

Responses from the Initial P136 & P137 Assessment Consultation

Consultation issued 16/09/03

Representations were received from the following parties:

No	Company	File Number	No. BSC Parties Represented	No. Non-Parties Represented
1.	Gaz de France	P136-P137_ASS1_001	1	0
2.	ConocoPhillips	P136-P137_ASS1_002	2	0
3.	EDF Energy	P136-P137_ASS1_003	9	0
4.	Corus Group	P136-P137_ASS1_004	0	1
5.	Innogy	P136-P137_ASS1_005	9	0
6.	Scottish Power	P136-P137_ASS1_006	6	0
7.	Edison Mission Energy	P136-P137_ASS1_007	1	0
8.	Ineos Chlor Limited	P136-P137_ASS1_008	2	1
9.	BizzEnergy Ltd	P136-P137_ASS1_009	1	0
10.	Powergen	P136-P137_ASS1_010	14	0
11.	Alcan Smelting and Power UK	P136-P137_ASS1_011	0	1
12.	Scottish and Southern	P136-P137_ASS1_012	4	0
13.	British Gas Trading	P136-P137_ASS1_013	1	0
14.	InterGen UK Ltd	P136-P137_ASS1_14	4	0

15.	Teesside Power Ltd	P136-P137_ASS1_015	1	0
16.	Entergy-Koch Trading Europe Ltd (late response)	P136-P137_ASS1_016	1	0
17.	Aquila Networks (late response)	P136-P137_ASS1_017	1	0

P136-P137_ASS_001 – Gaz de France

Respondent:	<i>Name</i>
No. of BSC Parties Represented	<i>1</i>
BSC Parties Represented	<i>Gaz de France Marketing Limited</i>
No. of Non BSC Parties Represented	<i>0</i>
Non BSC Parties represented	<i>N/a</i>
Role of Respondent	<i>Supplier</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	<p>The current pricing methodology delivered by modification proposal P78 has had significant impact on the prices to which parties out of balance are exposed. This methodology has yet to be tested during a winter peak maximum demand situation however has delivered high prices and additional volume, and therefore one would assume 'the correct pricing signals', during several instances this summer when NGC issued a series of Notice of Insufficient System Margin warnings.</p> <p>Ofgem stated in their P78 decision letter of 9th September 2002 that the P78 proposal would 'increase the level of competition by encouraging Parties to trade ahead of Gate Closure', whilst NGC stated that 'it had not experienced any adverse effects on the behaviour of market</p>

Q	Question	Response	Rationale
			<p>participants since the changes to BRL and Gate Closure and that the proposed change to Energy Imbalance Prices on 25th February 2003 presented no operational concerns’.</p> <p>Proposed modification P136 would introduce significant market risk regarding the increased potential for generation reserve to be withheld by portfolio players from the market to mitigate against potential supply side shortfalls and so, in our view, would not better facilitate any of the BSC objectives.</p>
2.	<p>Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)</p>	No	Same response as for question 1 above
3.	<p>Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale</p>	Yes	<p>We presume the modification group have yet to discuss in detail:</p> <p>the most appropriate balance between the incentive for participants to ensure a ‘long’ position in order to balance out the risk of inaccurate forecasting and avoid potentially significant marginal pricing versus NGC licence obligations to keep the transmission system in energy balance close to, and in, real time. This we assume could take into account the interaction between the Pre Gate Closure products NGC have at their disposal and potential for the development of further innovation in this area, particularly with reference to the inclusion of significant provision from the demand side versus the potential for significant gains following the adoption of a marginal pricing approach.</p> <p>evidence that the benefits forecast to be delivered following the introduction of modification P78 have failed to be achieved, especially as the current arrangements have yet to be experienced through winter peak demand conditions</p> <p>the effects on the small generation and renewables side of the market if marginal pricing were adopted</p>

Q	Question	Response	Rationale
			We would expect to see the result of the groups analysis in this area
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	Same response as for question 3 above
5.	Are there any further comments on P136 that you wish to make?	Yes	<p>The potential significant impact of a return to marginal pricing cannot be underestimated for a small new entrant specialist supplier to the energy market. We believe there to be numerous processes within our organization that will be impacted by this proposal, including:</p> <p>The business of pricing/forecasting going forward which will be far more difficult therefore is likely to result in increasing risk premiums and prices to our customers. As new entrants this will severely affect our ability to compete on an equal basis with those with a larger more balanced, integrated or predictable portfolio</p> <p>The credit implications are significant - with out-turn prices being calculated post gate-closure it will be difficult to predict the correct level of credit cover required therefore the potential for an increase of mistakes in this area is likely, particularly if high marginal prices (up to £99,999.99 MWh) persist over a number of half-hour periods. There is a very serious and real potential for bankruptcy for small players, including the potential 'double whammy' if those with any generation assets were to suffer a unplanned outage in the same half hours as a significantly high marginal price combined with an unforecast increase in consumption against purchased supply</p> <p>Timeliness of price reporting of great concern, as we would not know indicative prices immediately</p> <p>Impossible to forecast the impact on the Residual Cashflow Reallocation Cashflow element of the price</p> <p>Creates barriers to entry due to significantly increased market risk</p>

Q	Question	Response	Rationale
6.	Are there any further comments on P137 that you wish to make?	Yes	Same response as for 5 above

P136-P137_ASS1_002 – ConocoPhillips

Respondent:	<i>Name: Rekha Patel</i>
No. of BSC Parties Represented	2
BSC Parties Represented	<i>ConocoPhillips UK Limited and Immingham CHP</i>
No. of Non BSC Parties Represented	
Non BSC Parties represented	<i>Please list all non BSC Parties responding on behalf of (including the respondent company if relevant).</i>
Role of Respondent	<i>Trader and Generator</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	<p>ConocoPhillips do not support proposed modification P136. We do not believe that the proposal better facilitates the applicable BSC Objective (c) and (b).</p> <p>The proposal introduces a 'marginal' price methodology being applied to the 'main' energy imbalance price. A 'marginal' main imbalance price has the detrimental impact of over-recovering the cost of balancing the system, thus creating greater inefficiency within the market. Market participants that are exposed to the marginal 'main' price, shall be charged the cost of supplying the last increment of energy required to balance generation and demand. In reality, the cost of balancing the system shall be lower than the revenue gained from charging on a marginal basis.</p>

Q	Question	Response	Rationale
			<p>As a consequence of the BM cashflows being over-recovered, the Residual Cashflow Reallocation Cashflow (RCRC) shall be high. This allows a small section of market participants to benefit from the implementation of artificially, exacerbated marginal 'main' imbalance prices, through revenues gained from the RCRC. As a result of some participants gaining revenue from the over-recovery of balancing costs, applicable BSC Objective (c) shall not be better facilitated.</p> <p>The potential effect of introducing marginal 'main' imbalance price is incentivising market participants to undertake a 'long' position rather than being balanced, thus protecting themselves from the risk of exposure to a marginal imbalance price. The consequence of each market participant holding its own level of reserve leads to inefficiency, thus preventing improvements of applicable BSC Objective (b), 'the efficient, economic and co-ordinated operation by the Transmission Company of the Transmission System.'</p> <p>A 'marginal imbalance environment shall merely increase the cost of market participants' unmanageable risks, thus increasing the probability of parties going out of business. For example, on the demand-side, suppliers have a forecast error margin of 4-5%, whilst on the generation-side, a power plant may incur an unplanned outage, thus exposing both to penal, non-cost reflective, marginal cash-out. prices.</p>
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	ConocoPhillips do not support proposal P137. Please refer to the rationale provided above as a consequence of the modification proposal P137 also seeking to introduce a 'marginal' imbalance cash-out price methodology, thus replacing the current 'average' imbalance price mechanism.
3.	Does P136 raise any issues that you believe have not been identified so far and	No	

Q	Question	Response	Rationale
	that should be progressed as part of the Assessment Procedure? Please give rationale		
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	
5.	Are there any further comments on P136 that you wish to make?	Yes	<p>ConocoPhillips believe that the current 'average' energy imbalance price mechanism is an efficient and effective approach. Therefore, we do not believe it is appropriate to move the imbalance cash-out methodology to a 'marginal' environment esp. taking into consideration the adverse effects highlighted within question 1. We would like to propose changes to BSAD rather than implementing 'marginal' main imbalance prices.</p> <p>We believe that the artificial cap, within the current imbalance price calculation is associated with the inclusion of Balancing Services Adjusted Data (BSAD). The current BSAD methodology obscures the underlying true cost of balancing through option fees paid to standing reserve generators being feed through into cash-out prices as the average of the capacity fee paid for those periods in which they were made available, rather than in those periods in which they actually produce.</p> <p>Targeting BSAD payments to the settlement periods where the service is likely to be utilised, shall provide more appropriate signals to incentivise market participants to contact forward. By enhancing the incentives through building and improving upon the existing methodology of 'average' imbalance prices and better cost targeting of BSAD, shall incentive participants to</p>

Q	Question	Response	Rationale
			balance, thus increasing the level of competition by encouraging parties to trade ahead of gate closure, thus better facilitating BSC Objective (b).
6.	Are there any further comments on P137 that you wish to make?	Yes	Please refer to the comments provided above, within question 5.

P136-P137_ASS1_003 – EDF Energy

Respondent:	<i>Tony Diccico</i>
No. of BSC Parties Represented	<i>9</i>
BSC Parties Represented	EDF Energy Networks (EPN) plc; EDF Energy Networks (LPN) plc EDF Energy Networks (SPN) plc; EDF Energy (Sutton Bridge Power) EDF Energy (Cottam Power) Ltd; EDF Energy (West Burton Power) Ltd; EDF Energy plc; London Energy plc; Seeboard Energy Limited
No. of Non BSC Parties Represented	<i>Zero</i>
Non BSC Parties represented	
Role of Respondent	<i>Supplier/Generator</i>

Q	Question	A.	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC	No	Please see, first, our response to question 5. We believe that marginal pricing approaches may be too gameable and are likely to lead to results that are too volatile. This is why the marginal pricing approach (SMP) used in the Pool was abandoned.

Q	Question	A.	Rationale
	Objectives? Please give rationale and state which objective(s)		<p>It may be that after the winter has passed, reforms to the current cashout price formulation that are beneficial will be evident, but we do not at present see evidence that the passing of this modification would better meet the BSC Objectives.</p> <p>There is, however, one element of the modification which, taken in isolation, would be beneficial in respect of 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" – and that is the possibility that is raised that NGC's forward trade data, currently only fed to the market and into the imbalance cashout calculation process in aggregated form, could be fed to the market and into the imbalance cashout calculation process in disaggregated form, increasing market transparency and facilitating more accurate operation of the cashout calculations. The wording of the mod is ambiguous but we note that NGT's rep at the mods group has said this (disaggregated data) is likely to be acceptable to NGT.</p> <p>The gaming concerns that exist for Mod 136, also apply for Mod 137, as both are based on a marginal pricing approach.</p> <p>Our views may develop as further considerations of the modification at the mod group take place; we note that there is likely to be another assessment consultation with a more reasonable response timeframe later on.</p>
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	<p>It may be that after the winter has passed, reforms to the current cashout price formulation that are beneficial will be evident, but we do not at present see evidence that the passing of this modification would better meet the BSC Objectives.</p> <p>There is, however, one element of the modification relating to data transparency which, taken in isolation, would be beneficial (for a fuller explanation see our reply to question 1 above); note that mod 137 is much clearer on this point (it states that the data be disaggregated as a firm feature of the mod).</p> <p>Note also the mod 137 would appear likely, in its treatment of standing reserve option fees, to significantly increase the volatility of system buy prices. Although the treatment of standing reserve option fees under P137 would differ from that which preceded Modification P3, it would effectively take us back to a situation which we previously regarded as undesirable (and still do), because of the unwarranted extra risk to which market participants would be subjected.</p>
3.	Does P136 raise any other		Credit cover arrangements and the level of the credit assessment price would clearly need reviewing carefully.

Q	Question	A.	Rationale
	issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale		
4.	Does P137 raise any other issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale		Credit cover arrangements and the level of the credit assessment price would clearly need reviewing.
5.	Are there any further comments on P136 that you wish to make?	Yes	We see merit in stability of the NETA arrangements, especially the imbalance cashout pricing mechanism which plays such an important role in ensuring efficient competition in the electricity market. This is not to say that we would discount the possibility that changes in this area might better meet the applicable BSC objectives, but rather that we feel that this could be much better assessed after the effects and any defects in the operation of P78 during and throughout the coming winter have been observed. If the rules are changed too readily, even a beneficial change might have limited effect as investors would not give much weight to its effects, being uncertain as to its stability / endurance.
6.	Are there any further comments on P137 that you wish to make?	Yes	As above

P136-P137_ASS1_004 – Corus Group

Corus has directly connected and embedded demand sites and is also a licence exempt generator. Our response to the initial consultation is: Q1 and Q2. No in both cases. The increased level and volatility of prices that will result if these modifications were implemented will not promote competition. It is likely that they will impinge more adversely on smaller generators and suppliers, and the increased risk will create a further barrier to entry and hasten exit. Q3 and Q4. Yes in both cases. If not already explicitly identified, the effect on end-users must be at the heart of the analysis. Q5 and Q6. Yes in both cases. Marginal pricing was one of the main defects of the discredited Pool system and was quite rightly replaced by pay-as bid in NETA. We do not believe it is in the interests of those who pay the bills - ie consumers - for it to be resurrected.

Regards,

Stephen Macey.

P136-P137_ASS1_005 – Innogy

Respondent:	<i>Name Bill Reed</i>
No. of BSC Parties Represented	<i>9</i>
BSC Parties Represented	<i>Please list all BSC Parties responding on behalf of (including the respondent company if relevant). Innogy plc, Innogy Cogen Limited, Innogy Cogen Trading Limited, Npower Limited, Npower Direct Limited, Npower Northern Limited, Npower Northern Supply Limited, Npower Yorkshire Limited, Npower Yorkshire Supply Limited.</i>
No. of Non BSC Parties Represented	<i>None</i>
Non BSC Parties represented	<i>Please list all non BSC Parties responding on behalf of (including the respondent company if relevant).</i>
Role of Respondent	<i>(Supplier/Generator/ Trader / Consolidator / Exemptable Generator / BSC Agent / Party Agent / other – please state) Supplier/Generator/ Trader / Consolidator / Exemptable Generator / Party Agent</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	We support the introduction of marginal pricing in principle. However, we are concerned that the methodology in P136 may not accurately reflect the costs of energy balancing. Until a methodology can be defined that properly reflects the resource cost associated with energy balancing, marginal pricing will not better facilitate Objective (c) in relation to competition or Objective (b) in relation to the economic and co-ordinated operation of the system.
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	We support the introduction of marginal pricing in principle. However, we are concerned that the methodology in P137 may not accurately reflect the costs of energy balancing. Until a methodology can be defined that properly reflects the resource cost associated with energy balancing, marginal pricing will not better facilitate Objective (c) in relation to competition or Objective (b) in relation to the economic and co-ordinated operation of the system.
3.	Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	We are particularly concerned about the potential for prices to change ex post in relation to adjustments in the NIV or Offer and Bid volumes to reflect NGC's trading activities We believe that further consideration of the stability of prices in this context is required.
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure?	Yes	We are particularly concerned about the potential for prices to change ex post in relation to adjustments in the NIV or Offer and Bid volumes. For example, P137 introduces at least three levels of additional tagging to the price setting process (offset, undo and option fee tagging) to the existing four (de minimus, arbitrage, CADL and NIV tagging). The treatment of ABSVD volumes and non BM offers adds further levels of complexity (with the potential for a total of 9 levels of tagging, or even more with the maximum generation, demand turn down and intertrip

Q	Question	Response	Rationale
	Please give rationale		<p>services). We believe, therefore, that consideration of the trade off between accuracy and stability of prices is required in the assessment of P137.</p> <p>In the context of the proposal to treat standing reserve option fees in offer prices, we would note that standing reserve may be called at times when the system is not short of available energy offers. Rather standing reserve is called in response to particular events on the system such as a plant trip. P137 could, therefore, result in high prices at random times when the system is not under stress and undermine the price signal that could emerge.</p>
5.	Are there any further comments on P136 that you wish to make?	Yes	<p>We believe that the market requires confidence that the prices reported in imbalance cash out are cost reflective and provide the appropriate market signals. We believe therefore that energy purchased forwards by NGC and reported as energy BSAD should not feed into the NIV or the main price calculation.</p> <p>Furthermore, we believe that prompt reporting of cost reflective prices is imperative. While we recognise the issue associated with the treatment of non BM and ABSVD volumes we believe that the uncertainty in prices caused by inaccuracy associated with estimated volumes may outweigh the potential benefits.</p>
6.	Are there any further comments on P137 that you wish to make?	Yes	<p>We believe that the market requires confidence that the prices reported in imbalance cash out are cost reflective and provide the appropriate market signals. We believe therefore that energy purchased forwards by NGC and reported as energy BSAD should not feed into the NIV or the main price calculation.</p> <p>Furthermore, we believe that prompt reporting of cost reflective prices is imperative. While we recognise the issue associated with the treatment of non BM and ABSVD volumes we believe that the uncertainty in prices caused by inaccuracy associated with estimated volumes may outweigh the potential benefits.</p>

Q	Question	Response	Rationale
			Finally we note that the treatment of option fees introduces an estimated variable into cash out prices. We believe that further work is required to establish the potential impact of such prices on cash out and whether such treatment can produce cash out prices that are more cost reflective.

P136-P137_ASS1_006 – Scottish Power

Respondent:	Man Kwong Liu (SAIC Ltd)
No. of BSC Parties Represented	6
BSC Parties Represented	<i>Please list all BSC Parties responding on behalf of (including the respondent company if relevant).</i> Scottish Power UK plc; ScottishPower Energy Management Ltd.; ScottishPower Generation Ltd; ScottishPower Energy Retail Ltd.; SP Transmission Ltd; SP Manweb plc.
No. of Non BSC Parties Represented	0
Non BSC Parties represented	<i>Please list all non BSC Parties responding on behalf of (including the respondent company if relevant).</i>
Role of Respondent	<i>(Supplier/Generator/ Trader / Consolidator / Exemptable Generator / BSC Agent / Party Agent / other – please state)</i> Supplier / Generator / Trader / Consolidator / Exemptable Generator / Party Agent

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better	No	As we have stated previously, while we agree with the principle of sending clearer price signals to the market which would better facilitate BSC objective (b) " <i>the efficient, economic and co-ordinated</i>

Q	Question	Response	Rationale
	<p>facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)</p>		<p><i>operation by the Transmission Company of the Transmission System</i>”, but we believe that this is unlikely to happen with this. As with P135, this Mod does not encourage capacity to be made available at times of system stress and will increase the risk that less reliable plant will not be made available at all due to the potentially damaging imbalance charges associated with unexpected plant failure.</p> <p>Acceptance of the modification will greatly increase the risk of generators going out of business and also significantly increase the cost to participants in managing the risk exposure.</p> <p>This, as already been highlighted in P135 consultation, would be bad for promoting competition as potential new entrants would be more reluctant to participate in such market. It is also bad for facilitate the efficiency objectives, as parties would be withholding capacities and there would be significant increase in cost of operations for all concerned. It would be far more efficient for the System Operator to utilise the capacity to balance the system. As indicated in the P135 consultation, the industry is quite happy to pay for this service by the System Operator. The current imbalance charging mechanism still ensures that "pollutants pay".</p>
2.	<p>Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)</p>	No	See our answer to (1) above.
3.	<p>Does P136 raise any issues that you believe have not been identified so far and that should be progressed</p>	Yes	<p>These proposed modifications aim to tackle the security of supply issue but we believe the marginal price solution will exacerbate the problem. In particular, treatment of post Gate Closure plant loss needs to be addressed as imbalance settlement does not take place at Gate Closure, but some time later. Unless this is recognised and considered appropriately, generators would not be encouraged to</p>

Q	Question	Response	Rationale
	as part of the Assessment Procedure? Please give rationale		provide any potential spare capacity to meet peak demand or be incentivised to balance at Gate Closure.
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	See our comment in (3) above. In addition, we do not believe that it is appropriate to change the way that standing reserve option payments are allocated. Any artificial increase to SBP (through the increased BPA) brings with it the problems most recently highlighted in the industry response to Modification P135. Increasing imbalance prices does not encourage capacity to be made available at times of system stress and will increase the risk that less reliable plant will not be made available due to the potentially damaging imbalance charges associated with unexpected plant failure. This potential change (as with P135) requires further research and development especially in the key area of security of supply.
5.	Are there any further comments on P136 that you wish to make?	Yes	We believe an alternative, which would encourage generators to offer any potential spare capacity is required. Specifically, treatment of post Gate Closure plant loss needs to be addressed, as currently participants are prohibited from adjusting their position to maintain the balance, which they had achieved at Gate Closure. In this situation, either the shortfall should be treated as system balancing and removed from the price calculation or the generator should be able to self-balance after Gate Closure. There should be some dispensation for the generators in this circumstance.
6.	Are there any further comments on P137 that you wish to make?	Yes	See our comment in (5) above.

P136-P137_ASS1_007 – Edison Mission Energy

Respondent:	<i>Libby Glazebrook</i>
No. of BSC Parties Represented	<i>one</i>
BSC Parties Represented	<i>First Hydro Company</i>
No. of Non BSC Parties Represented	<i>none</i>
Non BSC Parties represented	
Role of Respondent	<i>Generator</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	Yes	P136 will send stronger long term signals to the market on the costs of failing to contract sufficiently when the system is under stress. This will provide positive investment signals to the market to encourage the building of new generation, and the continued presence of peaking plant contributing to security of supply. This will increase competition in generation (objective c). In addition, in applying marginal prices to the main price, when the system is long, the potential for a negative or at least lower System Sell Price will enhance incentives to balance, not go long as is now the case. This will improve the efficient operation by the Transmission Company of the Transmission System (objective b).
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and	Yes	In addition to the rationale above for P136, P137 explicitly improves upon the tagging methodology and targets the expected utilisation of standing reserve to better reflect the half hourly costs NGC incurs in balancing the system.

Q	Question	Response	Rationale
	state which objective(s)		
3.	Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes / No	
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes / No	
5.	Are there any further comments on P136 that you wish to make?	Yes	<p>NGC has not specified the scope of BSAD changes that will be required to implement this modification. The BSAD variables which feed into cashout prices can and do have a major effect on cashout prices. The mechanics of how these variables are calculated by NGC is outside the scope of the mod, all central systems sees are the numbers put forward by NGC.</p> <p>Whilst we support the introduction of marginal pricing as per mod 136, we have concerns that at this stage of the process we don't know what we are 'signing up for' in terms of changes to BSAD. These changes could have a far more significant impact on cashout prices than the basic P136 mod. Unlike the BSC mods process, following consultation, NGC determines the BSAD changes to put before Ofgem for decision. Whilst these changes are consulted upon, the consultation is largely a one way process. An example of this is the recent alternative to the CAP 47 CUSC proposal that has been issued to Ofgem for decision alongside NGC's recommendation on CAP 47. The CAP 47 alternative has been proposed by NGC and has not been consulted</p>

Q	Question	Response	Rationale
			upon. We are uncomfortable that so much discretion is being left to NGC. We would like to see a BSAD and its associated documents brought within the governance of the BSC to allow a holistic process for changes to cashout prices.
6.	Are there any further comments on P137 that you wish to make?	Yes / No	

P136-P137_ASS1_008 – Ineos Chlor Limited

Respondent:	<i>Ineos Chlor Limited</i>
No. of BSC Parties Represented	<i>2</i>
BSC Parties Represented	<i>Ineos Chlor Energy Limited, ICI Chemicals & Polymers Limited</i>
No. of Non BSC Parties Represented	<i>1</i>
Non BSC Parties represented	<i>Ineos Chlor Limited</i>
Role of Respondent	<i>Supplier/Generator/Very Large Consumer</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and	No	P78, which at times of system stress has appeared to deliver appropriate and transparent pricing signals, has been a significant step forward in providing an imbalance market operates effectively. The impact of this change has not been tested through a winter yet. The notion that extreme prices generated through marginal pricing signals will provide a better representation of true costs, and better operation of the market as a whole is in our opinion fundamentally flawed.

Q	Question	Response	Rationale
	state which objective(s)		<p>The claim that marginal pricing represents an “undiluted” signal to the market is nonsense. Such a signal is not undiluted (as claimed), but is, as a result of setting the price at the extreme (margin) of the balancing costs incurred, greatly amplified.</p> <p>Under P78, RCRC payments have been very close to zero. This strongly suggests that the market is currently neither over or under recovering the costs of imbalance.</p> <p>The impact of the proposed modification will not in our opinion lead to enhanced competition in line with BSC objective (c).</p> <p>The modification will not encourage parties to trade ahead of gate closure, it will encourage parties to trade to <i>a different position</i> ahead of gate closure. Parties trade to a position set by their forecast of production and consumption. This includes margin to cover the risk of the forecast being wrong, such margin being set in part by the risk of being wrong, and in part of the consequential cost of that risk. The current arrangements provide more than adequate incentive for all parties to trade actively to match their respective requirements. Creating an artificially high penalty for imbalance will not encourage trading, but will simply mean that parties trade to a significantly long position, which is likely to be <i>less</i> balanced than before.</p> <p>The proposed modification P136 will introduce significant market risk. In such market conditions small and independent players will face a real potential for bankruptcy, directly as a result of the modification, and may choose to leave, or not to enter the market. The suggestion that the modification will enhance competition seems at best ill conceived.</p> <p>Finally, P136 will most definitely not better facilitate applicable BSC Objective (b) "the <i>efficient, economic</i> and <i>coordinated</i> operation by the Transmission Company of the Transmission System".</p> <p>We believe one possible effect of P136 will be to encourage portfolio generators to hold significant volumes of reserve to mitigate the risks of (their own) plant failure. The efficient, economic and co-ordinated operation of such reserve is not best facilitated through independent action by all such generators. The creation of</p>

Q	Question	Response	Rationale
			artificially inflated penalties for imbalance will send price signals that encourage inefficient, uneconomic and uncoordinated operation of this reserve.
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	Response as for Question 1 above
3.	Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	<p>We would question whether the issues raised by P136 have been properly addressed, in particular we believe significant consideration should be given to:</p> <p>The effect on the market of marginal pricing, particularly with respect to small and renewable generation, and the likely actions participants will take to manage these effects, in particular the reversion to "long" positions within the market.</p> <p>Whether this likely impact will affect NGC's normal operations (when the system is not under stress) in providing energy balance to the system, on the assumption that NGC will have to manage the significantly long position of the market.</p> <p>Whether such a (long-term) long position by all participants has any effect on the operation of the transmission system when security of supply is an issue.</p> <p>Whether exposing parties to very high prices at times of system stress will change the security of the</p>

Q	Question	Response	Rationale
			<p>transmission system, or simply over-recover costs from out of balance parties.</p> <p>Reviewing the effect of P78 on sending appropriate signals to the market</p> <p>Reviewing more appropriate mechanisms for managing the energy balance of the transmission system, which encourage participants to adopt an energy balanced position and provide efficient tools for NGC to manage the transmission system.</p>
4.	<p>Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale</p>	Yes	See answer above
5.	<p>Are there any further comments on P136 that you wish to make?</p>	Yes	<p>The potential move to marginal pricing as a punitive charge to out of balance parties will in our opinion have a significant and severely detrimental impact on the behaviour of parties in the electricity market. In particular:</p> <p>We will move from targeting a closely balanced position to a deliberately long position, as was the case prior to the introduction of P78.</p> <p>This will introduce significant costs upon our business, with no benefit (other than the management of risks which are created solely by this modification).</p> <p>Other market participants will undoubtedly face higher costs for risk management. The costs will ultimately</p>

Q	Question	Response	Rationale
			<p>be passed onto consumers with no benefit.</p> <p>We believe far better tools are available to the Transmission Company to manage the Transmission System, which would meet the tests of being economic, efficient and co-ordinated. In particular under NETA, the demand side has progressively lost access to market mechanisms that help in managing the transmission system. This is a result of the complexity of the markets, and the risks involved.</p>
6.	Are there any further comments on P137 that you wish to make?	Yes	See above

P136-P137_ASS1_009 – BizzEnergy Ltd

Respondent:	<i>Name Keith Munday</i>
No. of BSC Parties Represented	<i>1</i>
BSC Parties Represented	<i>Please list all BSC Parties responding on behalf of (including the respondent company if relevant). BizzEnergy Ltd</i>
No. of Non BSC Parties Represented	<i>0</i>
Non BSC Parties represented	<i>Please list all non BSC Parties responding on behalf of (including the respondent company if relevant).0</i>
Role of Respondent	<i>(Supplier/Generator/ Trader / Consolidator / Exemptable Generator / BSC Agent / Party Agent / other – please state) Supplier</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	/ No	Increasingly volatile and extreme imbalance price lead to increased price risks on physical participants. Parties optimal contractual position will change, e.g Suppliers will go longer and Generators shorter, thus the aggregate level of imbalance will increase, leading to a possibly less efficient market. Participants are already strongly incentivised to balance, further increase in incentives may not improve forecasts but result in risk strategies that will have an overall negative impact on market efficiency. Any modification that has the potential to create prices of such magnitude that they will penalise rather than incentivise players is against the BSC objectives of efficient market operation.
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives?	/ No	As above

Q	Question	Response	Rationale
	Please give rationale and state which objective(s)		
3.	Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	Insufficient time to assess P78 behaviour – need to see it in action over at least one winter. The assessments have been done on modest market conditions. If they were to be carried out under conditions when the market is under stress the probability of excessively high prices will increase. It needs to be determined whether this is acceptable or whether they will be of such magnitude to cause other problems and issues such as unnecessary participant failure.
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	As above plus. The options are bought by the System Operator as they do not know when they are going to be called. Given this then the value of the option is equal for all periods in which it can be called and would be a distortion to allocate its costs to when it is actually called, i.e. need to reflect the fact that the option is of value at all times it could be called not just when it is called.
5.	Are there any further comments on P136 that you wish to make?	Yes	The assessments appear only to concentrate on the narrow aspect of price, with an inbuilt belief that the more cost reflective the price the better the result – has this been proven. A wider look at the impact of volatile prices should be considered, especially since virtually all mods to date have been orientated around reducing unnecessary price volatility.
6.	Are there any further comments on P137 that you wish to make?	Yes	As above

P136-P137_ASS1_010 – Powergen

Respondent:	Powergen
No. of BSC Parties Represented	14
BSC Parties Represented	Powergen UK plc, Powergen Retail Limited, Cottam Development Centre Limited, TXU Europe Drakelow Limited, TXU Europe Ironbridge Limited, TXU Europe High Marnham Limited, Midlands Gas Limited, Western Gas Limited, TXU Europe (AHG) Limited, TXU Europe (AH Online) Limited, Citigen (London) Limited, Severn Trent Energy Limited (known as TXU Europe (AHST) Limited), TXU Europe (AHGD) Limited and Ownlabel Energy Limited
No. of Non BSC Parties Represented	-
Non BSC Parties represented	-
Role of Respondent	Supplier, Generator, Trader, Consolidator & Exemptable Generator

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	<p>In the context of discussions so far, our initial position is that we are not convinced that these modifications will provide the necessary linkage to forward prices to provide sufficient remuneration for generation, to ensure an appropriate capacity margin.</p> <p>There may be a short term effect when participants react to initial high marginal buy prices. However, the likely longer term effect is for people to go long to reduce their risk. This is similar to the situation which pertained before the introduction of P78 when market prices were also very low. It therefore doesn't necessarily follow that prices will be increased by this proposal.</p> <p>There is still the concern first raised during the assessment of P135, that a marginal price signal would exacerbate asymmetric risk in the market as generators would be more exposed</p>

Q	Question	Response	Rationale
			than suppliers. The marginal price signal is dampened for suppliers as they are likely to recover a proportion of any over-recovery through RCRC. However, a generator who trips will be exposed to the full cost. This is likely to result in generators being reluctant to push their units at times of system stress, if this would increase their chance of tripping as the risk is that much greater. The only generator who would be neutral in this respect would be the marginal generator and only for that volume for which the acceptance had been made.
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	See answer to 1.
3.	Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	
5.	Are there any further comments on P136 that you wish to make?	No	
6.	Are there any further comments on P137 that you wish to make?	No	

P136-P137_ASS1_011 – Alcan Smelting and Power UK

Respondent:	<i>Jonathan Scott</i>
No. of BSC Parties Represented	<i>0</i>
BSC Parties Represented	<i>N/a</i>
No. of Non BSC Parties Represented	<i>1</i>
Non BSC Parties represented	<i>Alcan Smelting and Power UK</i>
Role of Respondent	<i>Other – Licence Exempt Generator</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	<p>The modification does not better facilitate Applicable Objective (c), the promotion of effective competition.</p> <p>Alcan recognises that the modification attempts to address the issue of the market not adequately responding to signals at times of strain on system margin. Furthermore, we agree with the proposer’s rationale that the mechanisms proposed – a shift to marginal pricing within the BM – would increase the incentive on players to sufficiently contract in peak demand periods and therefore lead to an increase in forward and short-term prices.</p> <p>However Alcan is concerned that a move to marginal imbalance pricing could have significant detrimental effects on small, single-site generators who are unable to absorb imbalance price risk, unlike vertically integrated companies and non-physical traders.</p>
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC	No	See answer to Question 1

Q	Question	Response	Rationale
	Objectives? Please give rationale and state which objective(s)		
3.	Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	
5.	Are there any further comments on P136 that you wish to make?	No	
6.	Are there any further comments on P137 that you wish to make?	No	

P136-P137_ASS1_012 – Scottish and Southern

Dear Sirs,

This response is sent on behalf of Scottish and Southern Energy, Southern Electric, Keadby Generation Ltd. and SSE Energy Supply Ltd.

In relation to the six questions listed in the Consultation Paper, contained within your note of 16th September 2003 concerning Modification Proposals P136 and P137, we have the following comments to make:-

Q1 Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)

No. We do not believe that P136 addresses the defect and furthermore does not better facilitate the achievement of the Applicable BSC Objectives.

Q2 Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)

No. We believe that the proposed treatment of Standing Reserve option fees (as outlined in P137) is fundamentally flawed. We note the comments of the PSMG that this approach may result in an overstatement or an understatement of the option fees. This clearly gives rise to a cross subsidy situation.

We provided comments on this specific matter in the recent BSAD consultation published on 4th September 2003 (concerning the proposed revisions to the BSAD Methodology Statement - Treatment of Standing Reserve Option fees) and we repeat them here.

First, we do not believe that options 2 or 3 or 4 [listed in the Consultation Paper published on 4th September 2003; concerning the proposed revisions to the BSAD Methodology Statement - Treatment of Standing Reserve Option fees] will incentivise parties to contract. We believe that adopting options 2 or 3 or 4 will lead to generators being more likely to reduce (rather than increase) their output as a result. Therefore this proposed change would result in perverse outcomes to that intended.

Second, we believe that the approach outlined in options 2, or 3, or 4, will introduce a cross-subsidy. Currently the option fee is paid out by NGT per half hour to guarantee continued security of supply. If a half hour goes past without having to utilise the generation (and pay out a utilisation fee), then is it gone, and all network users have had the benefit of the 'insurance' that the holding of that standing reserve has provided. To then not charge for that half hour, but lump those charges into a future half hour when standing reserve is utilised, wrongly charges those network users in the future half hour.

Third, we believe that NGT have a duty of efficiency. Accordingly they are required to contract efficiently and they should charge out efficiently. This should mean NGT charging out in the same way that they contract. If the market was in charge of purchasing these standing reserve services, the market would contract and charge out as efficiently as possible. This proposed approach outlined in options 2, or 3, or 4, are a concocted method of charging out, which pays for a service over a period of time; i.e. a whole year; yet seeks to charge it over a much smaller period of time; i.e. certain half hours.

Fourth, as indicated in the statement made in the Tender Report, NGT recognise that there is a benefit in the current (option 1) contracting strategy, i.e. that they pay option fees to 'guarantee' standing reserve. It should not only be NGT who benefit from this strategy. If however NGT are concerned about security of supply, then they should contract for more standing reserve.

Fifth, the fact that NGT purchase this standing reserve over peaks, takes it out of the market, thereby already inflating the market price. To gear up these costs (as outlined in options 2, or 3, or 4) again over the peaks would be wholly non-cost reflective of the costs at the peak.

Sixth, if NGT is meeting its duty of efficiency, why is it buying standing reserve for periods when the service is not likely to be utilised? The standing reserve is either purchased, because it is likely to be used, or it is not needed, so should not be purchased.

Seventh, allocating the standing reserve option fees, based on historic utilisation, (as outlined in options 2, or 3, or 4) is wholly arbitrary - if this is 'preferred' then why does NGT not just contract for these periods only?

Eighth, allocating the standing reserve option fees, based on a 'per call off' approach is inefficient and discriminatory. As noted, under option 3, (in "Options for winter 03/04" listed on page 4 of the summary note) this method could result in more (or less) than the option payment being allocated into prices, so therefore leading to discrimination which is inefficient.

Ninth, NGT have not justified the statement in "Options for winter 03/04", that "the proposed process must better reflect balancing costs into the periods in which they are incurred than the current mechanism". NGT have not justified (a) why they have chosen this criteria, (b) why this is necessary or (c) why the current mechanism is not appropriate. We believe that options 2, or 3 or 4 will all result in a cross-subsidy situation arising, which does not currently exist.

Tenth, NGT have not justified the statement in "Options for winter 03/04", that "the purpose of this consultation is to consider whether any other options better reflect balancing costs". NGT have not justified (a) why this is necessary or (b) why the current mechanism is not appropriate.

Eleventh, the statement in "Options for winter 03/04" that "on the basis of the arguments set out above, we have concluded that the only option that we can progress for implementation for this coming winter is option (2)" is wrong. NGT has not put forward any arguments in support of this proposition. The consultation paper (in "Options for winter 03/04") outlines the four options NGT put forward, specifies the three criteria NGT have set for assessing each option and then considers each of the four options against the three criteria. Specifically, this section of the report states that:-

- 1) Clearly this satisfies the latter two criteria as it maintains the current process. The purpose of this consultation is to consider whether any other options better reflect balancing costs; [this is a statement not an argument for/or against] and
- 2) Processes can be developed to satisfy the latter two criteria. Again, whether this better reflects balancing costs is the subject of this consultation; [this is a statement not an argument for/or against]

As noted by NGT, both option 1 and option 2 "satisfy the latter two criteria". Therefore the essence of the argument should be which option better reflects balancing costs (which, as we note in our tenth point above, it is not clear why this was chosen as an assessment criteria). NGT has provided no reasoning or argument as to why any option (1 or 2 or 3 or 4) does, or does not, better reflect balancing costs. Given this NGT cannot "concluded that the only option that we can progress for implementation for this coming winter is option (2)" because option 1 can also be progressed for implementation this winter.

For the eleven reasons we have outlined above, we conclude that option 1 better reflects the cost of balancing, can be implemented for this winter and should therefore be adopted as the mechanism for the BSAD Methodology Statement to use for the treatment of standing reserve option fees.

Therefore, for the avoidance of doubt, of the four "Options for winter 03/04" listed in the summary note, we believe that option 1 (as now) is the most efficient mechanism for the BSAD Methodology Statement to use for the treatment of standing reserve option fees.

Q3 Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale

Q4 Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rational

The distorting effect on the market of the Transmission Company determining the expected utilisation of Standing Reserve. If its utilisation can be determined in advance, why doesn't the Transmission Company contract for this specific period?

Q5 Are there any further comments on P136 that you wish to make?

None at this time.

Q6 Are there any further comments on P137 that you wish to make?

None at this time.

Regards

Garth Graham
Scottish and Southern Energy plc

P136-P137_ASS1_013 – British Gas Trading

Respondent:	Mark Manley
No. of BSC Parties Represented	
BSC Parties Represented	British Gas Trading (BGT)
No. of Non BSC Parties Represented	
Non BSC Parties represented	
Role of Respondent	

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	<p>BGT do not believe this modification will better facilitate any of the applicable BSC Objectives.</p> <p>The significant risks associated with marginal prices will result in parties going long and holding their own reserve. It is inefficient if all Parties hold their own capacity, as an inappropriately high level of reserve is likely to result. Therefore BGT do not believe the modification will better facilitate the efficient, economic and co-ordinated operation by the licensee of the licensee's transmission system (Applicable BSC Objective B).</p> <p>BGT also believe this modification will be to the detriment of Applicable BSC Objective (C), as it will have an adverse effect on competition in the generation and supply of electricity. Whilst</p>

Q	Question	Response	Rationale
			<p>BGT note the assertion of the proposer that marginal pricing does not necessarily mean that imbalance prices will be £99,999MWh, imbalance prices at this level could occur under a marginal regime. This introduces an unmanageable risk for BSC Parties and it could also be ruinous. If a generator trips during the settlement period in which the imbalance price reaches this level it could bankrupt the generator concerned. Equally from a supplier perspective demand forecasts contain errors. Even a good demand forecast may contain an error of 4 to 5 percent. BGT believe it is inequitable to penalise a Party so heavily on the basis of an incorrect demand forecast. If Suppliers' costs increase because of marginal pricing then customers are also likely to be adversely affected.</p> <p>The current market structure creates a period after gate closure when a Party is unable to undertake any remedial actions. If conditions change after Gate Closure there is nothing a BSC Party can do to mitigate those changes. Whilst BGT recognises this period exists under the current mechanism the imbalance prices are likely to be much more extreme under a marginal regime. A marginal-pricing regime means Parties will face potentially penal and unmanageable risks.</p> <p>The NETA structure was designed around weighted average imbalance prices. It is inappropriate to make such a fundamental change without fully reviewing which other design aspects may need to be modified. One example of this is the timing of gate closure. If marginal pricing were implemented then BGT would expect as a minimum that Gate Closure would need to be reduced to the start of each respective Settlement Period. The rationale for this is it would mean Parties would only be exposed to one Settlement Period in which they were not able to respond to changing market conditions.</p> <p>BGT also believes implementing marginal pricing will create a barrier to entry. Not only will the risks associated with entry to the market be high but also the financial cost of entering the market will be significant. This will be particularly relevant for commissioning power stations,</p>

Q	Question	Response	Rationale
			<p>which are much more likely to trip during their commissioning phase.</p> <p>The BSC places obligations on Parties to post appropriate levels of credit cover. The current credit arrangements use imbalance prices for the second stage of the calculation. Marginal imbalance prices are likely to create higher imbalance prices, which in turn will need to be reflected in the amount of credit cover lodged. The additional credit cover Parties will need to lodge will impact on potentially new and existing entrants in the market. This is especially true for small players.</p>
2.	<p>Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives?</p> <p>Please give rationale and state which objective(s)</p>	No	As above.
3.	<p>Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure?</p> <p>Please give rationale</p>	Yes	<p>Many of the responses to the consultation for Modification Proposal P135 recognised the significant impacts a marginal pricing regime could have on the credit cover arrangements. BGT believe the impact of marginal prices on the credit cover arrangement should be considered as part of the assessment process for this modification.</p> <p>If a marginal pricing regime is implemented then there is likely to be a significant impact on the amount of RCRC created. It maybe appropriate for the group to consider the implications of the increasing RCRC and the best way of distributing the surplus created.</p> <p>Marginal pricing is likely to have an adverse impact on unpredictable generation such as wind. Introducing a pricing regime that adversely effects renewable generation appears to be directly contrary to government policy on renewables.</p>
4	Does P137 raise any issues that	Yes	As above.

Q	Question	Response	Rationale
	<p>you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale</p>		
5	<p>Are there any further comments on P136 that you wish to make?</p>	<p>Yes</p>	<p>BGT note within the justification for Modification Proposal P136 the suggestion that P136 will incentivise Parties to forward trade to mitigate the risk of imbalance. BGT believe sufficient incentives already exist with imbalance prices in excess of £300/MWh being regularly posted during this summer. BGT do not agree with the justification of the proposer that the existing imbalance charges do not create appropriate incentives.</p> <p>Within the consultation document there are a number of key issues. One of these is the possibility for a non-delivered acceptance to set the imbalance price. Under this partial marginal pricing modification the effect of tagging may result in a non-delivered acceptance setting the energy imbalance price. BGT do not believe it is appropriate for a non-delivered acceptance to set the imbalance price for parties out of balance, as this does not reflect the cost of energy balancing.</p> <p>Under a marginal regime it is essential that prompt price reporting is available to all BSC Parties, equally important is the derivation of the imbalance price. BGT believe it is essential that NIV tagging be undertaken correctly and in a prompt manner especially under a marginal regime. Within the modification group there has been some discussion on the treatment of NGC system to system trades and when they are reported. The volume of these trades could have a significant effect on the outturn price and BGT believe it is essential that these feature in the real time calculation of the imbalance price. This is a fundamental issue to allow accurate real time reporting of imbalance charges.</p> <p>BGT has concerns that the implementation of a marginal pricing methodology may encourage</p>

Q	Question	Response	Rationale
			<p>Parties to self-balance. At the start of NETA when imbalance prices were particularly extreme it was suggested that some Parties were undertaking self-balancing actions. Due to the risks Parties may face in certain settlement periods this may encourage Parties to undertake self-balancing actions.</p>
6	<p>Are there any further comments on P137 that you wish to make?</p>	<p>Yes</p>	<p>As above.</p> <p>However BGT is supportive of the developments within the group to more accurately reflect the incorporation of option fees in the imbalance prices. BGT believe the new methodology being developed to target the settlement periods when the contracts are called will provide more representative cash out prices.</p> <p>BGT is also supportive of the suggested amendments to the tagging methodology to include an undo tagging action.</p> <p>Whilst BGT are not supportive of a move to a marginal pricing regime, BGT do recognise some of the defects identified in P137 in terms of the current treatment of tagging, the treatment of option fees and non BM Unit standing reserve contracts. BGT believe it would be much more appropriate to be addressing these issues rather than fundamentally changing the underlying pricing mechanism. BGT believe resolution of this issue with increased transparency of NGC actions would provide both a materiality and information signal to the industry. The combination of which would allow BSC Parties to be able to respond rather than just imposing substantial and arbitrary imbalance prices.</p>

P136-P137_ASS1_014 – InterGen UK Ltd

Respondent:	<i>Chris Ridgway</i>
No. of BSC Parties Represented	<i>4</i>
BSC Parties Represented	<i>CECL, IETS, RPCL, SPAL</i>
No. of Non BSC Parties Represented	<i>1</i>
Non BSC Parties represented	<i>InterGen (UK) Ltd</i>
Role of Respondent	<i>Generator</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	<p>The proposer claims that P136 "will increase the level of competition by encouraging Parties to trade ahead of Gate Closure" and hence facilitate Applicable BSC Objective c).</p> <p>In reality, the penal SBP's which would arise as a result of P136 are more likely to encourage generators to withhold capacity, particularly at times of system stress.</p> <p>The current spread between SBP and SSP during periods of system stress already provides more than adequate incentive on Parties to balance their position where this is within their control. Higher SBP's will simply increase the penalty on generators who trip rather than encourage the to forward trade.</p> <p>There is already a substantial smearing of imbalance cost over / under-recovery through RCRC indicating that costs are not correctly allocated to those that cause them under the current arrangements. Marginal pricing simply exacerbates this situation.</p> <p>For the above reasons we do not believe that P136 better facilitates any applicable BSC Objective.</p>

Q	Question	Response	Rationale
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	As P137 is essentially a refinement of P136 the same argument as Q1 applies.
3.	Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	Any mod which seeks to increase SBP increases the risk that a Party's credit cover will be insufficient to cover its Imbalance Charges.
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	As per Q3.
5.	Are there any further comments on P136 that you wish to make?	Yes	<p>The current methodology of determining system prices was implemented on 25th Feb 2003 following Ofgem's approval of Mod P78. The first and third bullet points in the "Issue or Defect" section of the P78 Mod Proposal were that "SBP remains unpredictable with a high mean and spread" and "the resultant high levels of SBP are driving the market long". P136 will result in a higher, more volatile SBP, thus reintroducing two of the defects Approved Mod P78 sought to correct.</p> <p>The current price determination methodology has yet to be tested throughout a Winter period. However, it has recently been demonstrated that it yields volatile prices during periods of tighter system margin. The knowledge that such prices can arise already provides</p>

Q	Question	Response	Rationale
			sufficient incentive for parties to balance where they are able to do so. Mods should not be applied on a seasonal basis and P78 should be allowed to run unchanged throughout the forthcoming Winter.
6.	Are there any further comments on P137 that you wish to make?	Yes	As per Q5.

P136-P137_ASS1_015 – Teesside Power Ltd

Respondent:	<i>Christine McKie</i>
No. of BSC Parties Represented	<i>1</i>
BSC Parties Represented	<i>Teesside Power Limited</i>
No. of Non BSC Parties Represented	<i>0</i>
Non BSC Parties represented	<i>N/A</i>
Role of Respondent	<i>Generator</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	No	See Note 1. below
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives?	No	See Note 1. below

Q	Question	Response	Rationale
	Please give rationale and state which objective(s)		
3.	Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	See Note 2. below
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	See Note 2. below
5.	Are there any further comments on P136 that you wish to make?	Yes	See Note 3. below
6.	Are there any further comments on P137 that you wish to make?	Yes	See Note 3. below

General

Please note that these are preliminary comments on the merits of the modification proposals P136 & P137. Whilst TPL welcomes the initiatives to improve what is generally considered as a flawed market pricing mechanism under NETA, TPL is concerned that these proposals, as they currently are drafted, have the potential for introducing significant risks to the generating companies, particularly those within the IPP sector, which will have a detrimental effect on competition.

Note 1.

TPL's preliminary view on this proposed modification is that it will not better meet any Applicable BSC Objective: the main reasons are:
it fails to take into account the fact that NGC may make decisions on behalf of consumers which are inconsistent with the action which would have been taken by customers, in the event that they had been aware of the cost of meeting their demand
given that the anticipated impact of this modification will be higher imbalance cash-out prices, particularly at times when accepted offer prices are likely to be high, it makes the disconnect between NGC's actions and customers even more significant

it is possible that offers accepted to manage system stability will result in high imbalance prices which are inconsistent with the overall supply-demand balance
reduce competition due to increased risk profile for single site generators

Note 2.

TPL's view is that the following need to be taken in to account:

what is likely to be the impact of the modification on BSC participants' behaviour as regards the bid and offer prices they submit

to what extent does will the modification increases the efficiency of a BSC participant's "bid/offer" process: i.e. does it provide market participants with a better view of the likely supply-demand balance prior to bids and offers being made

the requirement to reflect the fact that end customers, if exposed directly to imbalance prices, would choose to reduce demand at times of high prices: we suggest that consideration should be given in determining the value, which is attributed to different customer groups, which reflects the price at which they would choose to reduce demand if they were directly exposed to such a price: consideration should be given to the number of such "values" required for an efficient solution and the different options available to determine what these values are

should all participants in the balancing mechanism be paid/pay at SBP or SSP for accepted offers and bids respectively, rather than simply imbalances being charged at SBP and SSP

Note 3.

We believe that the Modification Group should give consideration as to what data should be analysed and presented to BSC participants to assist in their assessment of the modification proposal. In particular, we suggest that a full analysis of aggregate bid/offer behaviour over the past [twelve months] should be undertaken.

P136-P137_ASS1_016 – Entergy-Koch Trading Europe Ltd (late response)

Respondent:	<i>Adam Cooper</i>
No. of BSC Parties Represented	<i>1</i>
BSC Parties Represented	<i>Entergy-Koch Trading Limited</i>
No. of Non BSC Parties Represented	
Non BSC Parties represented	
Role of Respondent	<i>Trader</i>

Q	Question	Response	Rationale
1.	Do you believe Proposed Modification P136 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	Yes	The development of better pricing signals should provide more information to the forward markets, and encourages the efficient allocation of resources. This will promote increased security of supply and competition between BSC parties.
2.	Do you believe Proposed Modification P137 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state which objective(s)	Yes	As above, but as the solution is more complete it should be more effective.
3.	Does P136 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	P136 appears a more partial solution. The assessment should consider whether there is some risk that a partial solution may introduce more distortions than it is attempting to remove.
4.	Does P137 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	Yes	This proposal attempts to cover a range of constraints in the current price discovery process. In this respect it is more robust than P136, but there are possibly other issues, such as NGT's market behaviour that are relevant to price discovery, although these are outside of the scope of the BSC.

Q	Question	Response	Rationale
5.	Are there any further comments on P136 that you wish to make?	No	
6.	Are there any further comments on P137 that you wish to make?	No	

P136-P137_ASS1_017 – Aquila Networks (late response)

Please find that there is no impact to Aquila Networks Plc systems and/or processes.

regards
Rachael Gardener

Deregulation Control Group &
Distribution Support Office
AQUILA NETWORKS