P211 TRANSMISSION COMPANY ANALYSIS AND IMPACT ASSESSMENT – RESPONSE PRO-FORMA

In accordance with paragraph F 2.8 of the Code, please respond to the following questions concerning P211 (including the rationale for each response):

Q	Question	Response
1	Please outline any impact of the Proposed Modification on the ability of the Transmission Company to discharge its obligations efficiently under the Transmission Licence and on its ability to operate an efficient, economical and co-ordinated transmission system.	It is our understanding that the aim of the unconstrained schedule in this proposal is to reflect the feasible MWs accessible to the System Operator in a timeframe similar to that in which the System Operator would realistically make the decisions to use these MWs to balance the system. We appreciate that this is not a simple thing for an imbalance price methodology to achieve. The development of rules to reflect such circumstances must balance simplicity and accuracy and will always introduce a level of approximation. However, we believe the disregarding of plant dynamics, in determining the accessibility of MWs, moves too far towards simplicity with the consequence that it compromises the accuracy and appropriateness of the price generated by the proposal. It allows plant that would not realistically be accessible to the system operator to be included in the unconstrained stack. In such a scenario energy from plant with a long notice to synchronise and plant with very slow run up or run down rates would all be included in the unconstrained stack even if not accessible to the system operator. It is also our understanding that bid pair submissions that overlapped the level of SEL would be treated as single discreet accessible volumes when in reality dynamic considerations would mean a proportion of this volume would only be accessible in the event that the BMU was desynchronised and would have to be accepted in conjunction with a less attractive bid pair volume. It is likely that the inclusion of these MWs will hinder the ability of the price to be cost reflective. Participants will be able to price these inaccessible volumes at a significant discount to the market value of energy at that time, safe in the knowledge that the SO could not physically procure them. This then enables participants to price these MWs in a manner to affect cash out prices without the need to sell at an unattractive, unreflective price. The physical impact of this price behaviour on National Grids ability to operate the

		transmission system in an efficient and economic manner is not certain. Predominantly, however, this impact will be driven by the influence this price methodology has on the behaviour of market participants. This then will impact on the manner in which participants manage imbalance risk. If the risk of imbalance is diminished, but the cost of resolving imbalance risk in the forward market stays the same, then it is likely that participants will be less likely to contract in the forward market at times where there is a noticeable difference between this cost and the perceived imbalance price. This reduced incentive to balance is likely to reduce the level of NIV, especially over the demand peak, and will require the System Operator to carry greater levels of reserve and resolve greater volumes of short market imbalance. Both these activities will incur an associated extra cost to the market.
2	Please outline the views and rationale of the Transmission Company as to whether the Proposed Modification would better facilitate achievement of the Applicable BSC Objectives.	We are of the opinion that the increase in costs caused by the need to procure greater volumes of reserve to accommodate a market that goes shorter over the peak demand of the day will be detrimental to the System Operators ability to manage the transmission system in an economic and efficient manner. As such it will not better facilitate BSC objective B "The efficient, economic and co-ordinated operation of the GB transmission system". In relation to objective C an assessment of the benefit of this modification hinges on whether such a price methodology leads to a more efficient, competitive market. The determination of how this is demonstrated ads more complexity to the issue. One way to consider this question is whether a BSC participant is able to use the imbalance price to determine whether it is economically more efficient for them or the System Operator to manage the risk a BSC participant faces in relation to energy account imbalance. If this signal is not appropriate then the markets ability to promote competition is effected. Participants will not be fully exposed to the consequences of their actions and imbalance costs, rather than being reflected back on to the participants that contributed to them, will be socialised amongst the industry at large. More efficient, competitive market participants will not, therefore, benefit from their more efficient risk management strategy. Another view expressed is that this modification will lead to more predictable, less volatile prices. This trend in prices may occur under modification P211, not withstanding the ability of

		participants to game and consequently change the price quite dramatically. However this suggests that all price volatility reduces competition. It is our belief that although true in certain circumstances the price must be able to reflect the state of the market and must be able to react and reflect times of energy scarcity at all lead times. Otherwise there is no incentive for market participants to react to the conditions on the day. Therefore we have concerns that this modification may not be cost reflective. The methodology has the ability to both discount and overstate the costs incurred by the system operator in resolving imbalance. We are also concerned that it may not reflect genuine market volatility. It also has the potential to be distorted through gaming. As such we do not believe that this modification will better meet BSC objective 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"
3	Please outline the impact of the Proposed Modification on the computer systems and processes of the Transmission Company, including details of any changes to such systems and processes that would be required as a result of the implementation of the Proposed Modification.	National Grid will be required to modify systems receiving SAA data and business process to cope with the new IO14 variables
4	Please outline any potential issues relating to the security of supply arising from the Proposed Modification.	We do not believe there are any short-term, security of supply implications as a consequence of this modification although it will make the management of the transmission system more challenging and potentially more costly to the market. However we do note some concern over the effect a dampened, non cost reflective imbalance price may have on the forward market. As much as any imbalance price has an impact on the forward curve and the decisions BSC participants take regarding building new plant or keeping existing plant open, an imbalance price that does not appropriately incentivise the market to contract the marginal MW over the peak must be detrimental to the quality of investment decisions BSC participants make in regard to retaining existing capacity and providing sufficient generation into the future.
5	Please provide an estimate of the development, capital and operating costs (broken down in reasonable detail) which the Transmission Company anticipates that it would incur in, and as a result of,	An initial estimate of the cost of implementing this modification is approximately £80K with a lead time of approximately 7 months

	implementing the Proposed Modification.	
6	Please provide an estimate of the development, capital and operating costs (broken down in reasonable detail) which the Transmission Company anticipates that it would incur in, and as a result of, implementing the Proposed Modification if the Transmission Company were also to produce the EPUS stack (as defined in section 2.1-2.4 of the P211 Requirement Specification), after the application of EPUS Arbitrage Tagging, required to resolve NIV and provide this to BSC Central systems.	Regrettably, due the size and scope of this request it will not be possible to carry out this IS cost assessment in the timescales requested. However, if the working group feels there is benefit in progressing this solution, and subject to a clear requirement specification so that National Grid understands in some level of detail what is being asked of it, we would be happy to progress an assessment of the estimated cost and development lead time required for this particular implantation option.
7	Please provide an estimate of the development, capital and operating costs (broken down in reasonable detail) which the Transmission Company anticipates that it would incur in, and as a result of, implementing the Proposed Modification if the Transmission Company were also to The main Energy Imbalance Price as derived in the P211 Requirement Specification (section 2) and provide this to BSC Central systems (BMRA) such as to enable prompt price reporting in the same (or similar) timescales as present.	Regrettably, due the size and scope of this request it will not be possible to carry out this IS cost assessment in the timescales requested. However, if the working group feels there is benefit in progressing this solution, and subject to a clear requirement specification so that National Grid understands in some level of detail what is being asked of it, we would be happy to progress an assessment of the estimated cost and development lead time required for this particular implantation option.
8	Please provide details of any consequential changes to Core Industry Documents and/or the System Operator Transmission Owner Code that would be required as a result of the implementation of the Proposed Modification (and, if applicable, any Alternative Modification).	We are not presently aware that this modification would require consequential changes to any other core industry documents or the System Operator Transmission Operator code
9	Any other comments on the Proposed Modification (and Alternative Modification if applicable).	No

Please send your response by **17:00** on **2 July 2007** to modifications@elexon.co.uk. Any queries regarding the analysis should be addressed to Chris Stewart on 0207 380 4309 or email address chris.stewart@elexon.co.uk.