

Modification proposal:	Balancing and Settlement Code (BSC) P443: To cap NGESO Interconnector Trades at the Value of Lost Load (VoLL)		
Decision:	The Authority ¹ has decided to reject this modification proposal ²		
Target audience:	National Grid Electricity System Operator (NGESO), Parties to the BSC, the BSC Panel and other interested parties		
Date of publication:	20 October 2023	Implementation date:	N/A

Background

National Grid Electricity System Operator (NGESO or the ESO) is responsible for balancing supply and demand across the GB electricity system. The primary tool it uses to do this is the Balancing Mechanism (BM). In the BM, market participants submit *bids* to decrease electricity output or increase electricity consumption and *offers* to increase electricity output or decrease electricity consumption. In addition to the BM, the ESO has a range of other options to keep the system in balance and keep the system frequency stable. These options include trading with other system operators (SO) or market participants via interconnectors (high voltage cables which link the GB electricity network to the electricity networks of other countries).

NGESO typically takes the most competitively priced available actions, however operational and locational factors can sometimes result in more expensive actions being taken in order to solve a specific network issue. The order in which the ESO takes actions to balance the system is set out in its *order of actions*³, with actions classified as *everyday*, *enhanced* and *emergency* based on how far along the order of actions they sit.

¹ References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day to day work. This decision is made by or on behalf of GEMA.

² This document is notice of the reasons for this decision as required by section 49A of the Electricity Act 1989.

³ <https://www.nationalgrideso.com/document/270586/download>

Trades via interconnectors with market participants or other system operators may take place as an everyday action. These are undertaken in cost order and in competition with available BM bids and offers. However, if the system requires additional power that cannot be provided via everyday actions, NGENSO may request Emergency Assistance (EA), an enhanced action, where other SOs exchange energy via interconnectors, or interconnectors may receive an Emergency Instruction (EI), an emergency action, to alter their flows.

The Value of Lost Load (VoLL) is an assessment of the value that electricity consumers attribute to maintaining security of supply. There is no single, unique VoLL across the UK energy system. Within the BSC, VoLL is currently administratively set at £6,000/MWh.⁴ VoLL does not act as a cap for the ESO's balancing actions, but this value of £6,000/MWh is included in the Imbalance Price calculation to represent the cost of any disconnections and voltage reduction instructed by the SO.

In July 2022, system constraints in the South East led the ESO to accept interconnector trades to maintain GB system security. On one occasion, the price of some of these actions was extremely high (up to £9,500/MWh) due to scarcity on the continent driven by the unavailability of the French nuclear fleet.

The modification proposal

P443 was raised by Saltend Cogeneration Company Ltd on 17 August 2022. The following day, at an urgent BSC Panel meeting, the BSC Panel requested that Ofgem treat P443 as an Urgent Modification Proposal. On 25 August 2022, we issued a decision letter⁵ to the BSC Panel rejecting urgency for P443. The proposer considered the original proposal to facilitate objectives (b), (c) and (f) of the BSC.

This original proposal (considered but not formally raised by the BSC working group) suggested capping all buy actions taken over interconnectors (including trades with interconnector users, SO-SO trades, EA and EI) at VoLL and preventing NGENSO from taking interconnector trades above this cap, with the intention that this would limit the exposure of

⁴ [BSC Consolidated - Elexon Digital BSC](#) (Section T: Settlements and Trading Charges 1.12.2)

⁵ [P443 - Decision on urgency | Ofgem](#)

GB parties to tight margins across European energy markets, limit the impact of high prices on consumers and oblige NGESO to pursue other means of balancing the system.

The final proposal submitted by the BSC Workgroup ('the proposal') suggests instead that ESO actions taken over interconnectors and priced above VoLL would not be prohibited, but the price of these actions used in the imbalance price calculation would be capped at VoLL by Elexon (as opposed to NGESO).

The Workgroup submitted the final proposal in place of the original proposal based on advice that the changes proposed in the original proposal did not sit within the intended scope of the BSC, had potential impacts on the NGESO's licence and set a much higher bar for evidence to justify the change. While the proposer expressed that they would still prefer a solution that prevents NGESO making interconnector trades above VoLL, they accepted this feedback. The proposer viewed the revised proposal to facilitate objectives (b) and (c) of the BSC.

The Workgroup also considered a solution that would cap all actions to VoLL in the imbalance price calculation (not just interconnector trades), which was seen as potentially less discriminatory, but would also effectively act as a cap on wholesale prices, as market participants would be likely to go into cash-out short at a price up to VoLL rather than buying in the wholesale market above it. Given the strong feedback in the Assessment Consultation, the Workgroup did not bring this solution forward as a formal alternative.

BSC Panel recommendation

At the BSC Panel meeting on 13 April 2023, the BSC Panel agreed by majority that the proposal does not better facilitate BSC objectives (c), finding that it does not better promote competition within the electricity market. The panel also agreed by majority that the proposal does not better facilitate BSC objective (d) as they do not believe it promotes efficiency within the BSC arrangements due to the points raised by the Workgroup (that it would impact the marginal price and that it would not reflect the true cost of energy at that time). The panel agreed unanimously that the proposal does not better facilitate BSC objective (e) in that it was discriminatory to focus on interconnectors and that it may not satisfy the Trade and

Cooperation Agreement's requirement for free price formation. The Panel recommended by majority that the proposal be rejected.

Following the Report Phase Consultation, the Panel considered the P443 Draft Modification Report at its meeting on 8 June 2023 and agreed that P443 does not better facilitate Applicable BSC Objectives (c), (d) and (e), for the reasons previously given. The Panel therefore unanimously recommended that P443 is not better than the current baseline and should therefore be rejected.

Our decision

We have considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 12 June 2023 and have taken into account the responses to the industry consultation on the modification which are included in the Final Report.⁶ We have concluded that the implementation of the modification proposal will not better facilitate the achievement of the applicable BSC objectives.

Reasons for our decision

Following review of the FMR, we consider this modification will not better facilitate BSC Objectives (b), (c), (d) or (e).

(b) the efficient, economic and co-ordinated operation of the National Electricity Transmission System

We believe that the proposed solution does not improve upon the BSC obligations specifically related to BSC Objective (b). In capping the imbalance price, the proposed solution would suppress efficient imbalance price signals, which could weaken system security during periods of scarcity. The imbalance price (and market expectations of the imbalance price) provides an important signal to compel parties to balance their position and take all reasonable steps to make generation capacity available during times of scarcity. Capping the imbalance price

⁶ [P443 'To Cap NGESO Interconnector Trades' - Elexon BSC](#)

would weaken this important signal and result in market prices that were less reflective of system conditions.

(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

We believe that the proposed solution does not improve upon the BSC obligations specifically related to BSC Objective (c). In situations where the proposed solution would lead to the imbalance price being capped, this would suppress efficient price signals and be detrimental for effective competition. For example, when the system is short and requires additional electricity to balance it, the proposed solution of a cap on the System Buy Price would create a perverse incentive by lessening the penalty for parties with a short position who contributed to the system imbalance (by under-generating or over-consuming compared to their contracted volume), while lessening the reward for those parties with a long position who acted to minimise the system imbalance (by over-generating or under-consuming compared to their contracted volume).

(d) promoting efficiency in the implementation and administration of the balancing and settlement arrangements

We believe that the proposed solution does not improve on the BSC obligations specifically related to BSC Objective (d). As mentioned in (c) above, we see a clear perverse incentive as a result of applying the proposed price cap, but we do not see sufficient evidence provided to justify the position that the proposed price cap would result in a significant reduction in defaulting parties or that the positive impacts from this potential reduction in defaulting parties would exceed the negative impacts of dampening price signals and the general increase in complexity required to enact the solution.

(e) compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency

We believe that the proposed solution does not improve on the BSC obligations specifically related to BSC Objective (e). Through suppressing efficient price signals the proposed solution may not be aligned with the Electricity Balancing Guideline (EBGL) in respect of the objectives for fostering effective competition, non-discrimination and transparency in balancing markets and facilitating the efficient and consistent functioning of national day ahead, intraday and balancing markets. Moreover, the proposed solution may not satisfy the Trade and Cooperation Agreement's requirement for free price formation.

Decision notice

In accordance with Standard Condition C3 of the Transmission Licence, the Authority hereby directs that modification proposal BSC P443: *To Cap NGESO Interconnector Trades at the Value of Lost Load (VoLL)* should not be made.

Andrew Macdonell

Senior Policy Manager – Energy Systems Management and Security

Signed on behalf of the Authority and authorised for that purpose.