The background features a large, semi-transparent white arrow pointing from the bottom-left towards the top-right. Behind the arrow, there are faint, stylized images of solar panels and a white turbine or windmill component. The overall color palette is light, with blues, whites, and oranges.

Introduction and background to the Electricity cash-out SCR

30 April 2012

Electricity Cash-out

- Cash-out provides
 - the principal incentive for demand and supply to be balanced in the short term
 - longer term signals to invest in building and/or maintaining generation plant and potentially demand side response
- We believe that these signals could be improved to improve security of supply and reduce balancing costs

Issues with the cash-out arrangements

- Our Electricity cash-out issues paper (November 2011) identified a number of specific issues with the cash-out arrangements:
 - Cash-out prices may not fully reflect scarcity at times of system stress
 - Cash-out prices may not provide the right incentives for the engagement of the demand side
 - Cash-out prices suffer from a lack of transparency and predictability
 - Dual cash-out prices have a large spread
 - Participants lack incentives to provide accurate Physical Notifications
 - Reconciliation cashflows are large and opaque

Background to the Electricity Cash-out SCR

- Our Electricity Cash-out Issues paper sought participants' views on
 - whether Ofgem should take a lead role to review the arrangements
 - what the scope of such a review should be
 - what the cash-out principles of such a review should be
- Following consideration of the responses, our March 2012 open letter informed of our decision to launch an SCR in Summer 2012 and to refine the scope with stakeholder input in preparation for this

Purpose of this event

- Today we are seeking to
 - gain feedback from stakeholders on our proposed principles and scope for the SCR
 - understand stakeholders' views of the key areas for consideration
 - initiate the necessary discussion with industry
- We acknowledge the complexity of the issues and recognise the need for early and active engagement of the industry

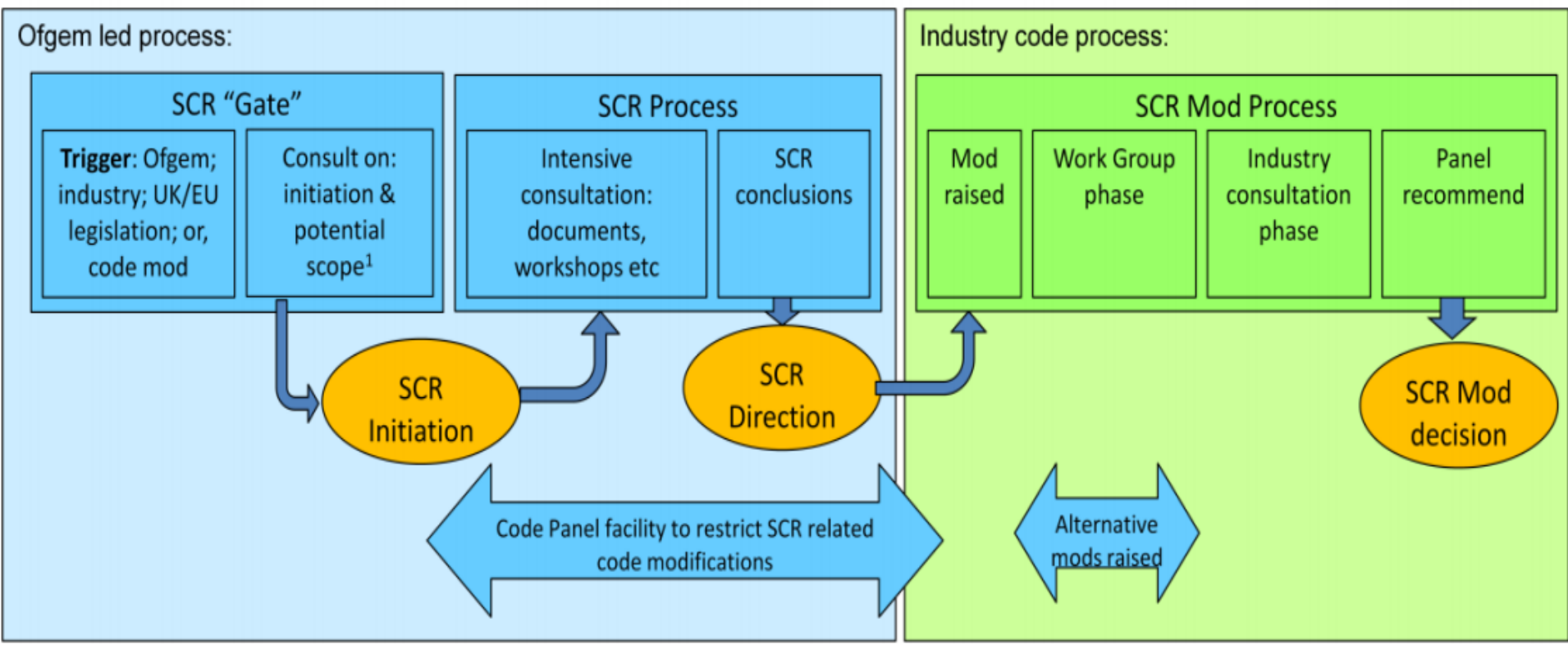
Reasons for our decision to launch a SCR

- An SCR will allow us to
 - complete a wide-ranging review of the arrangements
 - make directions leading to the delivery of any change which is deemed necessary as a result
- 28 responses received to the Electricity cash-out issues paper – diverse with regards to ‘if’, ‘when’ and ‘how’, but general agreement that issues with the cash-out arrangements do exist
 - This diversity supports the case for a wide-ranging review of the arrangements
- We believe that failing to consider reform to the existing arrangements could harm future electricity security of supply and unnecessarily increase the costs of balancing the system

SCR process (1)

- Our SCR launch statement in Summer will set out how we intend to manage the SCR and the steps involved. Generally the process will consist of:
 - Initial consultation setting out current issues and our thinking on how to best tackle these issues
 - Initial conclusions document setting out reasons for our approach and whether any further work is required
 - Consultation on final conclusions including final impact assessment of the proposals
- The SCR process is intended to last for approximately 12 months. However, we will take into consideration the refined scope, the complexity of the project, and the industry's ability to resource and support the process and may schedule the SCR to last for more than 12 months

The SCR process (2)



Indicative timeframes:



Interactions with other market developments

Government's EMR Capacity Market policy proposals

- Also aims to provide a signal for the value of additional capacity
- Depending on the design, cash-out prices may have a direct role in the capacity mechanism

European Target Model

- Balancing framework guidelines to be finalised this year and associated network code to be finalised in 2013

Ofgem's liquidity proposals

- No intervention in near-term markets at present
- Noted that cash-out may have an impact on liquidity
- We think it is appropriate and important to progress this work now. We will keep a close eye on developments in these closely related areas to ensure consistency

The background of the slide is a composite image. On the left, there are rows of solar panels under a bright sun. On the right, a hand is shown holding a white document. In the bottom left corner, a blue gas burner is visible. The overall theme is energy and customer service.

ofgem

Promoting choice and value
for all gas and electricity customers