

By email to EnergyMarket@cma.gsi.gov.uk

18 March 2015

Energy market investigation
Competition and Markets Authority
Victoria House
Southampton Row
London WC1B 4AD

ELEXON's comments on the CMA's updated Issues Statement

We welcome the opportunity to comment on the CMA's updated Issues Statement. As you are aware from our discussions with the CMA, ELEXON is responsible for managing the electricity balancing and settlement arrangements as set out in the Balancing and Settlement Code (BSC). We are independent of any part of the electricity industry and not for profit. We are pleased that we have been able to support the work of the CMA to date, through our submissions, hearing and data provision and are keen to assist further, if required.

We set out below a number of observations on specific aspects of your updated issues statement. These are ELEXON's observations and not those of the BSC Panel.

Observations on definition of Theory of harm 1

ELEXON provided a number of observations on the original drafting of theory of harm¹ 1 and we note that these have been assessed during the course of the CMA's work to date. The theory of harms includes reference to the outcome of Ofgem's Electricity Balancing Significant Code Review (EBSCR). We refer the CMA to the latest developments in the progress of two proposed Modifications to the BSC arising from the EBSCR work:

- P305 Proposed – reduces the Price Average Reference (PAR) value from 500MWh to 1MWh, introduces a single imbalance price, a price factor for reserve scarcity pricing and loss of load probability;
- P305 Alternative – reduces the PAR value to 100MWh;

¹ [ELEXON submission on CMA's Statement of Issues August 2014](#)

- P316 Proposed – reduces PAR to 50MWh and then 1MWh in 2018, reduces the Replacement PAR value to 1MWh and introduces a single imbalance price;
- P316 Alternative - reduces PAR to 100MWh, reduces the Replacement PAR value to 1MWh and introduces a single imbalance price;

ELEXON has now sent the final reports to the Authority for their consideration. The recommendations to the Authority from the BSC Panel are that the P316 Alternative solution is approved and the other proposed changes are rejected as, in the view of the BSC Panel, they do not satisfy the Applicable BSC Objectives (which are set out in the Transmission Licence).

The Authority will now determine which of the P305 and P316 Proposed or Alternative modifications (if any) should be made. The Authority can disagree with the Panel and make a decision to approve any of the Proposed or Alternative Modifications. There is no fixed time within which the Authority must make a decision.

We reiterate the reference in our original response that the CMA should consider the EU Electricity Balancing Network Code, currently in draft form, which is likely to harmonise the calculation of imbalance prices across Europe and so prohibit other formulations of how imbalance prices could be calculated.

Observations on theory of harm 5

ELEXON is encouraged that the CMA believes our observations regarding the complexity of the code arrangements for new entrants (and existing participants) warrant further consideration. We strongly support the decision to investigate the potential issues relating to market entry, collateral arrangements and use of data that the CMA has highlighted from our original response. We propose that the CMA should consider the following in its assessment of theory of harm 5:

- *Codes vary in their nature.* Some for example are essentially technical in nature (e.g. Grid Code) whilst others are commercial (e.g. the BSC and CUSC);
- *Code administration covers a range of diverse services.* Not all code administrators deliver the same set of services (e.g. the code administration activity for some codes is mainly secretariat functions, but the BSC administration involves additional activities such as credit monitoring, delivering cost/benefit and impact analysis, education, procurement, agent management, market assurance and other operational and support services);
- *The speed of change arising from an SCR.* The CMA notes that the SCR process has not speeded up change. We observe that whilst the SCR process is beneficial in tackling cross code change the SCRs undertaken to date have themselves taken a long time. The process is extended in that, once Ofgem publishes its conclusions, any proposed changes then go

through the code modification process. We question whether there is a need to undergo the full code modification processes given the already lengthy process of assessment and extensive consultation that accompanies a SCR.

- *Ofgem should more actively participate in industry code change assessment processes.* Given that the Authority makes the final determination on industry code changes it has an obvious interest in ensuring the assessment of changes considers any matters it believes are relevant. Ofgem should therefore contribute to setting the terms of reference for changes. In addition Ofgem should engage with the cost/benefit analysis process undertaken by industry code change groups, as otherwise Ofgem will often repeat such analysis (the CMA report notes this in two of the examples it cites in its codes paper), which seems an inefficient use of effort, time and cost, which is ultimately borne by consumers.
- *What can be done now to improve code co-ordination and simplify/improve the arrangements?* ELEXON recognises that any code consolidation activity will be a significant undertaking. However, it should improve the accessibility of codes to participants. ELEXON believes the following approaches will be a practical way to achieve greater efficiency in code delivery and management:
 - Establish a cross code expert group to consider changes. There are many market wide changes (European Network Codes, demand side participation, shift in the mix of generation, greater interconnection, the spread of microgeneration) that require a cross code strategic approach as to how and when to introduce changes, and co-ordinate these;
 - Consolidate code administration by appointing fewer code administrators and encouraging efficiency across code administration: This will allow for users to have a reduced number of interfaces for managing code activities, code change and allow for a consistent approach to code administration;
 - Consolidate code governance arrangements. This could be achieved by:
 - Recasting and, where possible, simplifying industry codes into a small number of code (for example this could be aligned with how the European Network Codes divide up the various parts of the industry);
 - Use the opportunity for planned cross code changes to consolidate elements of the current codes. For example Ofgem's project on next day switching will seek to centralise registration, which presents such an opportunity, albeit that Ofgem indicated in its report that it would not use the project to deliver any

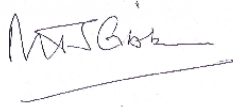
further code consolidation. It is likely that any shift in market arrangements (e.g. the introduction of greater demand side activity) would require significant code changes and would also be a useful trigger for improvements or consolidation of codes.

- Continue to develop the Code Administration Code of Practice (CACoP). ELEXON was instrumental in the production of the original CACoP and our Modification report template was adopted as the standard template for the industry change report. ELEXON has continued to lead on cross code reviews of the CACoP (better transparency, upfront identification of cross code issues, and better assessment with joint work groups).

We have a number of points of clarification arising from the Statement of Issues and its supporting material which is included in Appendix A to this letter. We will submit a separate response on the working paper 'gas and electricity settlement and metering'.

We would be happy to discuss our response and will continue to support the CMA in its work. If you would like to discuss any areas of our response, please contact me or David Jones, Director of Operations, on 020 7380 4213, or by email at david.jones@elexon.co.uk.

Yours sincerely,



Michael Gibbons
Chairman, ELEXON

Appendix A – clarifications from the Statement of Issues and supporting documents

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Codes working paper

Section 10(c)

The CACoP originated from the first phase of Ofgem's code governance work (not the subsequent phase) but it only applied to the BSC, CUSC and UNC and was later extended to other industry codes.

Section 11(a)

The CMA suggests the BSC's primary purpose is to maintain security of supply. In ELEXON's opinion, while the Balancing Mechanism (BM) and the BSC rules are important to the system operator in managing the security of supply, there are several other mechanisms at its disposal that are governed by other codes and agreements. The BM allows for residual balancing activity. Therefore the primary purpose of the BSC may be better described as being to ensure there is a fair and accurate allocation of units of electricity and therefore payments between Parties arising from this.

Section 13

The E-serve services are not usually regarded as codes as they are not codified in the same way as the other 'codes' referred to in paragraph 13. However it is sensible to consider the data flows and requirements and delivery mechanisms for those E-serve activities that are 'administrative' in nature as being candidates for simplification or consolidation with other codes.

Section 24

We have highlighted in our response various ways that consolidation and simplification could occur in the most cost efficient manner.

Section 55

Reference is made to 'those with code making power' and the need for their interests to be aligned with that of the wider industry and consumers.

We suggest that Ofgem does fulfil a role here, in so far that it has the power to amend licence obligations which cascade down into codes but it also plays a critical role in making the final determination on changes to industry codes and does so in accordance with its wider statutory duties and objectives.

ELEXON believes that the interests of consumers could be better met by:

- ensuring all code panels have consumer representation; and
- placing an objective on all code panels to consider the impacts on consumers arising from changes to codes.

ELEXON and other code administrators have an obligation to ensure they act as critical friend to industry and consider the views and impacts of users and others who may be impacted by, but unable to engage fully, with change.

Wholesale electricity market rules paper

Section 5

ELEXON receives contractual information from participants and calculates Imbalance prices (not National Grid as the System Operator (SO) as stated in the report).

Section 22



Generators are not mandated to bid into the Balancing Mechanism, however once they do bid there is an expectation that they deliver on their bids.