

P217 Report Phase Consultation Responses

Consultation Issued on 19 June 2008

Representations were received from the following parties

No	Company	File number	No BSC Parties Represented	No Non-Parties Represented
1.	RWE Trading	P217_dMR_01	10	0
2.	Scottish Power	P217_dMR_02	7	0
3.	National Grid	P217_dMR_03	1	0
4.	EDF Energy	P217_dMR_04	9	0
5.	Uskmouth Power	P217_dMR_05	1	0
6.	Scottish and Southern Energy plc.	P217_dMR_06	10	0
7.	Alcan Smelting and Power UK	P217_dMR_07	1	0

Question 1: Do you agree with the Panel's provisional recommendation to the Authority contained in the draft Modification Report that Proposed Modification P217 should not be made?

Summary

Yes	No	Neutral/Other
5	2	-

Responses

Respondent	Response	Rationale
RWE Trading	No	<p>We support implementation of the original proposal for the reasons outlined below.</p> <p>The proposed modification will better facilitate Objective B, related to the economic and efficient operation of the transmission system, by ensuring that cash out prices better reflect the marginal cost of balancing the system for energy purposes by removing system actions from cash out there will be appropriate market signals. This will ensure economic and efficient resolution of energy imbalances.</p> <p>The proposed modification will better facilitate Objective C, related to</p>

Respondent	Response	Rationale
		<p>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 by ensuring that system actions do not distort the calculation of energy imbalance prices. In addition, the proposal should result in more efficient despatch of generation and demand side management by resulting in energy imbalance prices that provide the correct signals into the market.</p> <p>The removal of the current confusing and inconsistent arrangements for separating system and energy actions and its replacement with a transparent and objective means of distinguishing the nature of SO actions means that the modification proposal will better facilitate Objective D relating to promoting efficiency in the implementation and administration of the balancing and settlement arrangements.</p> <p>These comments are based on the original submission in the modification proposal</p>
ScottishPower	Yes	<p>ScottishPower agree with principles of P217 in particular that the transmission constraint tagging methodology would reduce the effect of system constraints on the main Energy Imbalance Price, which has been the main issue/argument raised by the industry.</p> <p>However, ScottishPower remain concerned that the re-introduction of PAR 100MWh at this time could introduce unacceptable exposures from unmanageable risks and therefore detrimental to Objective (c) – promoting competition.</p> <p>We therefore believe the Alternative would be better and prudent, giving time for any imperfections of the new methodology to be refined, particularly as previous analysis showed that PAR 500MWh retains the benefit of a stronger signal to Parties to balance their position without the inherent unmanageable risks of PAR 100MWh.</p> <p>Irrespective of what effect P217 has on the Energy Imbalance Price from transmission constraints removal, we continue to believe that the more penal effect (with 100MWh PAR) will discourage generation capacity to be made available for the market, particularly at times of system stress. This would <u>not</u> better facilitate Objective (b) – efficient operation of the transmission system.</p> <p>Nonetheless, the Transmission Company has forecast significant cost for managing constraints and one of the key benefits of P217 was reducing the impact of constraint costs on the main Energy Imbalance Price. The fine balance between the exposures of potential extreme imbalance price resulting from PAR100 and the excessive price caused by transmission constraint pollution means that the case for P217 Proposed when compared with the current baseline remains 'marginal', particularly when the Alternative is a far better option under the current climate</p>

Respondent	Response	Rationale
National Grid	Yes	<p>The original P217 proposal moves the imbalance price towards a marginal methodology. Theoretically this is a move towards a more appropriate price, as a marginal price would allow participants to more appropriately assess whether it is economically efficient to resolve their energy position in the forward market, or allow it to be resolved by the System Operator in the BM and accept imbalance price exposure. This must ultimately lead to an energy market that clears more efficiently.</p> <p>However P217 introduces a new imbalance price methodology. The implementation of any new methodology carries inherent risk as to whether the methodology actually achieves its intended aim. Also the constraint flagging methodology does not presume to capture 100% of actions taken to resolve constraints. Although we are confident that the flagging methodology will identify the vast majority of constraint actions there may be occasions when they will be retained in the imbalance price. It is a peculiarity of this methodology that the retention of one unidentified constraint action within the price stack allows any others priced more favourably to be retained as well. Although we believe this will be a limited occurrence it does add a degree of uncertainty to the methodology. In such circumstances there is a risk that the imbalance price may occasionally still be polluted by transmission constraint actions, and therefore would not be representative of the cost of energy balancing. The greater value of PAR proposed in the alternative modification would lessen the materiality of any pollution, and therefore should act as mitigation against any loss of market confidence.</p> <p>On balance we believe that it is theoretically right to reduce the PAR value, however, the level of uncertainty regarding the implementation of a new methodology would suggest that the alternative P217 proposal what be the more appropriate, pragmatic proposal at this time. This would allow a period of assessment and review which may lead to a proposal to move the level of PAR in the future.</p> <p>Therefore we believe that the alternative, at this time, better facilitates applicable objective B & C</p>
EDF Energy	Yes	<p>We concur with the recommendation that the Proposed Modification should not be made.</p> <p>Our belief that the Modification should not be made is based on three principles: first, we do believe that reserve-related acceptances of bids and offers should be excluded from setting cashout prices. We believe that reserve is a system "good" in that it maintains security and quality of supply in according with the SQSS (Security and Quality of Supply Standard) Grid Rules. The maintenance of an adequate reserve margin is needed not for spot supply of power (spontaneous energy, minute by minute), but to maintain system security, and hence to maintain the quality (reliability) of supplies. It also contributes to the maintenance</p>

Respondent	Response	Rationale
		<p>of correct frequency and phase, which are other elements of system supply quality.</p> <p>Our second reason for opposing implementation is that the Modification (both Proposed and Alternative) contains a serious defect whereby the flagging and re-pricing process - which is supposed to remove BOAs that are subject to transmission constraints and are distorting imbalance price – is redundant over the peak periods of the day due to small volumes of fast response/reserve creation (which can be themselves classed as ‘system’ actions by NIV tagging respectively) resulting in constrained Offers being classed as ‘in-merit’.</p> <p>The final reason, which is of great concern, is that we believe that the flagging process will give greater opportunity for particular classes of generators (especially large portfolio generators and those geographically located near weak system infrastructure) to manipulate the transmission system and create constraints, ultimately leading to very high BSUoS costs landing on parties. The concept of parties ‘self-policing’ may not work well in some cases, as it has not worked well in some cases in the past - and is not working well even at the time of writing this response. There is a material impact on, ultimately, consumers from these patterns of behaviour.</p>
Uskmouth Power	No	<p>Uskmouth believes that the original modification would better facilitate the BSC objectives, notably objective b) as the prices under P217 would be more cost reflective and thus the true cost associated with the role of the SO could be better identified and incentivised. The modification does not remove the incentive to balance (unlike P211) and thus parties should still operate to balance their own positions. These factors should lead to an economically efficient operation of the transmission network as a whole.</p> <p>Uskmouth recognises that the Panel may have concerns that the PAR100 element of the modification will result in more marginal prices. However, as a general principle Ofgem has always favoured marginal pricing in order to ensure that the imbalance costs faced by a party are a good reflection of the actual cost of the marginal power used to make up the parties’ shortfalls. As the better tagging used by the modification should remove the majority of the system and energy plus actions from cashout prices, PAR100 seems appropriate. This cost reflectivity is important when considering the modification against BSC objective C).</p> <p>The greater transparency introduced by the modification would also better achieve objectives B) and C) as it allows the market as a whole to better understand how the system is balanced and what the costs of the different services are. In the longer term this may influence locational decisions by generators, changes in balancing behaviour, etc..</p>

Respondent	Response	Rationale
		Furthermore the transparency should better allow Ofgem to monitor activity when the market is thin, for example when a constraint is active and only two plants are operating behind it. Ofgem's ability to carry out effective market monitoring is important in achieving their duties to protect the interests of customers.
Scottish and Southern Energy plc.	Yes	For the reasons we have outlined at the Assessment Phase, whilst we have some sympathy with the Original P217 proposal we have concluded that, when compared to the P217 Alternative, the alternative better meets the applicable objectives. Therefore we conclude that the Original P217 proposal should not be made.
Alcan Smelting and Power UK	Yes	P217 Proposed offers many of the benefits associated with P217 Alternative (as discussed below), but the additional proposal for the PAR value to be revised from 500MWh to 100MWh creates additional complexity and uncertainty. Any imperfections in the revised tagging methodology would be amplified by a parallel move towards more marginal pricing. This increases the risk of an unrepresentative action setting the main cashout price. We consider that it is appropriate to address the issue of system balancing actions polluting the calculation of cashout prices as a priority without increasing the complexity of the solution and potential implications of unintended consequences by concurrently reducing the PAR value.

Question 2: Do you agree with the Panel's provisional recommendation to the Authority contained in the draft Modification Report that Alternative Modification P217 should be made?

Summary

Yes	No	Neutral/Other
6	1	

Responses

Respondent	Response	Rationale
RWE Trading	Yes	As we stated in the Modification Proposal: The proposed modification will better facilitate Objective B , related to the economic and efficient operation of the transmission system, by ensuring that cash out prices reflect the marginal cost of balancing the system for energy purposes. By removing system actions from cash out there will be appropriate market signals. This will ensure economic and efficient resolution of energy imbalances.

Respondent	Response	Rationale
		<p>The proposed modification will better facilitate Objective C, related to 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 by ensuring that system actions do not distort the calculation of energy imbalance prices. In addition, the proposal should result in more efficient despatch of generation and demand side management by resulting in energy imbalance prices that provide the correct signals into the market.</p> <p>The removal of the current confusing and inconsistent arrangements for separating system and energy actions and its replacement with a transparent and objective means of distinguishing the nature of SO actions means that the modification proposal will better facilitate Objective D relating to promoting efficiency in the implementation and administration of the balancing and settlement arrangements.</p> <p>These comments are based on the original submission in the modification proposal.</p>
ScottishPower	Yes	<p>ScottishPower support P217 Alternative and believe that this would better facilitate the achievement of the applicable BSC objectives in the following ways:</p> <p>Objective (b) – efficient operation of the transmission system - P217 Alternative would provide a more cost reflective main Energy Imbalance Price, as the impact of transmission constraints would be significantly reduced. PAR 500MWh will retain the benefit of a stronger signal to Parties to balance their position without the inherent unmanageable risks of a PAR value of 100MWh. The less penal effect will also promote more generation capacity to be made available for the market and at times of system stress.</p> <p>Objective (c) – promote competition - P217 Alternative should result in a more cost reflective main Energy Imbalance Price by more accurately reflecting only the energy costs incurred by the SO to resolve the net imbalance on the system and thus more accurately allocate the costs on those Parties out of balance. Greater transparency into the imbalance pricing arrangements means participants would have greater understanding of how the main Energy Imbalance Price is calculated and constrained areas. It offers a less penal scheme than the Proposed, which will help safeguard competition in the market. The strong signal under PAR100 is retained under this Alternative in times of system stress without penal costs where there is a genuine inability to balance. PAR100 greatly increases the risk to the market that some of these smaller Parties will default. This Alternative as well as significantly removing the effect of transmission constraints on the energy imbalance price will reduce this risk, avoiding a significant increase in the cost to all</p>

Respondent	Response	Rationale
		participants in managing their risk exposure. This would be better for promoting competition than the Proposed and the current baseline.
National Grid	Yes	See above
EDF Energy	No	<p>We disagree with the Panel's initial recommendation for the same three reasons associated with Proposed Modification, as outlined in our response to question 1 above.</p> <p>In particular, we urge the Panel to carefully consider the potential strategies and incentives for one or two strategically-located generators that could, post-implementation, have more information with which to manipulate the transmission system and the Balancing Mechanism at the expense of other classes of parties. Consideration must be given to the incentives (or lack of), and to past and current patterns of behaviour, when reviewing concepts such as 'self policing'.</p> <p>We also hope that the Panel has considered the worked example of the classification defect which we have provided as part of the Assessment process and understand the serious limitation of the proposed method during the peak periods which are the most relevant and volatile periods of the day.</p>
Uskmouth Power	Yes	<p>Uskmouth agrees that the P217 alternative does better facilitate the relevant objectives and is thus an improvement over the baseline. However, we do not believe that the proposal is as good as the original as it does not make prices as cost reflective. That said, we appreciate that Ofgem and smaller suppliers may have concerns about PAR100. It may therefore be best if Ofgem were to approve the alternative modification and the industry could review the value of PAR say 12 month after implementation.</p> <p>As discussed above, we believe that the general principles that are introduced by the P217 modification and the alternative better facilitate the relevant objectives, notably B0 and C). We have noted the comments about objective D) being fulfilled by adding understanding to the BSC, but feel this is at best marginal – it just is complicated!</p> <p>Uskmouth would note that the analysis performed by the working group does suggest that the cash-out prices between the original and alternatives vary very little so Ofgem may feel comfortable going to a more pure approach.</p>
Scottish and Southern Energy plc.	Yes	<p>As note in our response to Q1 above, we believe that the Alternative P217 Modification better meets the applicable objectives.</p> <p>As we have indicated previously we have noted the arguments discussed by the Modification Group with regard to the removal or reduction of</p>

Respondent	Response	Rationale
		<p>PAR values and the resulting move towards full or increased marginal pricing. In theory this seems more achievable with an improved means of identifying and removing the price impact of inappropriate constraint actions within energy imbalance prices.</p> <p>SSE consider however that a legitimate risk remains that the Flagging methodology proposed by the System Operator may fail to identify a constraint action and that as such, at times, a false perception may be created of the marginal energy action within the price stack. This in turn may allow high cost and volume constraint actions to influence the price, which would undermine the rationale for the modification. Were pricing to move to a marginal methodology, then a simple error in identifying an action could result in a pricing outcome influenced by inappropriate actions and with a potentially volatile and severe effect upon out of balance parties. We believe that there is sufficient uncertainty to warrant caution and to see how well the methodology operates in practice before deciding whether to establish an increasingly marginal pricing signal.</p> <p>As such, SSE would advocate that caution is exercised and that a PAR 500 value for the main energy price calculation is retained until an assessment can be undertaken as to how accurately constraints are being flagged by the proposed methodology (in particular with regard to unidentified constraint actions). For this reason, SSE prefer the alternative modification to the proposed, as it provides for a softer landing on impacted parties should the flagging methodology to be adopted prove less reliable and accurate than anticipated.</p>
Alcan Smelting and Power UK	Yes	<p>Applicable BSC Objective (b) – Efficient, economic and co-ordinated operation by the Transmission Company of the Transmission Service</p> <p>P217 Alternative aims to strip out from the calculation of cashout prices the impact of system balancing actions, which should result in a more cost reflective main Energy Imbalance Price. Enhancing the cost reflectivity of cashout prices should lead to more appropriate incentives for Parties to balance, which should, in turn, be beneficial for the efficient operation of the transmission system.</p> <p>Maintaining a PAR level of 500MWh reduces the extent of changes to the cashout rules and so mitigates some of the uncertainty associated with this rule change. P217 Alternative, therefore, delivers a solution to address the key issue of system balancing actions polluting cashout prices, without including additional rule revisions. This represents a pragmatic solution which should aid efficient system operation during the period of transition to the revised tagging arrangements.</p> <p>Applicable BSC Objective (c) – Promotion of effective</p>

Respondent	Response	Rationale
		<p>competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity</p> <p>Reducing the impact of system balancing actions on the calculation of cashout prices (as referred to above) should target more appropriate imbalance costs onto Parties. Appropriate cost targeting should enhance competition.</p> <p>The proposed revisions to the tagging mechanisms and the disaggregation of non-Balancing Mechanism actions should enhance transparency associated with the rationale for the SO's balancing actions and their inclusion in cashout prices. Enhanced transparency should be beneficial for competition.</p>

Question 3: Do you agree with the Panel's provisional recommendation concerning the Implementation Date for P217?

Summary

Yes	No	Neutral/Other
7	-	-

Responses

Respondent	Response	Rationale
RWE Trading	Yes	The solution that has been proposed by the System Operator requires development of an appropriate constraint flagging methodology using control room resources. This critical element of the design will require extensive testing to ensure that the solution is fit for purpose.
ScottishPower	Yes	n/a
National Grid	Yes	The implementation date is dependent upon a substantial amount of IS changes to the appropriate systems within Elexon and National Grid, as well as changes to industry participants systems. It is our belief that approximately one year, post modification decision is required in order to ensure the accuracy and robustness of the effected systems. Therefore we agree with the Panels recommendations.
EDF Energy	Yes	n/a
Uskmouth Power	Yes	n/a
Scottish and	Yes	-

Respondent	Response	Rationale
Southern Energy plc.		
Alcan Smelting and Power UK	Yes	-

Question 4: Do you agree with the Panel's view that the legal text provided in the draft Modification Report delivers the solution agreed by the Modification Group?

Summary

Yes	No	Neutral/Other
5	-	1

Responses

Respondent	Response	Rationale
RWE Trading	Yes	n/a
ScottishPower	Yes	n/a
National Grid	Yes	n/a
EDF Energy	Yes	n/a
Uskmouth Power	Yes	n/a
Scottish and Southern Energy plc.	Yea	n/a
Alcan Smelting and Power UK	Neutral	No comment

Question 5: Are there any further comments on P217 that you wish to make?

Responses

Respondent	Response	Rationale
RWE Trading	No	-

Respondent	Response	Rationale
ScottishPower	Yes	ScottishPower would reiterate the view that it is prudent to keep PAR at 500MWh now, giving time for any imperfections in the new methodology to be refined. Then assess and review the PAR value after 6 months of operational experience with further analysis to evaluate if a better PAR value between 100MWh and 500MWh could be found.
National Grid	No	-
EDF Energy	No	-
Uskmouth Power	No	-
Scottish and Southern Energy plc.	No	-
Alcan Smelting and Power UK	Yes	As noted above P217 Alternative will better facilitate applicable BSC Objectives. However its benefits are more wide-reaching than the BSC alone. As the modification will reduce the impact of imbalance prices on smaller participants it will provide a more attractive pricing environment for small scale renewable, CHP and distributed generation, all of which are crucial to both security of supply and reducing the impact of climate change.