

National Grid ESO
15th February 2024

Dear Alice Beddow (cc: Dave Philips, Ruby Pelling)

On the ESO proposal for an alternative price adjustment mechanism instead of ABSVD for the Local Constraint Market (LCM)

This is a follow-up to the letter we sent on 10th January 2024 in response to the informal C16 consultation on the same proposal (also attached for reference).

Our main point then was that members do not support an approach to change in which larger issues are resolved by adjustments on a service-by-service basis.

Piecemeal change risks unintended consequences elsewhere, creating complexity and increasing operating costs for market participants. Ultimately, members feel that a strategic review by Ofgem or DESNZ will be needed to resolve new kinds of imbalance between market participants and how/ whether these new flows can be accommodated within the current settlement process.

However, given the urgency of resolving this issue (for the LCM and other future services), members would support the ESO if it were to raise an Issue (rather than a Code Modification) with Elexon to facilitate wider industry discussion. Members are confident that, with the support of Ofgem, a solution could be agreed within six months (acknowledging that any solution may take longer to implement).

We thank the ESO team for noting our feedback during the consultation webinar (16th January) and considering an Elexon-facilitated approach. Energy UK supports the Local Constraint Market (LCM) as an innovative market-based approach. In line with this support, we initiated further member discussion on whether to support the proposed change as a short-term measure applicable only to the LCM.

However, members did not agree that the change would be neutral but instead one that risked disadvantaging suppliers. One party being disadvantaged by the actions of another in this way was viewed as counter to the principle of balance responsibility. For this reason and the reasons set out below, Energy UK does not support the proposal.

Suppliers could be disadvantaged via the proposal in any or all of the following ways::

1. Demand is not additional

The purpose of ABSVD is not to confer advantage but to bring the supplier back to a neutral imbalance position. Whilst demand turn-up will entail the consumer consuming more units within the specified period, this demand, more often than not, will be *time-shifted* rather than *additional*. Here the supplier may need to cover the cost of the imbalance without additional revenue from higher consumption.

Even where demand is *additional* rather than *time-shifted*, the supplier could lose out in either of the following situations:

2. Turn-up is via a low-price tariff

The majority of domestic turn-up will come from larger automated loads such as electric vehicle charging. Tariffs for overnight charging can be very low and therefore any profit here may be outweighed by the cost of resolving any subsequent imbalance.

3. Short market and high imbalance price

Whilst the LCM is usually only called when there is excess supply (market long, low imbalance price), it can also be called when there is a local surplus (creating a thermal constraint) within a wider context of national shortage. This would risk a high imbalance price that could outweigh any profit from additional demand.

In all of these scenarios, the supplier will be disadvantaged by the actions of another participant. As such, the proposal is not viewed to be neutral or fair for all participants, and so members opted not to back the specific proposal.

Members included the following comments in response to specific consultation questions:

8. Do you believe consumer LCM imbalances should be corrected via ABSVD for demand turn-up providers as per existing C16 arrangements?

It was suggested that, in addition to being an incremental approach to a wider issue, the proposed solution is a partial solution and the reallocations process will make it difficult for participants to understand the relevant energy flows involved.

9. Do you have any feedback on the potential proposed (LCM Provider-optional) compensation alternative to ABSVD? Please provide rationale.

Members support the principle that providers should not pay imbalance for participating in an ESO service to support the grid.

Thank you for providing us with the opportunity to respond.

Yours sincerely

Naomi Baker
Senior Policy Manager