CUSC Workgroup Consultation Response Proforma

CMP345: 'Defer the additional Covid BSUoS costs'

Industry parties are invited to respond to this consultation expressing their views and supplying the rationale for those views, particularly in respect of any specific questions detailed below.

Please send your responses to cusc.team@nationalgrideso.com by **5pm** on **3 June 2020**. Please note that any responses received after the deadline or sent to a different email address may not receive due consideration by the Workgroup.

If you have any queries on the content of this consultation please contact Paul Mullen at paul.j.mullen@nationalgrideso.com or cusc.team@nationalgrideso.com.

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CMP345

For reference the applicable CUSC Charging objectives are:

Relevant Objective
(a) That compliance with the use of system charging methodology facilitates effective competition in the generation and supply of electricity and (so far as is consistent therewith) facilitates competition in the sale, distribution and purchase of electricity;
(b) That compliance with the use of system charging methodology results in charges which reflect, as far as is reasonably practicable, the costs (excluding any payments between transmission licensees which are made under and accordance with the STC) incurred by transmission licensees in their transmission businesses and which are compatible with standard licence condition C26 requirements of a connect and manage connection);
(c) That, so far as is consistent with sub-paragraphs (a) and (b), the use of system charging methodology, as far as is reasonably practicable, properly takes account of the developments in transmission licensees' transmission businesses;
(d) Compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency. These are defined within the National Grid Electricity Transmission plc Licence under Standard Condition C10, paragraph 1 *; and
(e) To promote efficiency in the implementation and administration of the CUSC arrangements

Please express your views regarding the Workgroup Consultation in the right-hand side of the table below, including your rationale.

CMP345 - Standard Workgroup Consultation questions		
1	Do you believe that the CMP345 Original Proposal better facilitates the Applicable CUSC Charging Objectives?	No, the Original proposal does not facilitate the Applicable Objects a) Negative – During the periods of low demand, the share of demand is more residential than usual, as I&C and SME business have reduced or closed down completely, while residential demand has increased due to people remaining at home. The original assumes that demand will be back to expected levels next year, meaning a greater proportion of the demand volume will be commercial in nature. Since suppliers often have different business models and specialise in I&C versus residential demand, there are suppliers who will face an increase in BSUoS costs next year. While they will be able to recover those costs next charging year, it creates a distortion between different types of suppliers. In a similar manner, differences between generators' hedging strategies mean some will be more exposed than others. Whilst the extra BSUoS costs could not reasonably be predicted, some generators will be overhedged compared to others, which was a commercial & competitive decision. Backdating the Modification to include May's BSUoS, which has already been paid, could recreate distortions between types of supplier, based on the nature of their contracts with consumers. b) Negative – Whilst the effectiveness of the current BSUoS charging structure to send a useful market signal is very much in doubt, the baseline is an attempt to be cost-reflective, on the assumption that costs shown by bourne by users of the system at the time. The modification must be judged against the baseline, not a recommendation made by the 1st BSUoS Task Force or presumption of a recommendation by the 2nd BSUoS Task Force. The Original Proposal removes the attempt at cost reflectivity for Covid related costs. It is not clear that the ESO can accurately identify Covid related costs, as there is

		a danger than costs related to fine weather or low demand from other reasons would be included. c) Negative – the £500m cap proposed by the original is a logical starting point, given is it describes the financial shock the industry is forecast to receive. The ESO have made it clear in Workgroup discussion that they are not able to finance the industry to that extent and that deferring costs to the next year could have significant financial implications. The ESO have a licence obligation to keep a certain level of credit and, since the legal separation from the NG Transmission, they are not the scale of organisation that can take a £500m loss. d) Neutral e) Negative – The £500m figure was reached as a result of comparing recent forecasts. There is a real chance that the difference between pre-Covid forecasts and the latest will increase beyond £500m, in which case there will probably be follow-up Code Modifications to attempt to alter the codified figure. Any such modifications will largely consist of discussions around the suitable amount that have already taken place and are likely to be proposed as Urgent.
2	Do you support the proposed implementation approach for CMP345?	No. It seems reasonable to backdate the solution to apply from 1st June onwards, but May's BSUoS has already been issued and paid. The manual process that would be required to issue credit notes would be difficult for the ESO, as well as a high risk of error. It would also create confusion for suppliers who charge BSUoS as a pass-through and those who use embedded generation to net off their BSUoS cost. I understand the point of the defect is not just parties' ability to pay, but since parties have been able to pay May's BSUoS, clumsy and rushed intervention seems inappropriate.
3	Do you have any other comments?	It appears that the heart of the defect is about socialisation of BSUoS as cost recovery, with the Covid situation throwing the need for such a change into stark relief. Whilst that may be the case, as many parties believe BSUoS does not work as currently structured, attempting to partially-fix a long-standing issue so quickly does not seem appropriate, especially given the work of the 2nd BSUoS Task Force. I recognise that the Proposer is not attempting to change BSUoS as a whole, merely the unprecedented additional Covid costs,

		but identifying those costs in a robust manner is extremely difficult. Ofgem published an open letter[1] in 2nd June 2020, describing extended payment schemes across electricity and gas and this Modification should be viewed in relation to Ofgem's intention, as shown in that letter. The Original is not compatible with the broad criteria described in a number of ways: ○ The letter talks of "*suppliers and shippers*" – Ofgem do not appear to believe generators are at risk. The Original would affect all parties and would not be able to distinguish between types of Users. ○ The letter solely addresses "*temporary relaxation of payment terms for suppliers and shippers*", which is the Extended Payment options, not socialisation of unexpected costs. ○ The request is for network companies to do it through the ENA, with Code modifications if necessary. I believe this approach would be best to avoid overlaps/wider consequences and generally keep a more coherent view across charges. This Mod was raised (as far as I'm aware) independently from those discussions, and so may not fit in. There may be unintended interactions with this Original and any support schemes proposed by the ENA. It seems likely that Ofgem would want a view of all support that could be made available before making a decision, which puts the Urgent timeline at risk. ○ The proposed support from the ENA "*cannot be used by suppliers and shippers who have an investment grade credit rating*". All options under discussion in the Mod would be applied/available to all parties. The Extended Payment Terms options could be developed to include eligibility criteria but agreeing suitable criteria within the proposed timeline will be difficult. Any options that affect the calculation of the BSUoS tariff will naturally affect all parties, regardless of credit rating or need. ○ The payment holiday proposed is a 3 month period. The closest to that was the ESO's suggestion of a 5-month period, or deferral within the calendar year. The Original will not start to recover costs until 6 months after the lasts costs were incurred. ○ There is explicit mention of a cap, that sounds like it has already been agreed by Ofgem:

[1] https://www.ofgem.gov.uk/system/files/docs/2020/06/open_letter_on_relaxing_network_charge_payment_terms_1.pdf

		"*around £350m in total for eligible electricity suppliers and gas shippers*". This is far below the Original's starting point of £500m for BSUoS alone. ○ "*any deferred payments be repaid by the end of March 2021 with instalments payable prior to that deadline*" The Original proposal would not start to repay the ESO until after that date. With a sunset clause, the Extended Payment Term options could meet that condition. ○ Ofgem's intention is that these schemes would be "*a last resort*" – no options other than the Extended Payment Terms options have an opt-in/opt-out ability and the Original will be applied immediately, without knowing the eventual materiality of the requirement to delay/defer costs.
4	Do you wish to raise a Workgroup Consultation Alternative Request for the Workgroup to consider?	Yes, we will be raising an alternative in line with Extended Payments (other), as described in the Workgroup Consultation.
Specific Workgroup Consultation Questions		
5	Do you believe it is necessary to define Covid related costs for the purposes of BSUoS charging as a result of this Modification proposal? Please provide rationale to support your response.	Since the intention is not to change "business as usual" BSUOS, then there is a need to identify Covid related costs or identify a reasonable proxy that can be used. These costs will be difficult to forecast, so any identification method needs to be ex-post or suitably flexible that it can be adjusted with changing forecasts. The practicalities of identifying individual costs are significantly challenging, requiring strict criteria (for transparency) but also judgement. For example, balancing Mechanism actions may be taken for multiple reasons; low transmission demand is driven by Covid but also weather conditions; ancillary services sit in a suite designed to complement each other and work efficiently together, so it is not always suitable to treat them differently. By not identifying covid related costs appropriately, we risk affecting "business as usual" BSUoS, which is a wider scope than this Modification proposes and should not be done without significant industry consultation.
6	Do you agree with the Original Proposal (and each of the potential alternatives) as to what constitutes Covid related costs? Please provide rationale to support your response.	Attempting to flag certain costs and actions as Covid related is extremely difficult for the ESO and almost impossible to make transparent to the industry. The 18GW suggested by the proposer seems like a reasonable point at which to define dramatic low demand, based on the information provided by the ENCC. There is a concern that transmission demand

		may go below 18GW as a result of other factors than Covid, so the proposed definition may include costs than are only marginally covid related. The number of balancing actions between taken at any point in time, and the justification for each one to enable flagging as Covid related, would create a significant administrative burden on the ESO, at a time when they are working under already taxing conditions. However, the alternate suggestion of a flat 30% appears to be based more on the financial implications, rather than an attempt at an accurate assessment of the additional costs.
7	Do you think any deferral of Covid costs should be i) within the 2020/2021 Charging Year only, ii) deferred to the 2021/2022 Charging Year or iii) deferred to 2022/2023 Charging Year or iv) deferred equally across the 2021/2022 and 2022/2023 Charging Years? Please provide rationale to support your response.	Deferral of costs will create a cost for the ESO, as they must finance the underrecovery. A shorter deferral period will naturally minimise those costs and thus reduce the extra cost to the consumer that will result from any intervention. With the 2nd BSUoS Task Force due to report in September, the future of BSUoS is quite uncertain and solutions that extend beyond April 2022 may have unintended circumstances. Deferring within year gives the greatest protection to the ESO and requires less assumption about the nature of BSUoS in the future. It does, however, assume that there will be some predictability in the general BSUoS level later in the year, that would allow parties to recover the costs. If the Covid situation should continue into the winter, the higher BSUoS costs would be exacerbated. Ultimately, the uncertainty around whether costs can be recovered depends on the level of demand and society's recovery, which will remain unclear for some time, including into 2021.
8	Do you consider it appropriate to smear the entire deferred Covid costs equally across the whole of a Charging Year e.g. 2021/2022 or target the deferred Covid costs to the equivalent Settlement Periods in 2020/21 in which Covid costs arose? If the charge was to be applied equally across a Charging Year should that be on a per Settlement period only basis or on a per MWh basis? Please	Deferring costs to identifiable Settlement Periods provides opportunities to game using BSUoS and could well have impacts on the wholesale market. For instance, if the majority of the costs are to fall in late summer, forward trades would reflect those predicted costs, even though the costs were incurred this year. If costs are to be smeared, in order to socialise the cost, it then becomes a question of fairness. Socialised costs are recovered mainly through Transmission Demand Residual, but there is no way to include the additional BSUoS costs into the TDR in the time available. Recovery per settlement period would provide stability for the ESO, in that they can be sure the costs will be recovered as forecast. If costs are to be recovered per

	provide rationale to support your response.	MWh, that would require a forecast of total annual MWh. If correct, that forecast would give more certainty to industry parties, as it would be the addition to the tariff without further calculation. However, given society will still be adapting to the "new normal", an accurate total annual MWh will be very difficult, leading to over or under recovery in 2021/2.
9	Do you consider it appropriate to codify a capped figure for the Covid costs to be deferred? If so, based on the information available, what value do you believe it should be? Please provide rationale to support your response.	Without a capped figure, the ESO is left open to considerable financial risk, and it became clear in the Workgroup discussions that this would not be acceptable. Judging by the alternatives put forward, Workgroup members do not consider it appropriate for the ESO to bear all the additional costs, or to provide finance to industry parties. It is not clear whether the cap should be based on how much the ESO can safely support or the unrecoverable cost described in the defect. If a single cap is proposed that is less than the total forecast unexpected costs, such as the Extended Payment Terms – ESO suggestion, some users may be incentivised to use the payment holiday before the cap is reached, whether or not they strictly need to, which would give them an advantage over their competitors who 'play fair' and don't use the payment holiday if they don't have to. If a cap is set that turns out below the actual costs (either because of under-forecasting or as a conscious decision), the situation the Modification is looking to avoid will be postponed, and the unexpected costs will occur in the summer, rather than spring.
10	Do you agree that the period to be covered for deferral of Covid costs should be limited to those incurred up to 31 August 2020?	The argument that these unexpected costs are inherently "unrecoverable" seems to be based on that fact that suppliers offer fixed tariffs and generators trade in at least seasonally in the wholesale market. It is not clear that Suppliers would be able to reset their tariffs, or generators have sufficient opportunity to trade with this knowledge by September. The forecast figure of £500m comes from a short-term forecast by the ESO, but there is no strong evidence to suggest that demand will be back to previous seasonal levels by September, leaving industry parties in a similar situation to that currently.
11	Do you think the impact of the Covid pandemic on BSUoS is sufficient to justify a different approach to charging BSUoS in advance of the second BSUoS	There has been significant industry discussion on BSUoS without a clear consensus being reached over the last few years. Ofgem gave the 2nd Task Force a clear brief of the questions and the criteria by which to judge solutions. Those CUSC applicable objectives are

	Taskforce completing its work? Bearing in mind the short timescale for implementation do you agree with the approach in the option outlined above? Please provide a rationale with your response.	not equivalent to the TCR criteria and so should be not be used interchangeably. The Workgroup does not have the same level of representation across the industry as the Task Force and an incredibly tight timeline. Changing the charging structure of BSUoS could have significant impacts across the industry and that scale of change should be done in a considered manner with wide-ranging consultation, not in a month. It would be not reassuring to the industry to have CMP345 put an ongoing solution in place by changing the charging structure of BSUoS, only to have the 2nd BSUoS Task Force recommend a different structure to come in a year or so later. It is worth remembering that the BSUoS Task Force will provide recommendations only, and any changes will be the result of an Ofgem decision. Changing BSUoS as a result of CMP345 may limit Ofgem's ability to act on recommendations from the Task Force.
12	Do you agree with the financing options set out above? Is there another way? Please provide rationale to support your response.	I do not believe the prescribed rate of 8.1% from 6.6.6 of the CUSC would be appropriate. That rate is to prevent the ESO from developing an unexpected deficient and penalise parties who do not pay anticipated network charging invoices on time. The interest charged should be reflective of the actual financing costs the ESO incur, as close as possible, to allow the industry as a whole the make the most economically efficient decisions and reduce the total cost of this intervention to end consumers. It is possible that the best estimate of actual financing costs come close to that figure, but the Authority and government may consider it best to provide support to the industry through assisting the ESO with finance options, rather than pick winners/losers through more targeted actions. I agree with the principle that the role of the ESO is not to provide cheap finance for parties that are struggling, but overrecovery of financing costs through a fixed & unreflective rate with create additional distortions, such as those noted by the Workgroup that parties in receipt of the reconciliation will not be those who have overpaid.
13	Do you agree with the impacts we have set out in this Workgroup Consultation? Have we missed any impacted parties? Please provide details to support your response.	Large generators who have hedged out and are unable to adjust their position will have presumably also agreed a higher power price, as the drop in demand was not anticipated in any prices. The material impact for these

		generators is therefore less than might be immediately assumed. This change will have a disproportionately negative effect on small renewable generators, at a time when government is intending to look towards a green recovery and make up for lost time from COP26. When CMP333 comes into effect in April 2021, there will be no way for those generators to recover the lost revenue, as they will be incapable of accessing the deferred costs. Given that the forecast high costs have been made public to the industry, there will be parties who have acted on those forecasts in good faith and will find themselves disadvantaged if this Modification is approved. It seems unfair that those parties should lose out by acting on information they were given by the ESO