

BSC Modification Proposal P194

Revised Derivation of the Main Energy Imbalance Price

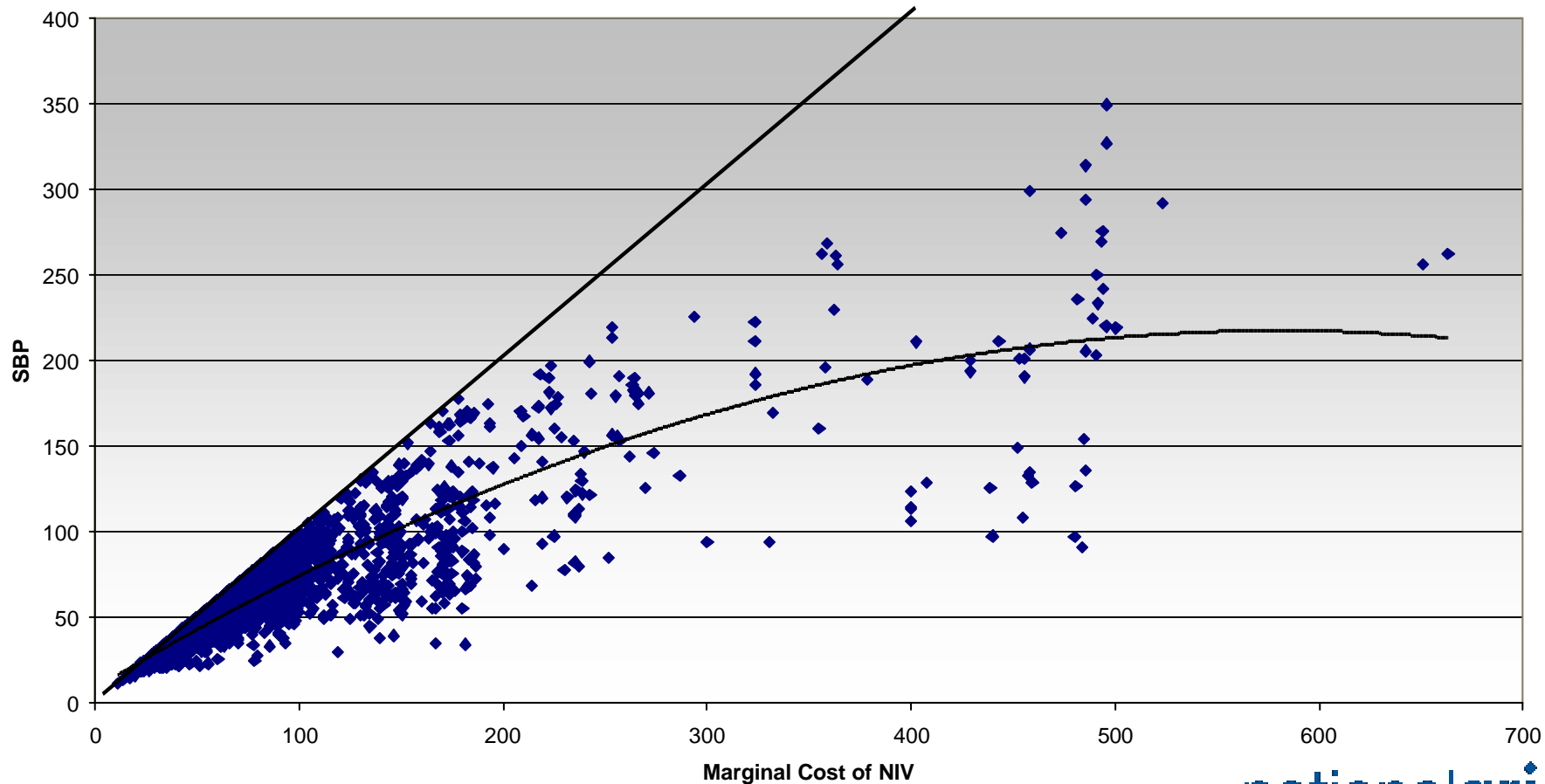
Rob Smith

Imbalance Price Behaviour

- Volume Weighted Average of Entire NIV - not always a good proxy for marginal cost of energy
- At times of energy shortage the difference between average price and marginal cost can be considerable
- Resultant imbalance price can be inhibited from appropriately signalling energy scarcity
- Can lead to inappropriate signals in the forward markets where commercial decisions are heavily influenced by the economics of imbalance exposure

Dampening Effect of Average Weighted Prices

Divergence between Marginal Cost of Energy Balancing and Average Pricing (SBP) - When NIV is Short

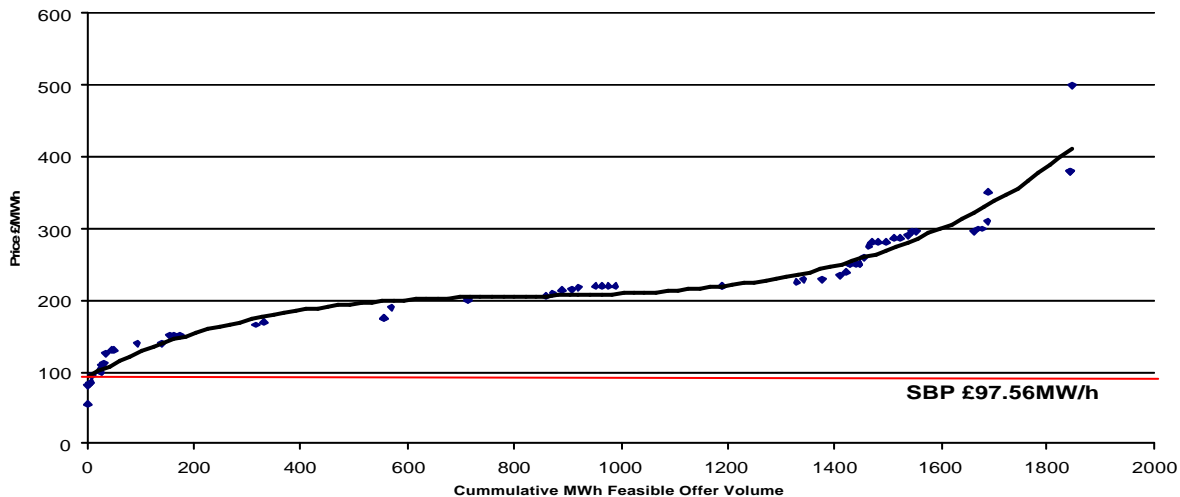


Offer Price Submissions Behaviour

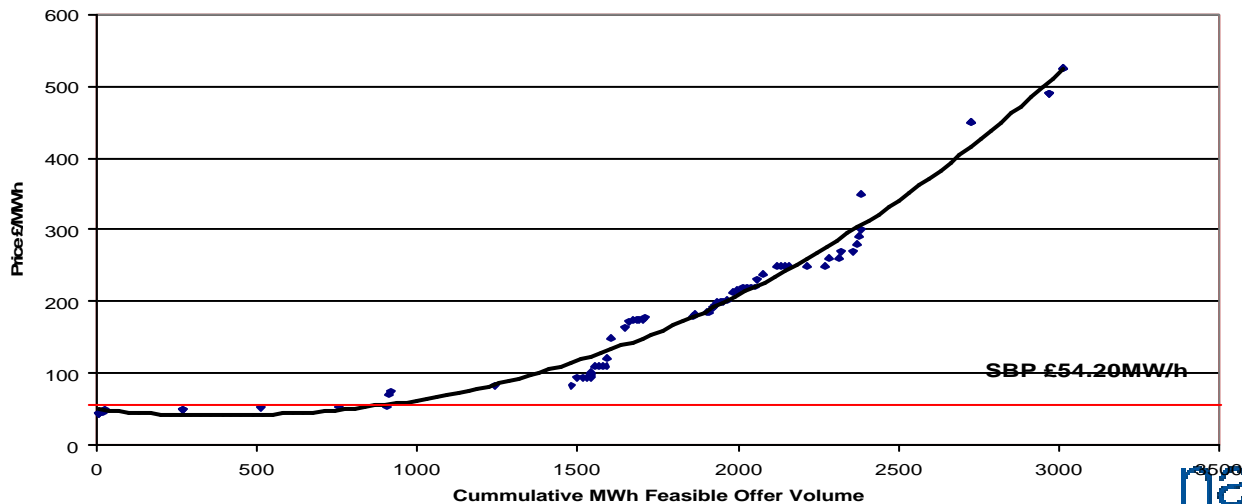
- Observed submitted BM prices tend to be static in nature and do not cluster around the Marginal Cost of resolving NIV.
- Therefore average of accepted offers does not always tend towards the Marginal Cost of resolving NIV

Offer Price Submissions Behaviour

Feasible Offers : 2nd March 2005 Period 35

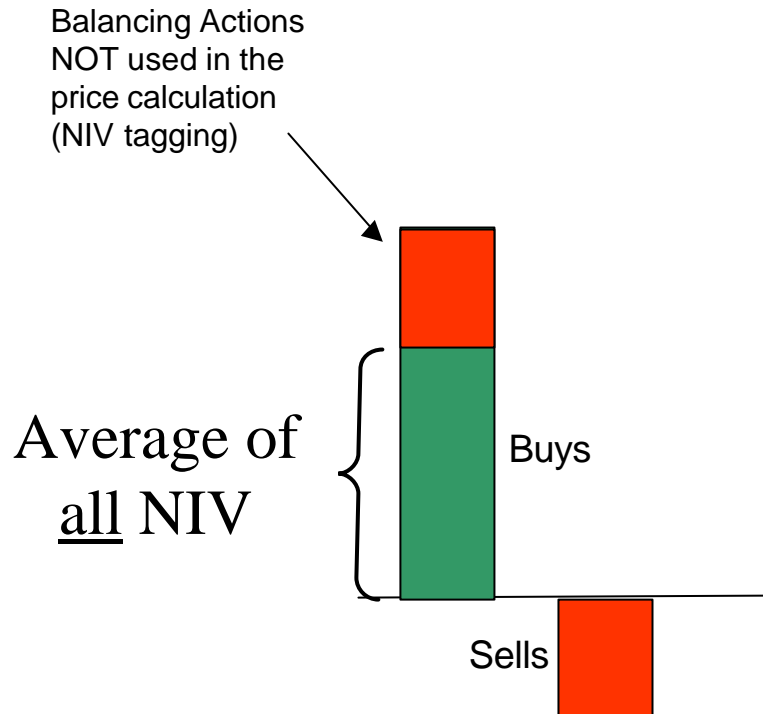


Feasible Offers : 16 June 2005 Period 35

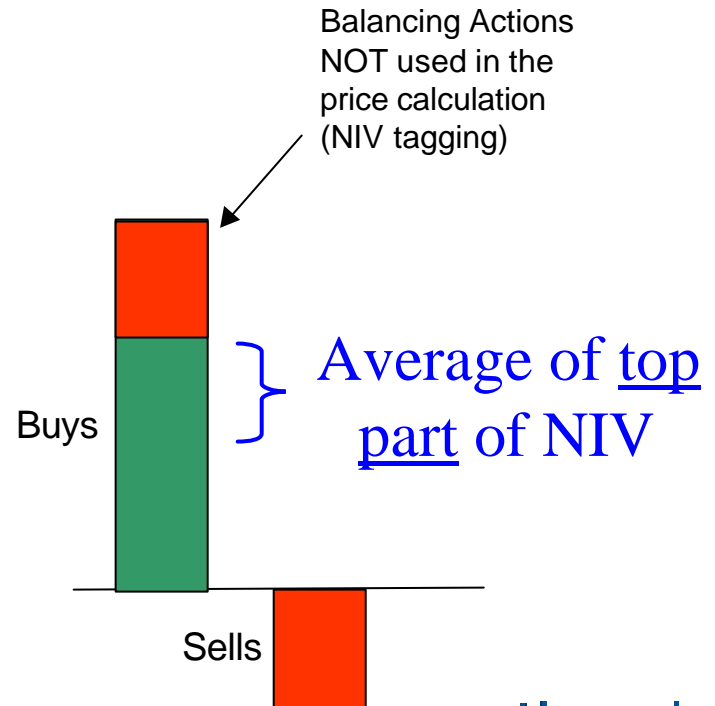


Proposal

Current (P78) Arrangements

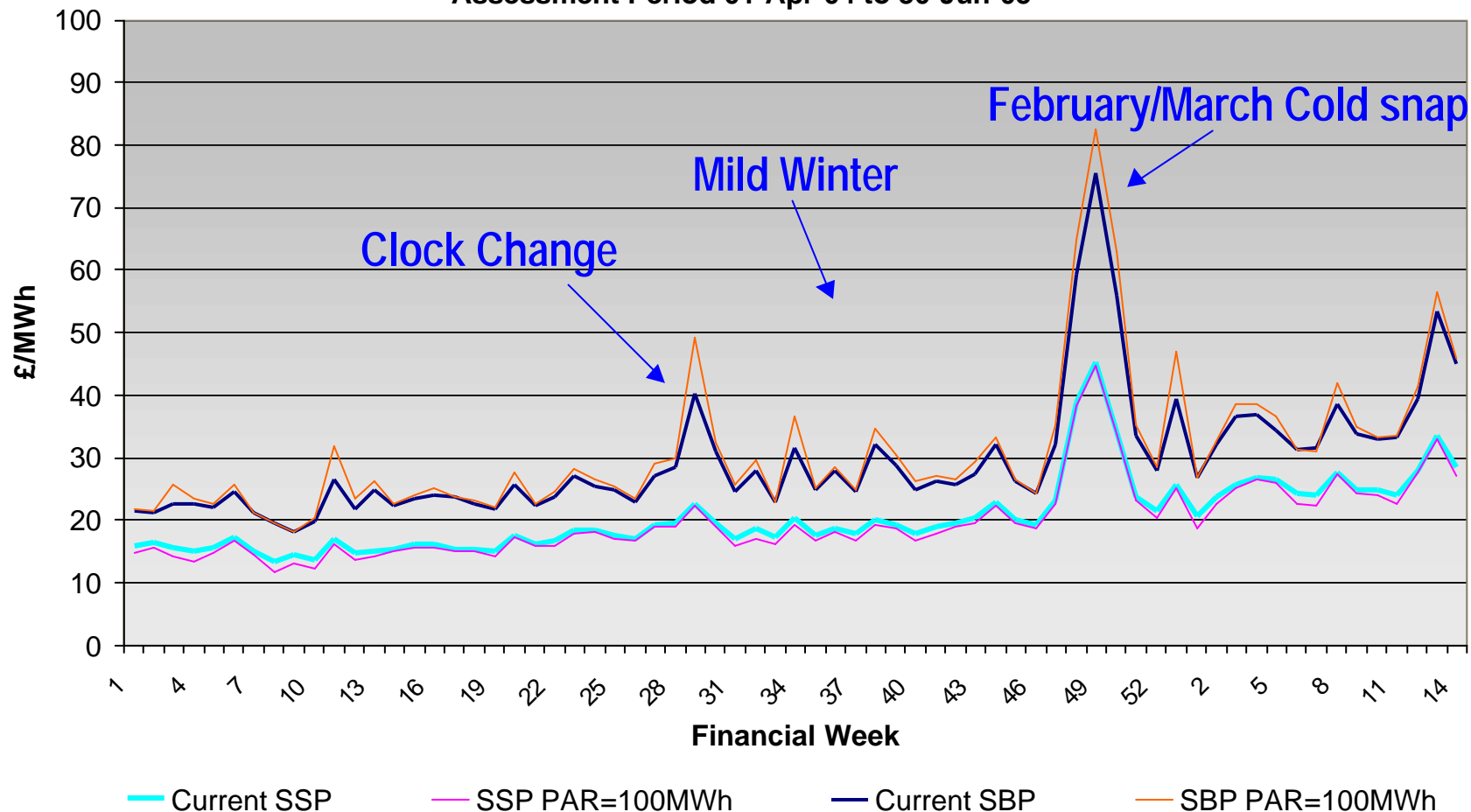


Our Proposal



Impact on Prices

Comparing Imbalance Pricing Methodologies - Weekly Averages
Assessment Period 01-Apr-04 to 30-Jun-05



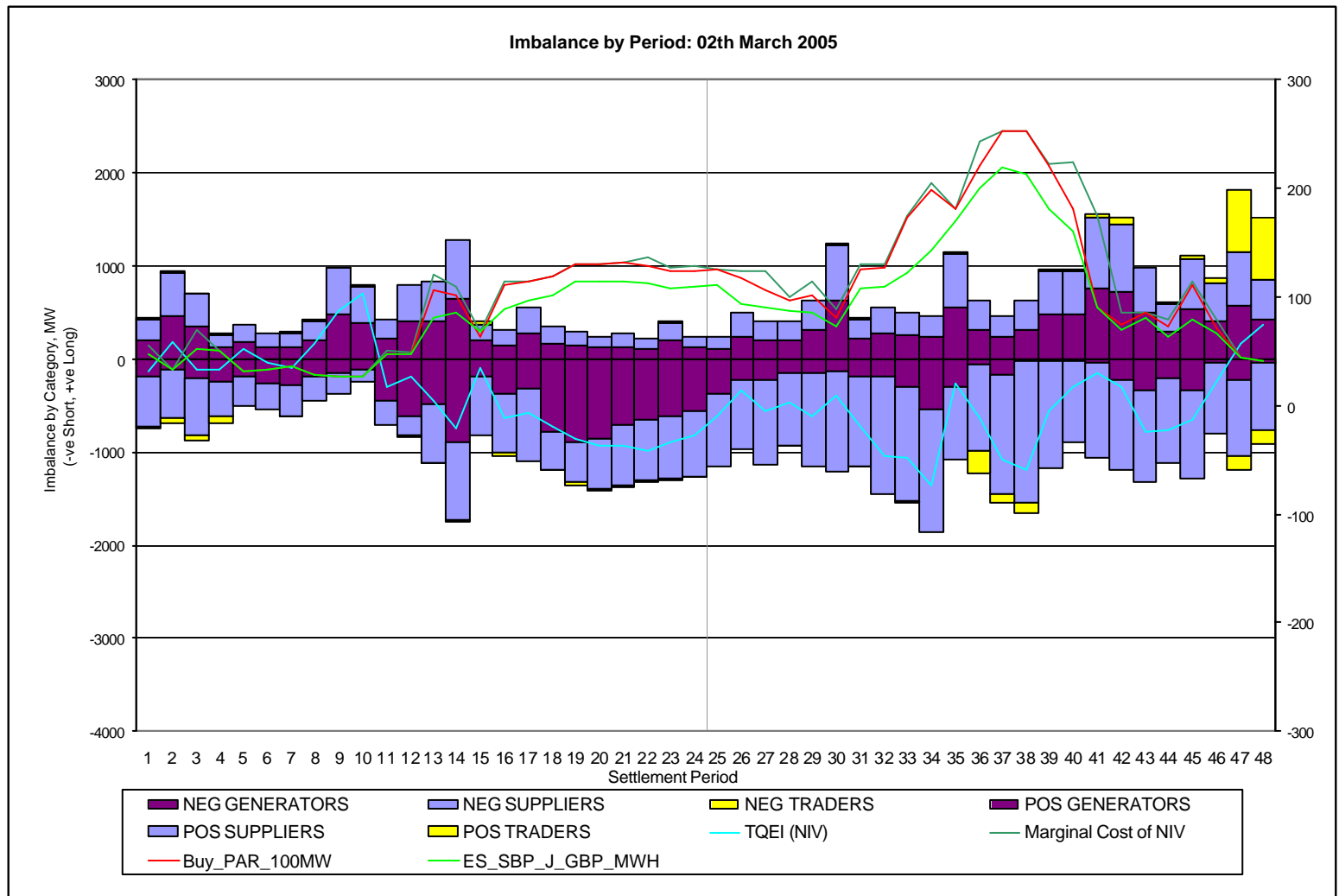
Why Take This Approach

- better approximate the Marginal Cost of Resolving NIV, particularly at times of energy shortage
- Minimise the impact of prices at other times
- Address the concerns of P136
- Appropriately incentivise parties to trade ahead of Gate Closure which will increase competition
- Benefit Security of Supply
- Recognise that other sizes/methodologies may be appropriate

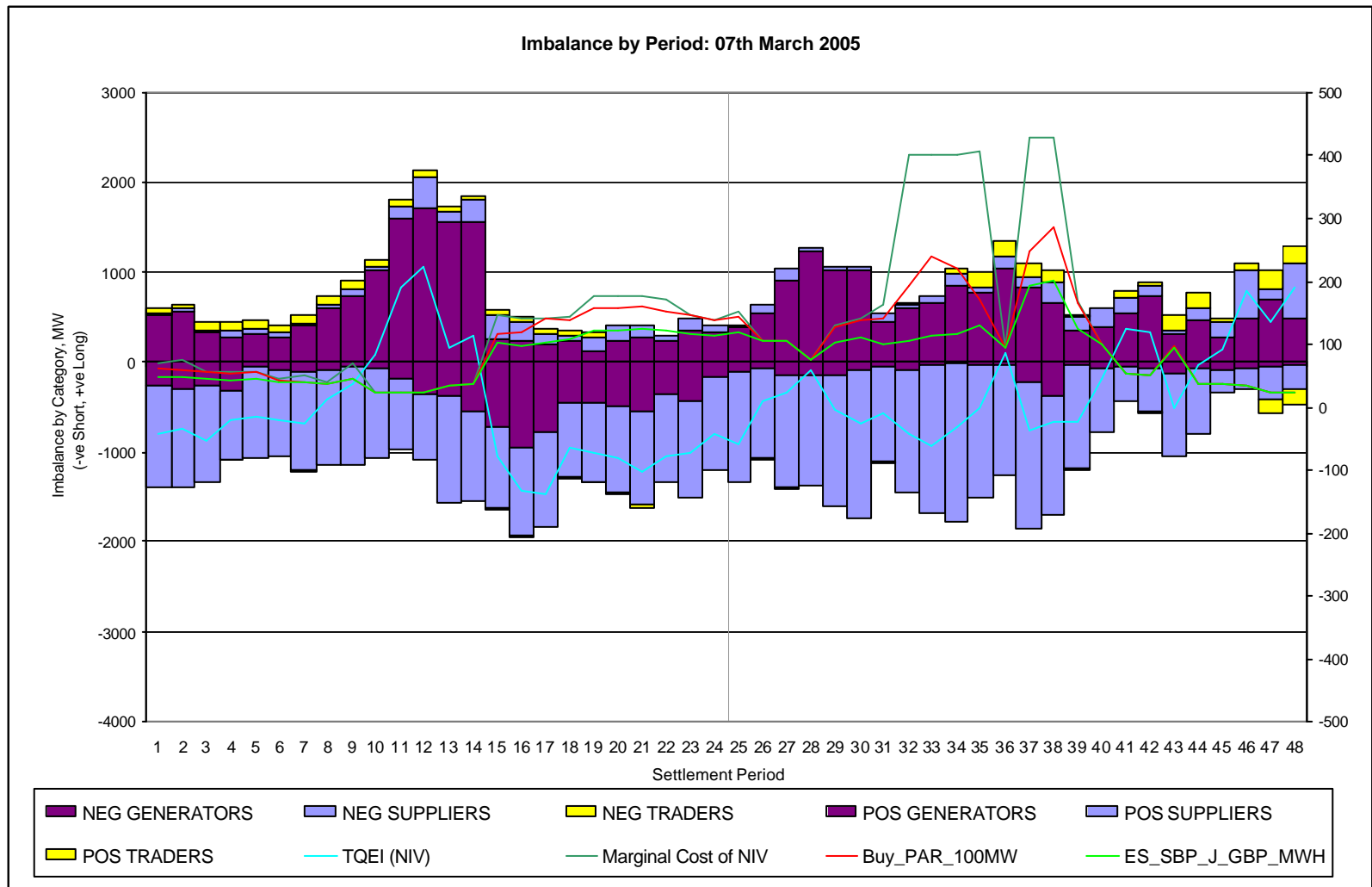
Example of Identified Periods of Concern

- The inability of Imbalance prices to send appropriate signals to the forwards markets was noticeable in the cold snap of late February and early March of 2005
- Sustained period of contracted energy shortfall across period between 25th Feb - 10 Mar
- Average prices did not approximate the marginal cost of resolving NIV for a large number of settlement periods in that time frame
- No Major Active Constraints in that Period

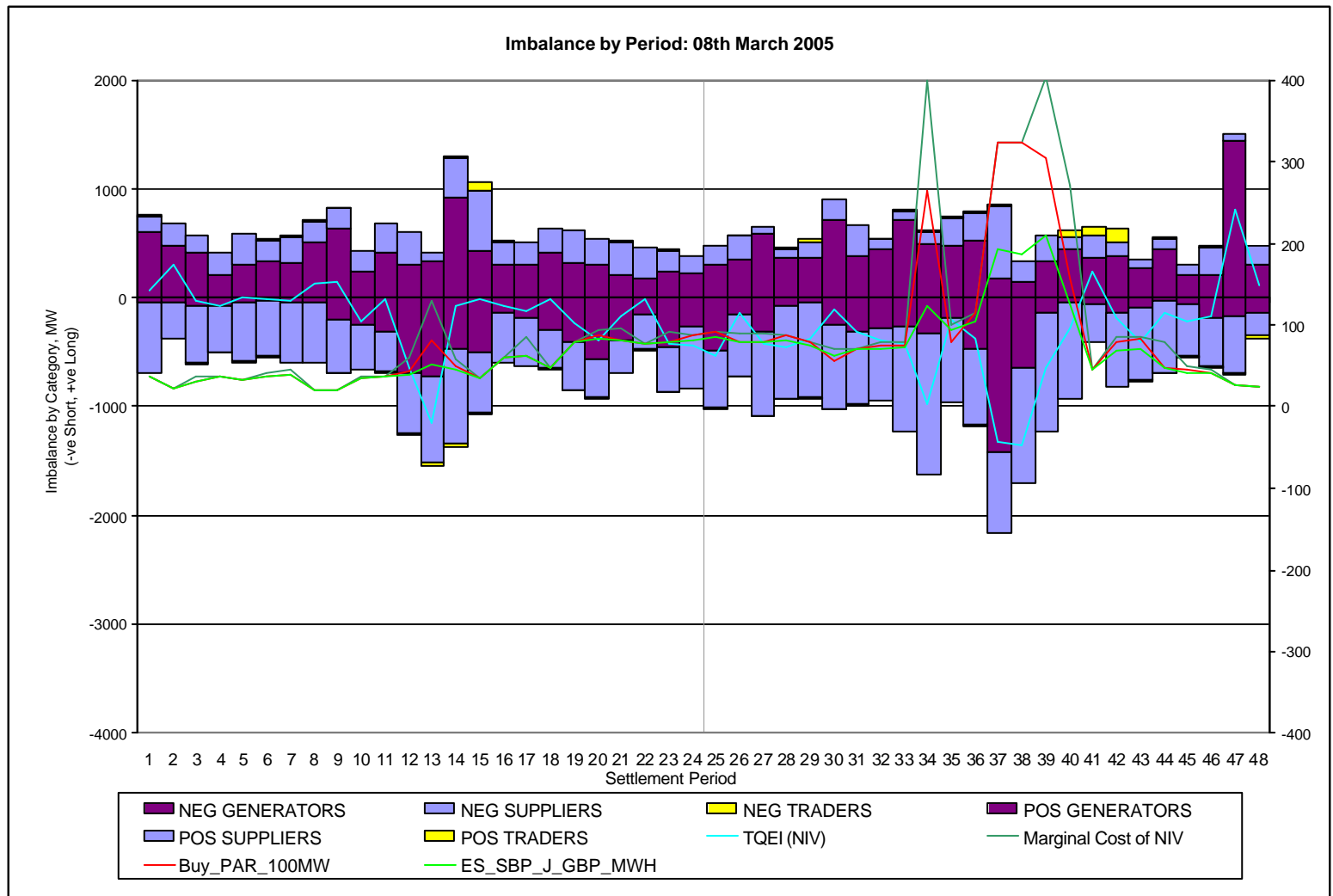
Within day - Cold Snap 2nd March 2005



Within day - Cold Snap 7th March 2005



Within day - Cold Snap 8th March 2005



Summary - Our Proposal

- ◆ Retains all tagging rules
- ◆ Averages over top chunk of NIV rather than all of NIV
- ◆ Does not change BSAD
- ◆ Does not change treatment of option fees
- ◆ Provides better signals in times of system stress without adversely affecting other periods
- ◆ Addresses concerns raised under P136