

Alternative CAP Review Process

BSC Panel

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Summary **Elxon are proposing an addition to the Credit Assessment Price Review Process Guidance Document in light of volatile electricity market prices. This change aims to allow an alternative review process to be used temporarily in volatile market conditions, that will give more flexibility to the Credit Committee to set a CAP faster.**

1. Background

- 1.1 The Credit Assessment Price (CAP) Review Process is described in the [CAP guidance document](#) and briefly in BSC Section M paragraph 1.4. The guidance document is owned by the BSC Panel and Panel approval is required for material changes to the guidance. It contains the detailed information on the mechanism for reviewing, consulting on and setting the CAP.
- 1.2 The current mechanism has been triggering a review to increase the CAP every few weeks since April 2021 in line with forward Market Prices. The most recent proposed CAP of £259/MWh is more than double the maximum CAP prior to 2021, which was £108/MWh and was set in 2008 during the market instability caused by the financial crash.
- 1.3 The current arrangements in the CAP Review Process are that Elxon will issue a consultation for 5 Working Days (WDs) for a new CAP. Once confirmed and notified to industry, it must be implemented after a minimum of 15 WDs. This means that in a volatile and changing market, the CAP can be out of date before it is implemented with large increases between CAP values.
- 1.4 BSC Section M paragraph 1.4 states that a consultation is required before notifying Parties of a new CAP, and that the CAP shall be effective no earlier than the 10th business day following the date of notification. To change either of these conditions, a BSC Modification would be required. A BSC Modification is not required for changes to the CAP Review Process guidance document to reduce timescales to these minimums.
- 1.5 A large jump in the CAP may cause cash flow issues for some BSC Parties. The most recent proposed CAP of £259/MWh would be a jump of £75/MWh from the previously notified value of £184/MWh due to be implemented on 21 October 2021. Once in effect, some BSC Parties may be asked to lodge a large amount additional Credit Cover at short notice or face the Credit Default consequences. Further, where market conditions result in the prices falling, CAP needs to respond as quickly as possible to avoid unnecessary excess credit cover demands on BSC Parties.
- 1.6 The CAP is based on forward market price to be used as a proxy for future System Prices, effective when the new CAP is live. The current forward market Prices are changing rapidly and creating significant step changes in the recommended CAP. In the current market conditions and future scenarios, this may not be a suitable proxy for how System Prices will out turn.
- 1.7 Three consultation responses to the two most recent CAP review consultations have disagreed with the proposed values set by current CAP calculation mechanism. They have raised concerns over the increased

credit burdens that an increased CAP may mean for market participants. Given these responses, and recent market trends, it may also not be suitable to use the current philosophy to set a CAP that works in the interests of the whole market.

2. Proposed alternative mechanism

- 2.1 In conditions where volatile prices are causing a significant number of CAP breaches or large changes in CAP, the existing CAP review mechanism may be paused if the Credit Committee request the move to an alternative process. Where a fast market situation might be characterised by three or more consecutive CAP breaches or by change in CAP value of more than £20/MWh. There are approximately five periods since 2008 that might be classed as fast market scenarios under this characterisation.
- 2.2 We are proposing that during these temporary periods an alternative process is used so that:
- The CAP can be set faster;
 - More control is given to the Credit Committee to determine a fair and appropriate price;
 - The CAP set can be representative of recent System Prices rather than just forward market prices; and
 - The guidance will allow deviation from the normal process of setting the CAP based on market prices if deemed appropriate.
- 2.3 For the proposed mechanism, the Credit Committee would propose a new CAP every two weeks. In setting a CAP value, the Credit Committee would consider System Prices from the last two weeks, any other relevant sources of information and recent consultation responses. The forward market prices would also be considered, but would not solely be used in setting a CAP.
- 2.4 A consultation is required under the BSC before notifying industry of the new CAP, however the time to consult is not specified. Given the current market climate, we propose shortening the consultation period to one WD. The Credit Committee, ex committee, would consider any consultations responses. Once received, the Credit Committee can also consider consultation responses when making future CAP proposals.
- 2.5 Following the one-day consultation, industry would be notified of the CAP value to be set and the CAP would become effective on the 10th WD after this notification.
- 2.6 In the event that the Credit Committee require a meeting to set a new CAP value following the consultation, then the committee would meet to determine a new CAP to be effective in 10 WDs time that would then be notified to industry.
- 2.7 The normal process will continue to be run for monitoring purposes. Once the market has stabilised, and volatile prices would no longer cause a significant number of CAP breaches or large changes in CAP, then the CAP review process can revert to the existing mechanism.
- 2.8 A notification to industry should be sent out to inform industry when the alternative CAP review process will be used and when the Credit Committee have returned to the normal process.

3. Credit Committee views

- 3.1 The Credit Committee have been given the opportunity to comment on and review the proposed changes. The committee agree with the approach to move to faster implementation timescales and more flexibility.
- 3.2 A member has raised concerns about how the alternative process moves away from a more mechanistic approach. In the absence of a prescribed formula to set the CAP they seek the views of the Panel in what philosophy should be used to set the CAP during a temporary alternative CAP review period.

4. Recommendations

- 4.1 We invite the Panel to:
- a) **PROVIDE** any comments on the proposed mechanism and how the Credit Committee can use their influence on setting the CAP
 - b) **APPROVE** the suggested edits to the Credit Assessment Price (CAP) Review Guidance Document
 - c) **NOTE** that if approved the guidance will be updated as soon as possible following this meeting so that they can take effect.

Attachments

Attachment A – Proposed edits to the Credit Assessment Price (CAP) Review Guidance Document

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