

# Annual Credit Assessment Price (CAP) Process Review

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<b>Meeting Name</b>	BSC Panel
<b>Meeting Date</b>	20 March 2014
<b>Purpose of paper</b>	For Information
<b>Summary</b>	This is the annual review of the CAP process by the Credit Committee. The view of the Credit Committee is that the CAP review process has worked well during the 2013-2014 BSC Year and the Credit Committee recommended no change to be made to the current process. The BSC Panel is invited to note the views of the Credit Committee.

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## 1. Why are we providing this review?

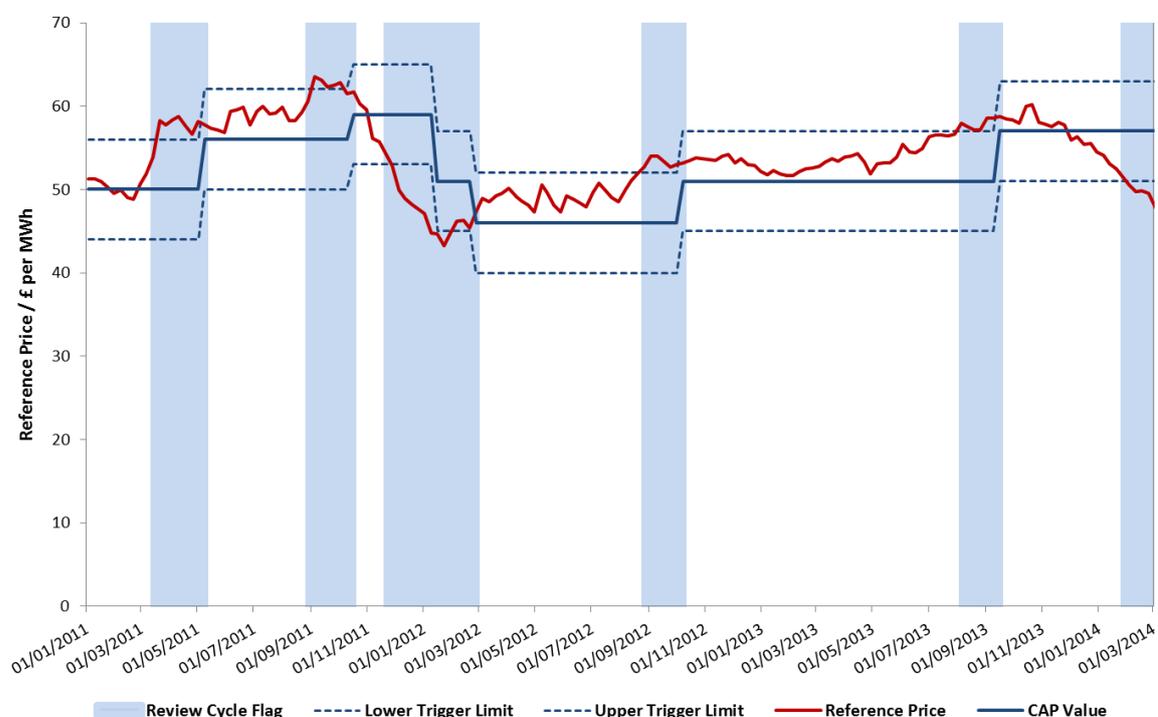
- 1.1 The last review of the Credit Assessment Price (CAP) process was presented to the BSC Panel in March 2013. The Panel agreed that such a review should be carried out at least annually.
- 1.2 The aim of the review is to report how well the process that monitors and amends the CAP value worked during the 2013-2014 BSC Year. This review is provided by the Credit Committee, which is the Panel Committee charged with operating the CAP review process, including determining changes to the value of the CAP.
- 1.3 Information on the [review process](#) is available on the BSC Website.

## 2. What happened during the 2013-2014 BSC Year?

### CAP Reviews & Changes

- 2.1 The monitoring and review process works by comparing the current value of CAP with a reference price derived from average quarterly forward market prices. This forward price data is currently provided by ICIS Heren. Where the absolute difference between the two values exceeds an agreed trigger level (currently £6/MWh), a CAP review is triggered. Graph 1 shows the values of the CAP and the reference price over the last three years (the CAP process was started in October 2007). The blue shading indicates periods when the CAP was under review.

Graph 1: Reference Price and CAP



Forward Prices provided by ICIS Heren

- 2.2 There were two reviews of the CAP during the 2013-2014 BSC Year (the same number of reviews as the previous year).
- The first breach occurred on 5 August 2013, when the CAP upper trigger was breached due to higher Q1 2014 forward prices. As a result, the CAP was increased from 51/MWh to £57/MWh on 12 September 2013.
  - The second breach occurred on 3 February 2014, when the CAP lower trigger was breached due to lower Q3 2014 forward prices. As a result, the CAP was decreased from 57/MWh to 49/MWh on 12 March 2014.
- 2.3 Details of CAP values and reviews during the 2013-2014 BSC Year are set out in the table below:

Date of CAP Trigger Breach	Effective Dates of CAP	CAP Value implemented	CAP Value proposed in Consultation
28 Aug 2012	4 Oct 2012 – 11 Sep 2013	£51	£52
5 Aug 2013	12 Sep 2013 – 11 March 2014	£57	£58
3 Feb 2014	12 March 2014 (live)	£49	£51

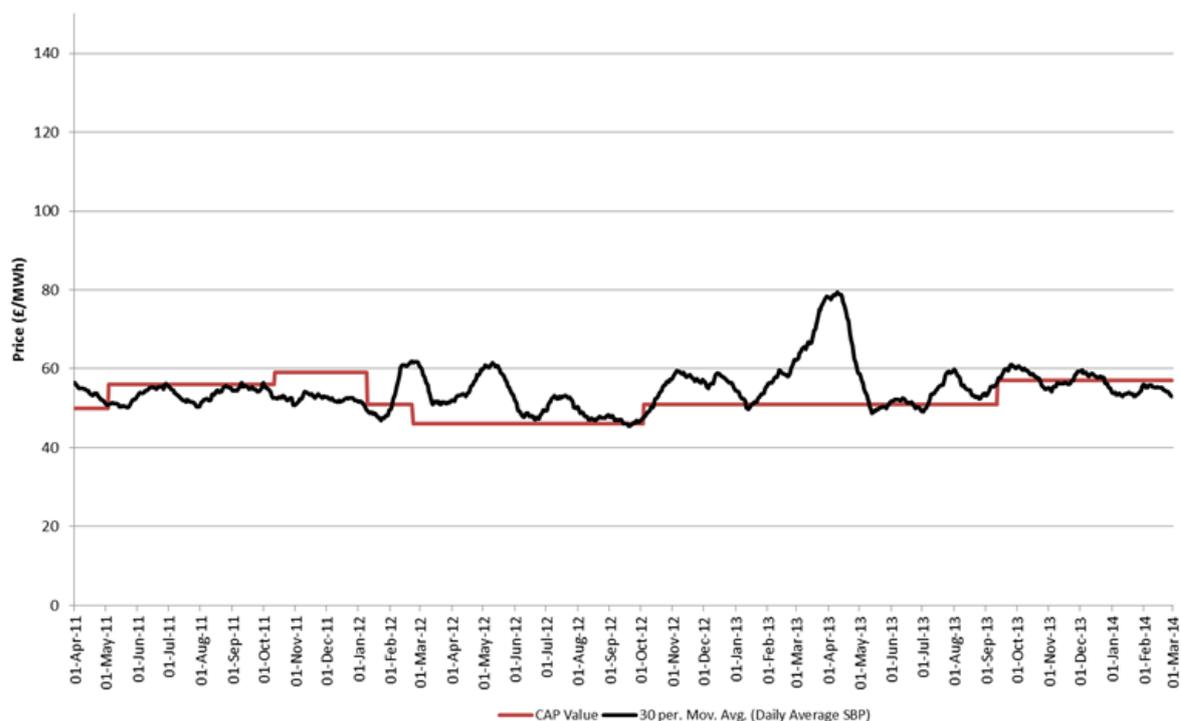
## Changes to the Trigger Level

- 2.4 No change was made to the £6/MWh trigger level during the 2013-2014 BSC Year. The Committee considered the value at its meetings and determined that it remained appropriate.

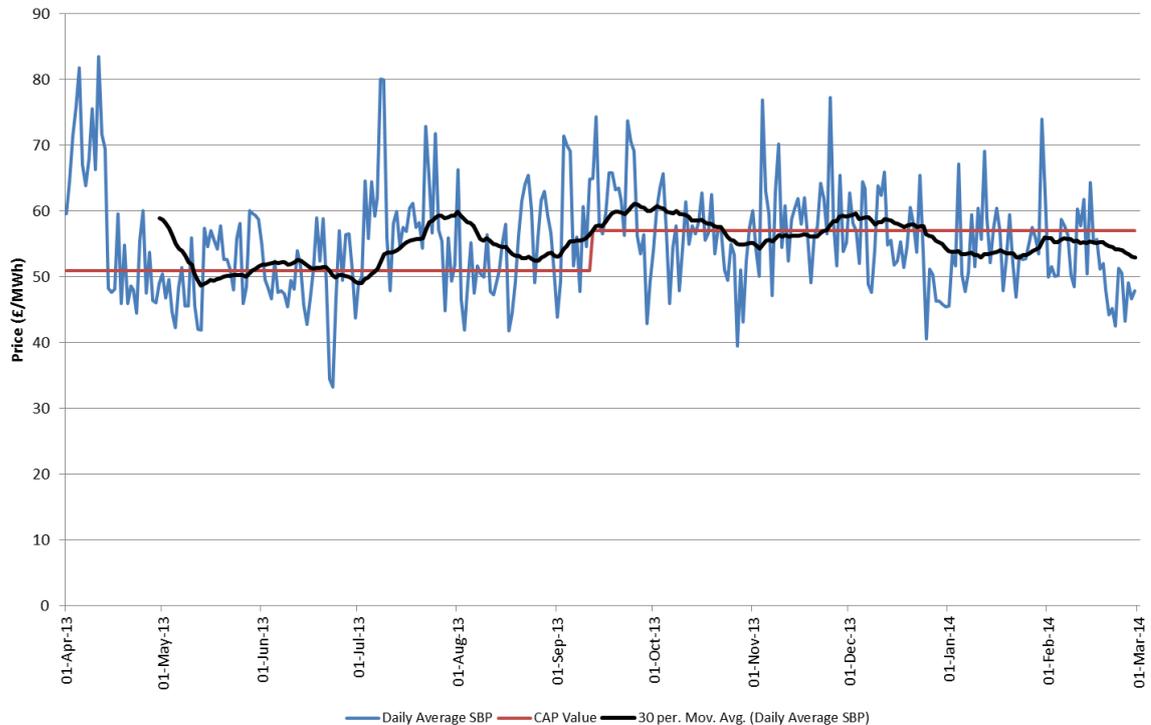
## How well did the CAP reflect System Buy Price?

- 2.5 The CAP is intended to be a proxy for System Buy Price (SBP). The underlying reason for the CAP review process is to set the CAP so that it gives a good reflection of what we expect SBP to be. Because of the time taken to review and change the CAP, we set the CAP based on the industry expectation of general electricity price levels in 2 - 6 months' time. So the way to measure how well this review process is working is to see how well the CAP value that we set matches the actual SBP.
- 2.6 Graphs 2 and 2a show the relationship between the CAP and daily average SBP. These graphs show how well the current CAP review process predicts outturn SBP. Graph 2 shows the last three years, while Graph 2a shows the data for the last 12 months only. To provide clarity over the longer time period in Graph 2, we have removed the daily average SBP but kept the 30 day moving average of daily SBPs.

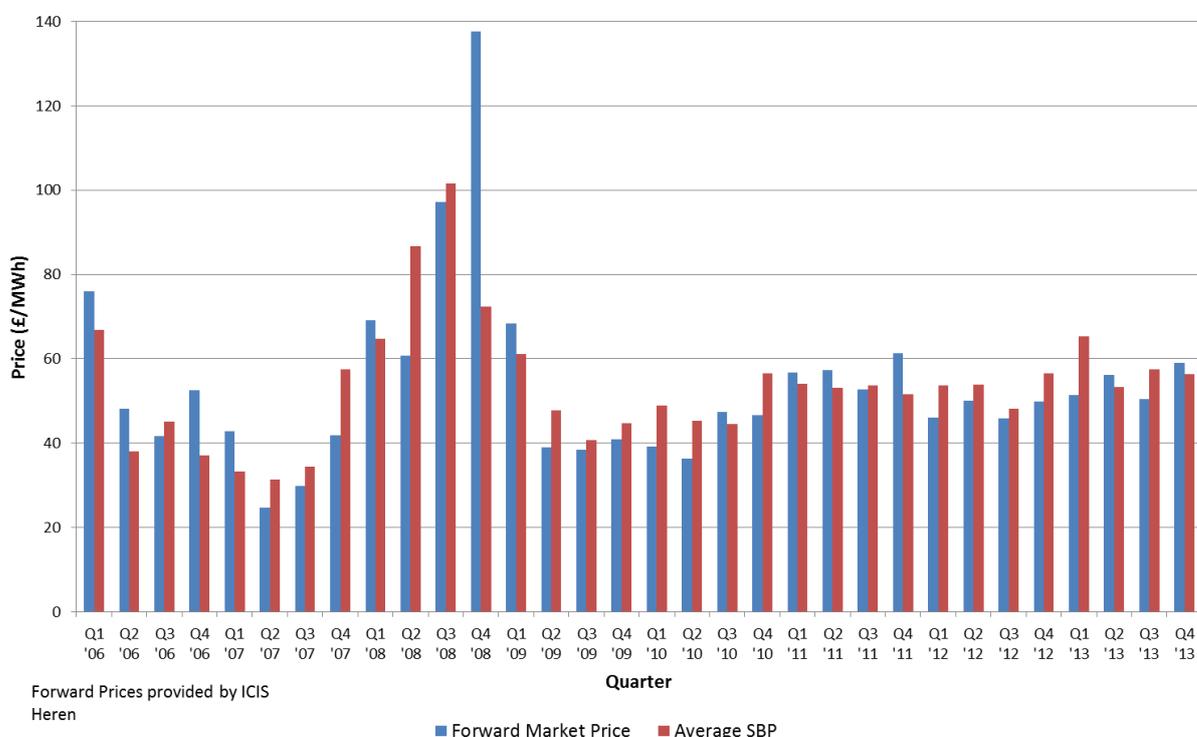
**Graph 2 Daily Average System Buy Price and CAP**



Graph 2: Daily Average System Buy Price and CAP



- 2.7 The graphs show that, the CAP has reflected the outturn SBP fairly well for most of 2013-2014.
- 2.8 Graph 3 shows the average outturn SBP over each quarter against the forward price for that quarter. This forward price is the last available forward market price before the quarter actually began. This is another measure of how good the CAP review process is overall. This is because if the forward price does not predict outturn future SBP movements well, then under the current methodology, the CAP will not reflect future SBP well either. Of course, forward prices are not necessarily used by the markets as predictors of SBP, but we have previously found that they are generally a good basis for this purpose, as can be seen over the years in Graph 3. Hence they have proved a good basis for use in the CAP review process.

**Graph 3: Average Outturn SBP against Quarterly Forward Market Prices**

- 2.9 The graph shows that the quarterly forward market prices predicted the outturn SBP well during the 2013-2014 BSC Year.

### Credit Committee Membership

- 2.10 There are currently six members of the Credit Committee. The BSC Panel Chairman, Michael Gibbons, is the new Chairman of the Credit Committee.
- 2.11 Under the Terms of Reference, the maximum membership is ten, with quorum for the meetings being three. Members of the Credit Committee are drawn from the Panel, Imbalance Settlement Group or Supplier Volume Allocation Group.

## 3. View of the Credit Committee

- 3.1 The Credit Committee believes the CAP review process is working well within the constraints of the current BSC and has captured the movement of market price well during the 2013-2014 BSC Year.
- 3.2 The Committee recommends no change to the current CAP process.

## 4. Recommendations

- 4.1 The Panel is invited to:

- a) **NOTE** that the Credit Committee recommends no change to the CAP review process; and
- b) **NOTE** that the Credit Committee will recommend changes to the BSC Panel should it believe changes are appropriate in future.

**For more information, please contact:**

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