

## **EFET response to Ofgem's consultation on Responding to high balancing costs in winter 2021: Update and proposal to introduce a new licence condition**

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The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent and liquid wholesale markets. We build trust in power and gas markets across Europe, so that they can underpin the sustainable and secure supply of energy and enable the transition to a carbon-neutral economy. EFET currently represents more than 120 energy trading companies, active in over 28 European countries. For more information, visit our website at [www.efet.org](http://www.efet.org).

We appreciate the opportunity to comment on the Ofgem consultation on introducing a new licence condition in response to the high balancing costs in winter 2021. Regarding the drivers for this specific price rise, we cannot comment, as that needs to be assessed in view of the relevant data and evidence. However, in principle, **it is our view that enhancing competition in the Balancing Mechanism (BM) would have important benefits for improving price signals and reducing costs, which are ultimately borne by consumers**. We would therefore encourage the introduction of measures that seek to increase competition and participation in the BM, as opposed to measures that will have the effect of limiting competition, such as making it more complicated to bid or introducing price caps.

At the moment, we see three distinct blockers to participation in the BM, namely:

- 1) Behavioural issues: The Control Room is used to dispatching larger assets as it is easier to do so and that is how they have always operated. This is evidenced by increasing 'skip rates'. Therefore, even if smaller assets endure the costs and effort required to participate in the BM, there is currently no guarantee of being dispatched.
- 2) System capability issues: Until there are significant upgrades to the Control Room systems, the dispatch process remains highly manual which does not support efficient dispatch of smaller assets.
- 3) Reliability over participation: There is little experience with the participation of distributed energy resources (DER) which does not give the Control Room enough comfort that it will provide the required response. This could be improved by greater visibility and a larger level of participation to improve learnings.

Facilitating the (more active) participation of a diverse range of market participants, including demand response and energy storage, as well as smaller units, would help to improve competition, enhance flexibility and security of supply, and reduce the carbon intensity of the BM. Therefore, we believe there are a number of issues which need to be addressed across

the short to medium term in order for there to be a significant improvement in the operation of the BM.

In terms of the new licence condition proposal, we see this as an additional measure to address the specific concern that Ofgem has identified with the submission of zero MW Physical Notifications (PNs). We do have concerns, however, about some of the other measures that were mentioned in the consultation document.

**Option 1:** With respect to the first option - **implementing a price cap on BM offer prices - we would advise strongly against introducing such a measure.** A price cap, as the consultation document recognises, would dampen price signals, which would affect investment, security of supply, and competition. Setting the level of the cap would also be difficult and would need to involve regular reviews and potential adjustments to reflect changing market conditions, which would create uncertainty for market participants.

**Option 2:** The second option - **changes to BM bid/offer structures** – could potentially offer some helpful improvements in the form of simplified bid/offer structures. The potential impact on smaller generators and investment in generation, however, as highlighted in the consultation document, should be carefully assessed. More complex bid/offer structures, at the same time, may make the ESO's decision-making less transparent, which should certainly be avoided. We also recognise that such changes would need much consideration and may take longer to implement.

**Option 3:** Regarding the proposal to introduce **a new NGESO Balancing Service to procure firm reserve**, we see this proposition being aligned to the proposed 'Balancing Reserve' Product which has recently been proposed by National Grid, whereby they procure a fast-responding Reserve at day-ahead to ensure it is available in the BM. We believe this product will provide early certainty to assets ahead of real time and lead to lower BM costs.

**Option 4:** The proposal for **a new licence condition preventing excessive benefit after submitting a zero MW PN** may be helpful in addressing the specific issue identified by Ofgem in relation to the submission of zero MW PNs. We do not have specific concerns regarding this option and agree that it is not likely to impede price signals or unduly disrupt existing trading arrangements. However, it would be important to define carefully what is meant by 'excessive benefit.'

**Option 5:** We would advise strongly against **restrictions on amending PNs close to real time.** This would reduce the flexibility of market participants' dispatch decisions and would constitute a significant departure from the current self-dispatch market arrangements, as also highlighted in the consultation document. Importantly, it would also impact intermittent generators where flexibility to adjust positions closer to real time is essential.

**Option 6:** With respect to the option to **clarify 'good industry practice' in the Grid Code**, we agree that this option would be straightforward to implement and is unlikely to have any negative consequences.

**In summary**, we agree with the qualitative criteria used by Ofgem in assessing the six options. We would also add "transparency in the functioning of the Balancing Mechanism" as an important criterion.

We also agree with the assessment itself, as summarised in Figure 1 of the consultation document. **We would advise strongly against the introduction of a price cap on BM offer prices and against restrictions on amending PNs close to real time** for the reasons highlighted above.

In our view, the option presented by Ofgem for adoption – **introducing a new licence condition preventing excessive benefit after submitting a zero MW PN (option 4)** – could potentially help to mitigate the specific issue with respect to submitting zero MW PNs. However, **we believe that in addition competition in the BM needs to be strengthened, as that would help to improve price signals and reduce the costs of the mechanism to consumers more generally.**

## **Responses to the consultation questions**

*1) Do you agree that our preferred option will effectively prevent the behaviour that caused last winter's high balancing costs? Please provide reasons for your answer.*

In our view, option 4 could be helpful in reducing or preventing the described behaviour in relation to the submission of zero MW PNs. However, as emphasised in our introductory comments, we think that improvements to competition would have a stronger positive impact on bringing balancing costs down more generally.

*2) Is the proposed licence condition drafting in Annex 1 sufficiently clear? Are there any drafting edits or additions that you would encourage us to consider?*

In our view, 'excessive amount' would need to be defined. The guidance might include a reference price such as intra-day power trading.

*3) Do you agree with the initial list of factors to consider when assessing excessive behaviour? Are there any other factors that you would encourage us to consider?*

Yes, we agree.

*4) Is there any specific information you would like to see in the accompanying guidance related to interpretation and enforcement of the new licence condition?*

How will the license condition be monitored and will it be across each BMU?