON website	<a href="http://www.elexon.co.uk/mod-proposal/p205-increase-in-par-level-from-100mwh-to-500mwh/">http://www.elexon.co.uk/mod-proposal/p205-increase-in-par-level-from-100mwh-to-500mwh/</a>

External Links		
Page(s)	Description	URL
5	EBSCR webpage	<a href="https://www.ofgem.gov.uk/electricity/wholesale-market/market-efficiency-review-and-reform/electricity-balancing-significant-code-review">https://www.ofgem.gov.uk/electricity/wholesale-market/market-efficiency-review-and-reform/electricity-balancing-significant-code-review</a>
6	Final EBSCR Policy Decision	<a href="https://www.ofgem.gov.uk/publications-and-updates/electricity-balancing-significant-code-review-final-policy-decision">https://www.ofgem.gov.uk/publications-and-updates/electricity-balancing-significant-code-review-final-policy-decision</a>
7	P314 page of ELEXON website	<a href="http://www.elexon.co.uk/mod-proposal/p314/">http://www.elexon.co.uk/mod-proposal/p314/</a>
9	BSC Section T	<a href="http://www.elexon.co.uk/wp-content/uploads/2014/03/Section_T_v23.0.pdf">http://www.elexon.co.uk/wp-content/uploads/2014/03/Section_T_v23.0.pdf</a>