

Future Trading Arrangements Forum, 4th Meeting

Minutes from the 4th Meeting of
the Future Trading Arrangements
Forum

Date and time of Meeting
Location

04 July 2014 12pm – 4pm
Ofgem, 9 Millbank

1. Present

Chair	Mark Copley (Ofgem)
Present	Andrew Claxton (APX) Bill Reed (RWEnpower) Brian Galloway (Scottish Power) Chris Alexander (Consumer Futures) Colin Prestwich (Smartest Energy) Danielle Lane (DONG Energy) Ed Reed (Cornwall Energy) Fiona Navesey (Centrica) Ian Moss (National Grid) Lesley Gray (SSE) Mark Cox (EDF) Melle Kruisdijk (Wartsila) Nick Haines (Good Energy) Phil Hicken (DECC) Stephen Powell (CER) Stuart Cotten (Drax Power)
By telephone	Paul Jones (EON)
Ofgem representatives	Andrew Ryan Dipali Raniga Gareth Davies Grendon Thompson James Earl Leslie Neubecker Mark Copley Rachel Fletcher

Welcome and reintroduction to Future Trading Arrangements

Mark Copley opened the meeting and initiated introductions from around the table. He outlined the plan for the meeting and stated the aim to have a collaborative session to hear industry thoughts and talk about the big issues.

Mark Copley gave a background to the Future Trading Arrangements programme and developments since the open letter published in February 2014. On the Bidding Zones workstream, he stressed that Ofgem are thinking about how we would go about considering the issue and that all thinking shared in the meeting is initial thinking only.

Update on the Long Term Market Arrangements (LTMA) workstream and other workstreams

Andrew Ryan gave an update on the Managing Intermittency and Wider Balancing/Reserves workstreams. He confirmed that Ofgem are not yet planning to begin these workstreams, given other industry and regulatory priorities, but will reconsider the appropriate time to begin them later in the year.

Andrew talked through the Longer Term Market Arrangements workstream: the motivation behind it, the benefits of doing it and the expected outputs. Ofgem are beginning work on the LTMA workstream, which will consider the market arrangements under different scenarios and how these scenarios may put the arrangements under stress. We will report back to the next Forum meeting with an update on this.

- Stakeholders raised questions around the guiding principles that underpin the LTMA work eg
 - What is the approach to Europe? Are we assuming a push for early implementation of network codes or not? Are we looking to implement the legal minimum or more?
 - Approach to market versus regulation?
 - What is the headline industry structure that is assumed?

Ofgem: The European codes are law and have to be implemented so there is not much of a question here. The questions around market versus regulation and headline structure of industry are points to consider in the long term work.

- One stakeholder questioned the interaction between this work and the ACER Bridge to 2025 work that is going on at a European level.

Ofgem: These are distinct, but related, pieces of work, with one in the EU sphere and one in GB. The Bridge to 2025 should feed into the LTMA work, but not constrain it.

- One stakeholder questioned how this work would take into account the potentially transitional effect of EMR.

Ofgem: This is something to be mindful of when progressing the LTMA work.

- Stakeholders agreed that we shouldn't just consider the impact of trading arrangements but consider what they are trying to achieve and whether or not they are actually doing so. We need to think beyond market arrangements and all the other ways that value is provided eg security of supply, sustainability.
- The Forum recognised that the LTMA work is wide in scope and that 'trading arrangements' can be interpreted in different ways, and they need to be clearly defined.

- Stakeholders questioned the status of the LTMA workstream with respect to other workstreams and whether LTMA is a separate piece of work or a framework from which other FTA workstreams continue.

Ofgem: Whilst LTMA could well end up drawing on other workstreams and having a lot of similarities, it differs as it aims to take a step back from the immediate issues and focus on the future.

- One stakeholder asked about the scenarios in the LTMA work and what they are likely to include, ie generation mix, pattern of demand. It was suggested to look at levels at which renewables cause stress to the trading arrangements.

Ofgem: This is part of our work over the summer and industry views on what these scenarios should be are encouraged. This is not a big modelling exercise though; it is more of a 'stress test' of the current trading arrangements.

Focus on the Bidding Zones workstream and Ofgem's Literature Review

Mark Copley now moved to discuss the Bidding Zones workstream. He gave an overview of what a bidding zone is (with a definition) and then talked through the context sitting behind the workstream. He mentioned the European context, with the CACM network code yet to be finalised and roles and responsibilities yet to be made absolutely certain. He stressed that the purpose of Ofgem's work on bidding zones is to put together a methodology which could be used to assess the configuration of bidding zones in GB.

- Stakeholders asked about Ofgem's communications with other NRAs (Dutch, Irish, French), given the effect changing bidding zones could have on prices and price convergence across markets.

Ofgem: We need to involve other NRAs and we are doing so - we have CER in the Forum, we are observing the ENTSO-E pilot studies and we speak with fellow NRAs frequently.

- One stakeholder warned that though the reports are straightforward for an AC network, more clarity is needed on whether everything is relevant or how it applies to DC connections.

Grendon Thompson gave more of a background to the European context, talked through the guidance that is in the CACM network code and the reports that ACER and ENTSO-E have produced.

- One stakeholder highlighted the timing of the assessment compared to other countries and a concern that if one country were to change the configuration of their bidding zones, it might affect the analysis that another country is doing.
- In response to a stakeholder question, Ofgem confirmed that there is no obligation in CACM to look at bidding zones on an individual country basis, but there is certainly nothing to prohibit that.

James Earl discussed the Literature Review that Ofgem had carried out and shared with the Forum members before the meeting. He talked through the variety of literature that had been reviewed and the wide reaching effects that the configuration of bidding zones may have. He distilled these into five key areas of impact which he then went into more detail on: liquidity and hedging, investment, efficient use of the network, market power and cross-zonal flows.

- Stakeholders agreed with the importance of both liquidity and investment in the assessment frameworks. They particularly reiterated the question that came out of the literature as to what the biggest investment signals actually are.

- Liquidity and hedging: One stakeholder stressed that even if a review of bidding zones suggested that an alternative configuration would cause problems with liquidity, that shouldn't be a block to doing anything as there are other ways to address liquidity.
- Investment: One stakeholder highlighted a concern that changing the configuration of bidding zones could result in sunk investment and stranded assets, at a high cost. They stressed the need to have stability of zones.
- Efficient use of the network: Two stakeholders both made the point that market efficiency depends on the SO being responsible for redispatch and how efficient/inefficient that redispatch mechanism is. Stakeholders advised to consider the cost of buying capacity between zones against the SO having to take redispatch actions to manage congestion.
- Market power: Stakeholders discussed the constraints on opportunities for market abuse provided by REMIT and the Transmission Constraint Licence Condition (TCLC).
- Cross-zonal flows: Stakeholders mentioned the need to consider the influence of the capacity mechanism, administrative VOLL pricing and the Reserve Scarcity Function in EBSCR.
 - One stakeholder initiated a conversation about long term transmission rights and firmness. The US precedent as to how to assess congestion rents was highlighted and the Nordic example of using CfDs was discussed, citing EFET as a critic of the Nordic model. The issue was discussed around the table and several stakeholders stressed the importance of the issue. Not having (tradable) financial transmission rights was said to be discouraging investment. Ofgem was encouraged to look at the experience of the PJM market.
- Stakeholders discussed the need to also focus on policy and how policy interacts with the configuration of bidding zones. Examples provided included: CfDs; the capacity mechanism; REMIT; and financial EU legislation such as MiFiD.
- Retail markets, distribution networks, settlement arrangements, gas markets (including investment in the gas network) were also suggested as further areas to consider.
- The importance of politics in the issue was highlighted by one stakeholder, particularly the need for clarity on governance and who is doing what.

Mark Copley summarised the key findings from the discussion to be considered further:

- **Costs of transition**
- **Impact on retail markets**
- **Interactions with other countries and how these are modelled**
- **Wider policy framework, ie financial and other legislation**

In the next discussion, each attendee was asked to think about the top two or three priority issues (related to bidding zones) from the perspective of an alternative entity. The results are summarised overleaf.

Entity	Top Issues
Power Exchange	- Liquidity - Max. exchange boundary capacity
Supplier	- IT systems/implementation - Liquidity/hedging - small supplier exposure
Generator near load	- Long term transmission rights - Grandfathering congestion charges
Generator behind constraint	- Same as generator near load - Investment signals
Investor in generation	- Wholesale prices - Price signals - Capacity markets
Storage/DSR investor	- Price signals - volatility
Interconnector	- Revenue/zone stability - Investment signals - interaction with CRMs
Consumer representative	- Market power > competition > prices
System operator	- Stability/robustness of zones - New roles (eg, capacity calculation) - Investment signals
Transmission owner	- Investment signals - Efficient use of the network

Tentative thoughts on bidding zones assessment methodologies

Grendon Thompson talked through the strawman methodology framework for the Market Report that Ofgem has been working on. He outlined four key themes: investment, liquidity and hedging, efficient system operation and market power, before going into more detail on how each of these could be measured.

- Stakeholders suggested additional analysis could look at the historic counterfactual, ie 'if a congested area hadn't existed and what the impact would have been on prices'.
- Stakeholders agreed that we should only conduct a bidding zones review if the Market Report and Technical Report provide a compelling case to do so.
- There were two suggestions from stakeholders on the liquidity theme: to measure actual products as well as volume of trades in markets and to look at the different parties trading and how accessible the markets are.
- The Forum agreed that the market report should look into the future, not just use historic data. It was also suggested that the report should look to include a measure of economic surplus, similar to how power exchanges calculate economic surplus from market coupling.

National Grid then talked through the methodology for the Technical Report. They outlined the process (at a European, not GB level) set out in the CACM Network Code as to who delivers the report, when and what it should include. They went into more detail on their proposed approach, which aligns with CACM by considering 4 key areas: location and frequency of congestions, expected removal of congestions, power flows not resulting from capacity allocation and congestion income and firmness.

- Stakeholders agreed with the approach to the Technical Report that National Grid outlined and had no comments.

Grendon Thompson explained the strawman methodology for a Bidding Zones Review report. He noted the inherent complexities of such a review and explained how Ofgem's preliminary thinking has built upon the current work of ENTSOE. Ofgem is currently thinking about the problem in terms of the types of questions which ought to be answered as part of a bidding zones review. It was noted that evaluating different bidding zones options would involve a series of trade-offs and judgements about the relative importance of different aspects.

- Stakeholders summed up the report process by saying that we first need to know if there is a problem, then need to know if assessing the configuration of bidding zones is the best way to solve the problem.
- In response to a stakeholder concern that the DC-links on the border prohibit expanding bidding zones, it was stressed by Ofgem that the framework should be designed to be fit for the future, therefore allowing for larger or smaller bidding zones.
- Stakeholders stressed that is important to consider whether looking at bidding zones was the right solution. If the problem is inefficient locational signals for generation and load, there may be other solutions. Stakeholders felt it was important that there is clarity as to what problem the Bidding Zones Review could seek to solve.
- Stakeholders questioned how long it would take to get to a decision once a bidding zones review had been launched.

Ofgem: This is uncertain, but ENTSO-E are using a 16 month review process, which they have recently launched for the pilot study. This does not include time after for regulatory review and possible implementation.

- One stakeholder queried the step between completing the Market and Technical Reports and launching a Bidding Zones Review. They considered that, at this point, we would need to consider whether there are other options that are a better way of dealing with any problems uncovered, and would like to see clarity on this in the methodology.

Concluding remarks and next steps

Mark Copley summarised the discussion and welcomed any further stakeholder views on the process. He thanked Forum members for their involvement and outlined the next steps for the Future Trading Arrangements project. Ofgem will keep Forum members updated with progress on the CACM Network Code and will report back to the Forum later this year with an update on the development of the LTMA and bidding zones workstreams discussed in this meeting.