

I-SEM

Response to Balancing Market Principles Code of Practice (SEM-17-026)

If you have any questions in relation to our response, please don't hesitate to contact Connor Powell (connor.powell@sse.com)

Thank you for giving SSE the opportunity to comment on the Balancing Market Principles Code of Practice consultation paper. This is an important document for the industry, regardless of whether operators expect their plant to be dispatched under these complex offers – while we recognise the RAs commentary in SEM-17-020 that:

*“[I]t should be noted by market participants that the BMPCOP will not materially affect the majority of energy traded in I-SEM, as it is intended that the BMPCOP will only be applied to complex bid offer data in the I-SEM BM, which primarily affect non-energy actions, a relatively smaller subset of the overall I-SEM electricity market. **By way of comparison, based on how the system was dispatched under the SEM, the level of non-energy actions may correspond on a value basis to 10% or less of total system revenue.**”*

SSE believes that some of the practical implementation of earlier decisions has been overlooked, particularly Section F which sets out both system flagging and NIV tagging as a basis for using Complex Bid Offer Data:

- (b) If any Bid Offer Acceptance for Generator Unit, u , at rank, k , has, after applying the Flagging and Tagging process in accordance with Chapter E (Imbalance Pricing), a Net Imbalance Volume Tag ($TNIV_{uk\phi}$) with a value less than one, or a System Operator Flag ($FSO_{uk\phi}$) with a value less than one, for any Imbalance Pricing Period, ϕ , within the Imbalance Settlement Period, γ , the most recently submitted valid Complex Bid Offer Data for the relevant Trading Day as at the Bid Offer Acceptance Time,
where:
 - (i) $FSO_{uk\phi}$ is the System Operator Flag for Generator Unit, u , and rank, k , in Imbalance Pricing Period, ϕ , determined in accordance with Chapter E (Imbalance Pricing) and where in the absence of a value for the period resulting from the process outlined in Chapter E (Imbalance Pricing) a value of one shall be used; and
 - (ii) $TNIV_{uk\phi}$ is the value of the Net Imbalance Volume Tag for Generator Unit, u , and rank, k , in Imbalance Pricing Period, ϕ , determined in accordance with Chapter E (Imbalance Pricing) and where in the absence of a value for the period resulting from the process outlined in Chapter E (Imbalance Pricing) a value of one shall be used;
- (c) Otherwise, the most recently submitted valid Simple Bid Offer Data for the Imbalance Settlement Period as at the Bid Offer Acceptance Time.

While it is unlikely that an in-merit unit would be consistently NIV tagged and paid at Complex Bid Offer Data, given the **5 minute imbalance pricing approach** selected, it is likely that offers with a value of far more than 10% of total system revenue will be subject to complex bid offer price regulation.

While an in-merit unit providing positive balancing energy may be taken at a simple incremental offers against an aggregate **short system** with a corresponding NIV across a 30 minute period, it is much less likely that the system will be short (as defined by the NIV) within every single 5 minute pricing period within that 30 minute settlement period, consistently triggering complex offers at most stations.

With that in mind, complex bid offer price regulation and the structure of the BMPCOP becomes a central consideration for every generator in the market, regardless of whether or not they expect to be taken by the TSO to provide non-energy products or compete in unconstrained markets for energy. SSE therefore has two major issues with the document proposed:

- **Price Regulation without monopoly:** we are still very concerned by the **Governance Arrangements** proposed – this BMPCOP document explicitly provides for far more regulatory flexibility, allowing the RAs to change and update terms whenever they feel they are required. It does not provide either flexibility or protection for generators who are faced with a far more prescriptive set of terms and none of the protections they may expect under standard price regulation. While some generation units could have local market power in a large proportion of settlement periods and might expect a more prescriptive set of terms for balancing market operation, the majority of units should be trusted to follow a broader market power licence condition.
- **Sledgehammers to crack nuts:** it would be far more appropriate to use the enforcement mechanisms provided for under REMIT to apply targeted, direct intervention against the few generation units who may not operate in line with balancing market principles set out in the generation licence. A prescriptive overarching BMPCOP document alongside the balancing market algebra as now finalised **will mean that the majority of generators in the I-SEM Balancing Market will be taken at price controlled offers during a typical trading day.**

SSE would far prefer an approach whereby the generation licence introduces clear principles to protect the market from the few units with local market power. The BMPCOP should be a more detailed subsidiary document setting out expected market practice which the Market Monitoring Unit can use to inform enforcement action against Balancing Market Units who do not appear to follow the broad market power licence condition rather than a formulaic prescription for Complex Bid Offer composition.

The rest of our response provides comments on the detailed BMPCOP changes, outlining some of the practical concerns with the proposed wording.

Section I

As stated above, SSE disagrees with the SEM-17-020 decision and believes that the licence should contain some broad principles for generators who would not expect to have local market power within the Balancing Market. This BMPCOP should cover accepted market practice and provide clear guidelines for the MMU to investigate using the broad enforcement powers already provided for under REMIT.

Section II

Complex Decremental price-quantity pairs should apply in very few trading periods, given the range of downward flexibility across the Transmission System and the Balancing Market Algebra (qBIAS, qTOTO) that removes incentives for constrained generators to inflate their bid price. However, in order to provide cost reflective complex decremental prices, generators could need to continuously route captured trades to calculate accurate bids.

We believe decremental bids are better subject to a principle based assessment of cost reflectivity by the MMU rather than the strict formulaic approach applied to incremental offers.

Section III

As per comments on section II, the formulaic approach to cost reflectivity is far more appropriate for MMU assessment of complex incremental offers.

We would also note that under a proposed PAR value of 0.17MWh within individual pricing periods, the ETA parameters issued for consultation do not seem to align with the BMPCOP sections as drafted.

Section IV

We welcome the wording changes for incremental fuel costs – the key goal is that participants ensure that the Regulatory Authorities understand how these are being derived – it should not seek to prescribe how participants must contract for fuel.

The primary issue with Section III is the ineligible costs that have been explicitly excluded – while the RAs stated in relation to risk in SEM-17-020 that:

“It is the SEM Committee’s view that generation units can best mitigate against risk to plant and equipment through insurance. There exists a global insurance market for power generation that offer various risk management solutions to cover such events. It is not unreasonable to expect prudent generation units to have taken out such policies to cover against such events.”

There are no insurance products that would adequately reflect all of the risks entailed by changes to running regimes, unique market-specific penalty arrangements etc that could be better provided for under a risk component in Complex Offers.

Standardised insurance products are by definition, standardised, converting a general set of power generation asset risks into an insurance policy and a fixed insurance premium. These products are not bespoke enough to provide for such a complex set of risks.

By making asset risk and penalty risk items ineligible costs, the RAs may incentivise generation units to contract differently for their provision of variable operation and maintenance costs to ensure that they can recover these costs through the market. This is inefficient – enforcement against any units that may be submitting costs out of line with a broad licence definition is surely a far more targeted, effective way of resolving this issue.

Section VI

The change management section does not appear to resolve any of the concerns raised by respondents in the Complex Bid Offer Controls consultation – it simply states that the Regulatory Authorities *may*, but will not be obliged to consult generation licence holders if they wish to direct changes to the document.

Given that the BMPCOP is effectively imposing a price control on all generation licence holders, this is a very limited standard of governance that the Regulatory Authorities are holding themselves accountable to – we cannot understand why this section hasn’t been strengthened given the comments from across the industry on previous consultations.