

## ***Annex To Modification Proposal – Removal Of Price Spikes Associated With System Balancing From System Prices***

**Extract from Ofgem Consultation: “NGC systems operation under NETA: transitional arrangements”, April 2000.**

**Chapter 4, page 50**

### ***Introduction***

4.1 Under the new trading arrangements, NGC as SO will be purchasing a range of services through a variety of different arrangements, both inside and outside of the Balancing Mechanism, in order to meet its licence and other obligations to operate the electricity transmission system in an efficient, economical and co-ordinated manner and thus to ensure the security and stability of supply. In doing so, the SO will incur a range of costs. The December Consultation summarised these services and their costs into two broad categories:

- Energy balancing - the activities of the SO in matching overall supply and demand at a half-hourly level; and
- System balancing – the activities of the SO in achieving the stable and secure operation of the transmission system.

4.2 The December Consultation argued that participants who are out of energy balance should be exposed to all the costs incurred by the SO in achieving a gross energy balance (i.e. matching demand and generation at the half-hourly level). The actions the SO takes in the Balancing Mechanism naturally flow through to energy imbalance prices i.e. the System Buy Price (SBP) and System Sell Price (SSP) charged to out of balance participants. However, imbalance prices based solely on actions taken by the SO in the Balancing Mechanism are unlikely to reflect the total costs incurred by the SO in maintaining a gross energy balance. For example, they would not include the costs incurred by the SO in contracting ahead for reserve to meet energy imbalances.

4.3 Furthermore, **some Balancing Mechanism actions will be taken for system balancing reasons** such as those taken to provide frequency response services or to relieve transmission constraints. The December Consultation argued that **system balancing actions taken by the SO should be recovered from all participants on a fair and non-discriminatory basis**. In addition, the July 1999 and October 1999 NETA documents argued that ways in which the costs of transmission constraints, in particular, could be removed from imbalance prices should continue to be explored.

4.4 We address first the issue of how imbalance prices can be changed to reflect better the full costs including contract costs of energy balancing then consider how to exclude system balancing costs from energy imbalance cash out. The next section discusses how the costs of energy and system balancing services should be recovered under NETA. Finally, we consult on detailed proposals for the recovery of central NETA system costs being incurred by BSCCo.