
Call for input: Transmission Constraint Licence Condition

7 December 2023

Summary

This call for input invites views from industry participants on whether any changes are required to the Transmission Constraint Licence Condition (TCLC) in order to ensure that it is as effective as possible in keeping down balancing costs. It accompanies a formal consultation on a proposed update to the guidance that Ofgem publishes alongside the TCLC. Responses should be received no later than 1 February 2024.

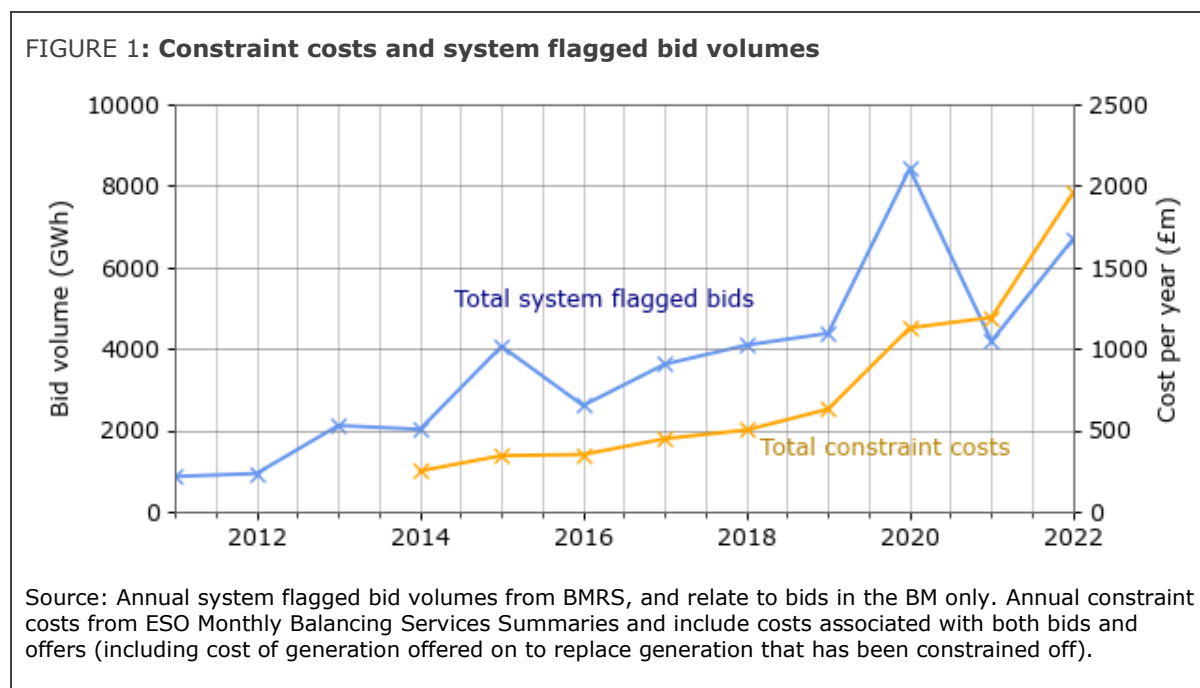
Transmission constraints are any limits on the ability of the electricity transmission system (or any part of it) to transmit the power supplied onto the transmission system to where it is needed. Where transmission constraints occur, then individual electricity generators, or groups of generators in particular areas, can hold a position of market power, with the electricity system operator (ESO) having limited options to manage the constraint other than reaching an agreement with the owners of those specific units to alter their planned output.

The TCLC (standard licence condition 20A of the Generation Licence) exists to protect against this market power. By prohibiting licensees from obtaining an excessive benefit in relation to bids submitted in the Balancing Mechanism (BM) in transmission constraint periods, it helps to keep down balancing costs – and, ultimately, consumers' bills.

We publish guidance for licensees and other interested parties on our interpretation and approach to the enforcement of the TCLC. On 7 December 2023, we launched a consultation on a number of proposed updates to this guidance, intended to provide generators with a greater level of detail in relation to our expectations regarding compliance with the TCLC.

The licence condition itself was last updated in 2017. Since then the volume of bids accepted for the purposes of constraint management has increased significantly as the expansion of renewable generation has outpaced network reinforcement (see blue line in Figure 1 below, with constraint management bids approximated using system flagged

bids) – as has the total cost of constraint management (see orange line). The extent of constraint management activity that the ESO is required to carry out is forecast to increase further as the decade progresses.¹



While work is underway to minimise the costs to consumers of managing constraints (including via the development of new balancing services),² these trends mean that the importance of the TCLC in protecting against the inherent market power which can arise in the presence of transmission constraints is greater than ever. With this in mind we have chosen to – alongside the consultation on the TCLC guidance - collect views from market participants via this call for input on whether any changes are required to the licence condition in order to ensure that it is as effective as possible in keeping down balancing costs.

Any submissions received in response to this call for input will be considered within the context of wider policy reform, including the UK Government's Review of Electricity Market Arrangements (REMA) programme. This includes considering whether a case exists for making changes in advance of broader market design changes resulting from REMA, or whether any changes should be subsumed within that package of reforms.

This is not a formal consultation, and at this stage we have not made any decision about whether any changes to the TCLC are required. A formal consultation would follow were,

¹ See for example [ESO Modelled Constraint Costs, NOA 2021/22 Refresh, August 2022](#)

² For example, under the ESO's [constraint management pathfinder](#)

having reflected further in light of responses to this letter, we were to consider there was a case for change.

For the purposes of generating discussion, we have in the remainder of this document set out potential changes to the TCLC which might in principle be made in order to extend its scope and maximise the protection that it offers against the exercise of market power in the presence of transmission constraints. We would welcome views from industry on each of these potential changes, as well as suggestions for any other changes which could be made which would improve the effectiveness of the licence condition in achieving its aims.

1. Expanding the TCLC to balancing services used by the ESO to manage constraints other than the BM

In its current form, the TCLC places a restriction on the prices of bids that are submitted by licensed generators in the BM. While the BM remains the primary way that the ESO manages transmission constraints, it also uses other balancing services to do so, including bilateral contracts with market participants ahead of BM timescales under Schedule 7A of the Grid Trade Master Agreement,³ and intertrip services.⁴ While the BM accounts for the majority of the ESO's constraint management activity, the costs incurred in managing constraints outside of the BM appear to have been significant during certain months in recent years (and in particular in summer 2020 and summer 2022).

One change which therefore could in principle be made and on which we are inviting views would be to expand the TCLC to prohibit licensees from obtaining an excessive benefit in relation to reductions in generation procured via other categories of balancing services, not just bids in the BM.

2. Expanding the TCLC to offers

At present, the TCLC places a restriction on the bid prices which can be submitted by licensees in the BM in transmission constraint periods, but not on offer prices. We understand that constraints requiring the ESO to increase the output of generators on particular parts of the network (such as voltage constraints) have historically only accounted for a relatively small part of constraint costs. Nevertheless, we would expect

³ [Trading | ESO \(nationalgrideso.com\)](https://nationalgrideso.com/trading)

⁴ [Intertrips | ESO \(nationalgrideso.com\)](https://nationalgrideso.com/intertrips)

generators operating in the presence of such constraints to benefit from market power in much the same way as generators subject to any other transmission constraint.

Therefore, another change which could in principle be made and on which we are inviting views would be to expand the TCLC to prohibit licensees from obtaining an excessive benefit in relation to offers in transmission constraint periods, in the same way that generators are currently prohibited from doing so under the TCLC in relation to bids. This could be limited to offers in the BM, or could extend to increases in generation procured under balancing services more broadly (see 1 above).

3. Expanding the TCLC to bids to import or offers to export

At present, the TCLC places a restriction on the bid prices which can be submitted by licensees in transmission constraint periods only where those bids relate to reductions in generation. That is, the restrictions of the TCLC apply only where a generator is – absent the bid – due to export power.

The rationale for this is that the TCLC should only apply where a licensee's intended level of output for a particular generation unit causes or exacerbates a transmission constraint. In doing so, the TCLC ensures that licensees are prevented from benefiting from market power which may arise as a result of a transmission constraint; while at the same time ensuring that the BM can work to reward generators that are available to help to resolve a constraint (incentivising further investment by providers that can offer such services).

Nevertheless, where constraints exist, even if a generator is not itself making the constraint worse via its expected level of output, it may still benefit from significant market power. To the extent to which generators take advantage of this by submitting expensive prices, this will push up the cost of managing constraints. The nature of the market may mean that barriers exist which prevent other providers from competing effectively for the constraint management services in question.

Therefore, another change which could in principle be made and on which we are inviting views would be to expand the TCLC to prohibit licensees from obtaining an excessive benefit on bids in transmission constraint periods even where that generator was not due to export (ie it had submitted a final physical notification of zero or lower). Were the TCLC expanded to include offers (see 2 above), then similarly this extension could include prohibiting licensees from obtaining an excessive benefit on offers in transmission constraint periods even where the generator was not due to import (ie it had submitted a final physical notification of zero or higher).

4. Replacing the requirements of the TCLC with an explicit cap on generators' prices or profits in constraint periods

The current licence condition prohibits generators from obtaining an excessive benefit on bids in transmission constraint periods. While we publish guidance providing details of our approach to assessing whether a bid price is excessive, "excessiveness" is not fully defined in advance, and will instead be considered on a case-by-case basis.

One possible change to the existing licence condition would be to introduce explicit price controls, which either set out the maximum permissible bid (or offer) prices in transmission constraint periods, or alternatively set out a cap on the mark-up which generators could charge over and above the short run marginal costs of reducing output. The price controls could in principle be set at different levels for different technology types, and might vary dynamically with certain key cost drivers.

International examples exist where the amount that market participants can charge in constraint periods are regulated in this way.⁵ An approach of this type could have an advantage over the existing regulation in that it would provide greater certainty to the market about what prices would and would not be acceptable. It would, however, be administratively much more complicated than the existing licence condition.

5. Extending the requirements of the TCLC to providers of balancing services other than licensed electricity generators

At present, the specific requirement not to submit excessive bid prices in transmission constraint periods exists in the standard conditions of the electricity generation licence. However, it is possible that market participants other than licensed electricity generators may provide balancing services used by the ESO to manage transmission constraints, and may enjoy market power in much the same way as a licensed generator. This could include smaller, licence-exempt generators; those offering increases or reductions in output via interconnectors; or providers of demand-side flexibility.

One possible extension to the existing requirement would therefore be to introduce new requirements on providers of balancing services other than licensed electricity generators, equivalent to the prohibition under the TCLC.

⁵ See [Assessment of Locational Wholesale Pricing for GB \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/publications/assessments/assessment-of-locational-wholesale-pricing-for-gb), page 41 and 42

Next steps

We request that any responses to this call for input are received no later than 1 February 2024. Submissions should be marked indicating that they relate to the TCLC call for input, and sent to WholesaleMarketPolicy@ofgem.gov.uk, or by post to:

Domestic Market Management team
Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

Following receipt of any responses to this document, we will consider our next steps. This could include concluding that no changes to the TCLC are required at this time, or the launching of a formal consultation on potential changes to the TCLC, or using the responses received as an input to any wider package of reforms emerging from the REMA programme.