

A blue-tinted background image showing a close-up of electrical components, including a three-pin UK power plug and a circuit board with various electronic components.

Cash out review working group - introduction

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Scope of this meeting

- Introduction
- Proposed approach
 - analytical framework and associated discussion
- Terms of reference
 - scope and aims
- Prioritisation
 - which issues first?
- Process going forward
 - meeting arrangements etc

Recent Modification Proposals

- Recent focus on cash out arrangements
- Issues raised via modification proposals:
 - BSC P135, P136, P137, P138
 - BSAD v3.0, v3.1
 - NC 0606, 0607, 0635, 0636
 - BSC P171, P172, P173, P175 – *specific to Damhead Creek*
- Very complex issues and some difficult decisions

Need for change?

- Some strong views on need for change
 - *'short-term and forward energy markets have largely failed to respond effectively at times when the system has been under particular stress...the failure of short-term prices to respond to market shortages raises longer-term concerns about the ability of the forward markets to respond effectively to emerging shortages and consequent risks to security of supply'* Barclays Capital
 - *'We consider that the design of cash out pricing mechanisms should strive to reflect all the costs incurred in balancing the system. The market would then have a clear signal of the costs of securing the system during the balancing period and market participants would have the incentives to try to ensure balance for low probability events'* NGT, Winter Ops Report

Cash Out Review

- Feedback and recent proposals indicated a wider review was required
- Limitations of looking at issues that have wider governance considerations
- Cash out review announced on 1 March 2004
- Cash out review document published in May 2004
 - highlighted key issues for consideration
- Open letter published in August 2004
 - established the cash out review working group
- Clearly no 'moratorium' on modifications in the interim

Review moving forward

- Other priorities have delayed commencement of the review until now
 - Gas Probe
 - Exemptions
 - Top Up Review
- Unfortunate delay – focus now on options for coming year
 - events have now moved on
 - increased priority for review going forward

Proposed objectives

- Ofgem propose the two main objectives of cash out are:
 - to provide appropriate commercial incentives for market participants to balance their own positions (including incentives to provide reserve) and therefore deliver security of supply
 - to reflect the costs, including reserve costs, incurred by the relevant SO when undertaking energy balancing actions as residual balancer
- Secondary objectives are:
 - not being easily open to manipulation or gaming
 - transparency
 - prompt (or real time) reporting of prices
- Interested in the views of the group on these objectives

Purpose of the CORWG

- Ofgem propose to:
 - assess the existing gas and electricity cash out arrangements against these high-level aims
 - consider potential revisions which could better achieve these aims
- Outcome expected to be:
 - recommendations from the group about possible revisions
 - combination of quantitative and qualitative analysis of options
 - Ofgem paper summarising analysis and discussions undertaken by the group and the recommendations reached
 - recommendations can be progressed via the relevant modification process as considered necessary by market participants

Proposed approach of the CORWG

- Cross-governance focus
 - enable issues that cut cross both the gas and electricity cash out arrangements to be examined holistically
- Analytical assessment
 - analysis of historical and simulated data
 - assess whether cash out prices reflect costs incurred and provide appropriate incentives to balance on average and difficult days
 - assess different inputs and resulting prices
- Discussion based on analysis
- Develop recommendations where appropriate

Proposed scope of the CORWG (1)

- Ofgem propose for the following issues to be excluded:
 - single versus dual cash out prices
 - pay-as-bid versus cleared price
 - ex post trading in electricity and gas
 - Gate Closure
 - system balancing/energy balancing split principle
 - balancing periods
 - separate production and consumption accounts for electricity imbalance volumes
- Issues not subject to split governance
 - Market participants can raise modification proposals via normal channels to address these issues

Proposed scope of the CORWG (2)

- Issues to be included:
 - weighted average vs marginal prices for cash out
 - pricing of SO reserve contracts and how these feed into imbalance
 - reverse pricing, in the case of electricity, and default differentials in the case of gas
 - split of system and energy balancing actions, how these do/don't feed into the calculation of cash out prices
 - the methodologies for redistributing imbalance cash flows
 - the methodologies for determining cash out prices in emergency circumstances
 - pricing of demand control and/or voltage reduction

Next steps

- Remainder of this meeting will discuss further:
 - proposed approach
 - draft scope
 - proposed timetable
- And will consider:
 - prioritisation of issues
 - process going forward
- Next meeting will begin the assessment of the issues



Promoting choice and value for all
gas and electricity customers