P415 Workgroup Meeting 9 Summary

The P415 Workgroup met on 1 February 2022 to discuss the hypothesised P415 balancing market benefit to feed into the CBA and conduct an end-to-end review of the Proposer's P415 Solution to date, noting any differing opinions on elements of the P415 proposal.

Next Steps

Due to time constraints, it was not possible to gather Workgroup views on all elements of the P415 solution, so it will be necessary to revisit the imbalance settlement and reporting requirements in the next session.

The Workgroup will reconvene on 22 February 2022 to consider the methodology and assumptions for the P415 CBA and provide views on the remaining elements of the P415 solution.

Understanding the Hypothesised P415 Balancing Market Benefit

CEPA sought Workgroup views on the potential Balancing Market benefit that could be expected under P415 for the purposes of feeding this information into the CBA.

CEPA had identified two possible mechanisms:

1) Positive externalities for other markets, including the balancing market, caused by additional revenue opportunities from increased volumes of aggregation in the wholesale market.
2) Net Imbalance Volume (NIV) reduction. This assumes that additional volume of flexible aggregation in the wholesale market will generally work in the opposite direction to the imbalance position. This mechanism assumes that this activity will tend to reduce the NIV relative to the counterfactual in which aggregation is not participating.

The Workgroup were invited to answer which of these hypothesised mechanisms they agree with and which they would expect to be the most significant. CEPA clarified that this would be modelled by reduction in BM price if possible, but certainly by modelling additional volume.

Some Workgroup members felt that positive externalities seemed to incur the most significant effect. The Proposer noted that once customers are 'over the hurdle' of participating in one market, it is relatively straightforward to encourage participation in the other markets and that P415 provides a (currently missing) route for lower short-run marginal costs and more frequently dispatchable flexibility which could lead to greater amounts of flexibility from customers who are already participating.

One member cautioned against using NIV to represent increased trading, recalling work with Ofgem and Elexon several years ago that suggested NIV is generally driven by System Operator rather than wholesale actions. The member wondered whether gross party imbalance volumes could be a better metric, but agreed to try to find and share this work with Elexon to ensure it could be considered.

P415 End to End Review

Elexon took the Workgroup through the end-to-end Proposer’s solution as reflected in the draft Solution Summary document that was shared with Workgroup members ahead of the meeting.

Supplier Compensation Volumes

The group were invited to provide their views on whether they agreed with the Proposer’s view regarding Supplier Compensation Volumes - that Suppliers should be compensated for VLP activity at a registered site.

In the Proposer's solution Suppliers shall only be compensated for Deviation Volumes allocated to VLP Wholesale Market trades.

The group had previously heard Elexon’s legal opinion that the scope of P415 is not sufficient to introduce Supplier compensation in the BM, and therefore another Modification would need to be raised to cover this element.

Acknowledging this constraint, under the Proposer’s solution the Supplier shall only be compensated for Wholesale Market volumes and so settlement will need to identify for each SBMU what volumes are to be allocated as balancing volumes and what volumes are to be allocated as wholesale market volumes.

Regarding the allocation of volumes, one member suggested that it could be simpler to allocate non-delivery first to the WM (which is planned ahead of time) then to the BM (which is closer to real-time). Elexon explained that this approach had been discussed previously by the Workgroup but rejected as they didn’t want to disaggregate to BMU level. As National Grid would have to know what VLPs intend to do in the WM to balance the system effectively, Elexon would have to know WM contributions at the BMU level which would undermine the VLP's aggregation.

One member queried whether it would be possible to perform BM dispatches at the account level, but National Grid confirmed that this would not be acceptable -their requirement is that it has to be at GSP level, as they are concerned about where this energy would be coming from to flow onto the total system. The member stated that a zonal WM (as opposed to the single zone WM in GB currently) would be beneficial for better geographical understanding and other members were sympathetic but noted this would be a major change to the market and a wider discussion that is not in the scope of P415.

Workgroup views

From the Workgroup voting members and observers in attendance for this meeting, respondents either agreed with the Proposer (9/11) or stated they were still unsure (2/11).

One comment was received stating that “Correction and compensation should go together. Elexon made it clear there is a legal constraint that P415 is only about WM, and cannot tackle BM.” This reflected the general view that it would be simpler and appropriate for Supplier compensation to extend to the BM, but acknowledged the aforementioned constraints around including this in the scope of P415.

Supplier Compensation Liability

Proposer's views

The group were invited to provide their views on whether they agreed with the Proposer regarding Supplier Compensation Liability - that VLPs should be liable to pay impacted Supplier compensation because the VLP directly benefits from activity at the Supplier's site.

The group discussed the wording used to justify this statement. One member questioned the use of 'directly benefiting' and wondered why the Supplier is mentioned at all, with Elexon explaining that, because of the VLP's actions, the supplier can't sell the energy that they would have sourced. There was disagreement over the conceptual framing of why the Supplier buys and what the VLP directly benefits from. Following discussion "VLPs should be liable to pay impacted Supplier compensation because the VLP causes activities at the site which causes the Supplier's position to be corrected" was felt to be a useful way to frame the dynamic.

Alternate views

An alternate view, articulated in previous meetings, was also presented - that all Suppliers in the market (mutualised by market share) should be liable to pay for impacted Suppliers compensation.

Previous arguments to justify this position state that all Suppliers benefit from lower sourcing costs due to flexibility in the WM (noting that practically flexibility will only be chosen when at a better price point than traditional generation and so both lowers the system demand and the generation costs).

One member preferred the wording "…liable to pay for *adjusted* Suppliers compensation…" rather than "*impacted*".

This approach would not present a barrier to VLPs (as they would have to pay compensation) but arguably could be viewed as a Supplier levy and an additional cost to pass on to the end consumers, therefore presenting a potential barrier to Supplier market entry.

One member questioned this, noting that it prompted the question of whether Suppliers would have more benefit than cost under P415 – expecting that they would all pass on the net cost (or more likely net benefit in his view) to consumers and so mutualising the cost across all Suppliers seemed more fair.

Workgroup views

From the Workgroup voting members and observers in attendance for this meeting, a majority of respondents did not agree with the Proposer and supported the alternate view (6/10) while a minority agreed with the Proposer (3/10) or stated they were still unsure (1/10).

Comments received
Most important point is that the CBA studies both scenario.

The Proposer's approach (VLP liability) gives the correct economic signals to all participants and avoids suppliers having any cause for complaint.
Support the alternative solution. The proposer's solution would create a barrier. Note that both solution ensure suppliers are protected.; Supplier would be compensated in both solutions, but liability to pay compensation for correction being on VLP would make it an unfair competition with generation.; VLP would have to bear their own cost plus a (generation) sourcing cost, thus making it impossible to compete
I agree with the Proposer. P415 won't be accepted by the industry if it exacerbates the lack of supplier compensation in P344.
I support the alternate view. The alternate view ensures that it makes economic sense to invest to unlock large volumes of DSR. Conversely, the proposer's view creates an artificial barrier to entry by charging the compensation to VLP.
The alternate view guarantees that no supplier is negatively impacted by VLPs, especially smaller suppliers who have a higher exposure to day-ahead prices.
Disagree with the proposer because I am concerned about barriers to entry. I find the alternative more convincing and consistent with the net benefits principle adopted in the US. But I think the important point is that the CBA should study both.
agree with the alternative view, do not agree with the proposer's view

Several comments centred around the Proposer's preferred solution creating barriers to entry for VLPs. Noting the slight majority in favour of mutualised liability across all Suppliers, the Proposer maintained that he is still supportive of the original proposal (VLP liability) as the method which is his view provides the correct incentives, maintains a level playing field for VLPs while avoiding a risk that industry would not accept P415 or give it a reason to "shoot down" this important Modification.

P415 Trading Charges

Each Trading Party is liable to pay or receive Trading Charges for each Settlement Day and these charges are calculated in relation to Imbalance Settlement and Balancing Mechanism activity. Under P415, new Trading Charges will be necessary, proposed as using a compensation volume per period multiplied by a price (compensation reference price) to get the amount per period.

In this manner, the Proposer's preferred solution for Trading Charges uses the WM proportion of the VLPs (how much they put forward) and then separately work out how much the Supplier is impacted, and then pay them appropriately based on the volumes that we calculated, in the same manner as most BSC Trading Charges.

Workgroup views

From the Workgroup voting members and observers in attendance for this meeting, a majority of respondents did not agree with how the Proposer's solution implements new Trading Charges (5/10) while a minority agreed with the Proposer (4/10) or stated they were still unsure (1/10).

It was noted that this might be a misunderstanding, as this was discussed immediately after the compensation liability question. Elexon wished to understand whether some respondents were disagreeing with the principle that the VLP pays compensation rather than the formula it - if this was not the case then this would be disagreeing with basic BSC Trading Charge methodology, as they are the same and there are very limited ways to "add it up". One member clarified, as the slide suggested VLP liability when discussed Trading Charges, it was likely that the two issues had become mixed.

Supplier Compensation Price

Elexon summarised the different options for prices to apply to Supplier compensation and previous arguments for and against each of these.

The retail price reflects commercial arrangements Suppliers have with their customers and would ensure the Supplier is completely unaffected by any activity at site caused by VLP – but would be very complex and lead to a prohibitively expensive solution.

The Imbalance price would be simple and cheap with no supplier adjustment needed at all. However the Imbalance Price is designed as a market signal to self-balance (or not) an imbalance position and therefore is not meant to be reflective of the real price of energy, also falling foul of the principle that Supplier could benefit or suffer detriment from its application.

For the Spot market (day ahead) price – arguments in its favour stated that this would be the £ if the Supplier traded away the imbalance created by VLP but arguments against stated that this is not representative of Supplier incurred costs (where energy is usually bought days or months ahead) and the Supplier could incur benefit or suffer detriment.

The Supplier sourcing cost is the Proposer's preferred compensation price, arguing that it is a cost effective solution that would ensure Supplier would not benefit/suffer detriment from VLP activity, however recognising that it adds complexity and a sourcing cost methodology would need to developed and implemented.

It was agreed by the group that there is no universally right answer to the question of which price is best, and discussions focused on trying to make it as fair as possible for all players in the market.

One member advocated for compensating at the day ahead price (on the assumption that P415 should compensate for the correction imposed on Suppliers rather than the raw cost of buying energy) while the Proposer believed that compensating at Spot price would lead to overcompensation for most Suppliers and it would be fairer to use a long term average Supplier sourcing cost formula (on the basis that Suppliers buy most energy further ahead than day ahead).

Workgroup views

The group were invited to provide their views on which price they thought compensation should be paid at, at this stage.

From the Workgroup voting members and observers in attendance for this meeting, a majority of respondents preferred the spot market cost (6/10) while a minority support Supplier sourcing cost (4/10)

Comments received
Supplier sourcing cost is not all that complex (it's a simple formula), but should (a) be much less wrong (i.e. closer to neutral) from the supplier's perspective, and (b) would avoid creating a barrier to participation (and in fact give the correct economic signal) if sourced from VLP rather than socialised.

To protect suppliers, the spot market price is safer, and ensures fair treatment of all suppliers
It seems odd to assume that suppliers' costs are best reflected by the spot price
The wholesale market price is the best option to reflect the cost incurred by the supplier.
Sourcing Costs would add a layer of complexity and does not represent the cost incurred at the time the service is used.
Does it make sense to ask what answer would apply regardless if one did not know who was going to pay the compensation?

There was general agreement that it is not possible separate out the “what cost” and “who pays” questions entirely, as some combinations just don’t work. For example, if a VLP pays Spot price compensation, there would no value to be had from the day ahead market as any money they would receive would then be paid out in compensation.

Agreeing that it is better to reduce variance in the CBA where there is no benefit to including impractical combinations, the group agreed that the CBA should consider the scenario of “if the VLP pays compensation, then it compensates at the Sourcing Cost” but not the scenario where the VLP pays Spot price compensation.

The group considered whether there was benefit to modelling both Sourcing Cost and Spot Price for the scenario where the Supplier pays mutualised compensation and felt that it would be worth looking at both price variants within this solution.

Clarifications on process for raising Alternative Modifications

Elexon provided some clarifications to the group on the process and governance around raising an Alternative Modification. This process requires a majority of voting Workgroup members (those authorised to vote and who have attended a minimum of 50% of Workgroup meetings) to agree that an alternate proposal better achieves the BSC Objectives than the Proposed Solution.

In theory, an Alternative Modification can be raised at any point in the Assessment process, however the Workgroup agree that this is best considered at a point in time after the results of the CBA have been returned and understood by the group.

One member made the valuable point that, while the BSC is limited to one Alternative Solution, the Workgroup are able to seek views on multiple alternatives in the Consultation document.