

**CUSC Code Administrator Consultation Response Proforma****CMP345 'Defer the additional Covid -19 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](mailto:cusc.team@nationalgrideso.com) by **3pm on 12 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 Panel.

If you have any queries on the content of this consultation, please contact Paul Mullen [paul.j.mullen@nationalgrideso.com](mailto:paul.j.mullen@nationalgrideso.com) or [cusc.team@nationalgrideso.com](mailto:cusc.team@nationalgrideso.com).

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**For reference the applicable CUSC objectives are:**

- 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. *Promoting efficiency in the implementation and administration of the CUSC arrangements.*

*\*Objective (d) refers specifically to European Regulation 2009/714/EC. Reference to the Agency is to the Agency for the Cooperation of Energy Regulators (ACER).*

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

Standard Code Administrator Consultation questions		
1	Do you believe that the CMP345 Original solution, WACM1, WACM2, WACM3, WACM4, WACM5, WACM6, WACM7 or WACM8 better facilitates the Applicable CUSC Objectives?	<p><u>Original</u></p> <p>As set out in the CMP345 proposal form, the Original proposal (as well as WACMs 2, 5 and 8 as we set out below) is positive in terms of Applicable Objective (a) as it will ensure that BSUoS paying market participants are not adversely impacted by the costs incurred by the ESO to manage the transmission system during the unprecedented Covid event. Deferral of BSUoS will better facilitate 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.</p> <p>The Original is neutral in terms of Applicable Objective (b).</p> <p>The Original is positive in terms of Applicable Objective (c) as it will ensure that the BSUoS methodology properly takes account of the developments in transmission licensees’ transmission businesses arising from the unprecedented Covid event.</p> <p>The Original is neutral in terms of Applicable Objective (d).</p> <p>The Original is neutral in terms of Applicable Objective (e).</p> <p><u>WACM1 – Extended Payment Terms (6 months)</u></p> <p>This WACM <b>does not address</b> the core element of the CMP345 defect, as noted on page 5 of the proposal, namely:</p> <ul style="list-style-type: none"> <li>○ <i>“The effect of recovering the additional costs arising from the unprecedent Covid-19 event from those parties under the status quo arrangements would be profound as they will be unable to fully recover the amounts via retails tariffs (for Suppliers) given fixed price contracting and price caps, or via wholesale prices (for Generators) given that most sales for May to August generation have already been made before indications of these significant BSUoS cost increases over forecast were given by the ESO.”</i></li> </ul> <p>As noted at the bottom of page 16 of this consultation document <i>“The first BSUoS Task Force concluded that it was</i></p>

*not practical to charge [BSUoS] cost reflectively and BSUoS should be treated as cost recovery.”*

Given that the BSUoS task force has determined that BSUoS should be treated as cost recovery, it therefore follows that the wider societal effects from Covid that gave rise to the increase in electricity system costs, should be recovered from the parties who are, according to the 1<sup>st</sup> BSUoS Taskforce, in the correct position to ultimately pay those costs. This can only be done if the deferral period allows for this; i.e. deferring cost recovery beyond the current 2020/21 Charging Year.

WACM1 therefore is not positive in terms of Applicable Objective (a) as it fails to ensure that BSUoS paying market participants are not adversely impacted by the costs incurred by the ESO to manage the transmission system during the Covid event. It will not better facilitate effective competition in the generation and supply of electricity and (so far as is consistent therewith) not facilitate competition in the sale, distribution and purchase of electricity.

WACM1 is neutral in terms of Applicable Objective (b).

WACM1 is not positive in terms of Applicable Objective (c) as it does not ensure that the BSUoS methodology properly takes account of the developments in transmission licensees' transmission businesses arising from the unprecedented Covid event.

WACM1 is neutral in terms of Applicable Objective (d).

WACM1 is neutral in terms of Applicable Objective (e).

#### WACM2 – Apply a £15/MWh BSUoS price cap

WACM2 is positive in terms of Applicable Objective (a) by limiting the extent to which BSUoS paying market participants are adversely impacted by the costs incurred by the ESO to manage the transmission system during the unprecedented Covid event. It will better facilitate 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.

However, compared to the Original, WACM2 does not fully ensure that all the Covid costs incurred by the ESO to manage the transmission system in these uncertain times are fully recovered.

WACM2 is neutral in terms of Applicable Objective (b).

WACM2 is positive in terms of Applicable Objective (c) as it will ensure that the BSUoS methodology more properly takes account of the developments in transmission licensees' transmission businesses arising from the unprecedented Covid event.

WACM2 is neutral in terms of Applicable Objective (d).

WACM2 is neutral in terms of Applicable Objective (e).

WACM3 - Deferral of costs of ODFM and nuclear Contract(s) to October 2020 – January 2021/February 2021 with daily reporting

WACM3 is not better at facilitating Applicable Objective (a) as it **does not address** the core element of the CMP345 defect (as noted on page 5 of the proposal and reproduced under 'WACM1' above) and therefore will not better facilitate effective competition in the generation and supply of electricity and (so far as is consistent therewith) not facilitate competition in the sale, distribution and purchase of electricity.

WACM3 is neutral in terms of Applicable Objective (b).

WACM3 is not positive in terms of Applicable Objective (c) as it does not ensure that the BSUoS methodology properly takes account of the developments in transmission licensees' transmission businesses arising from the unprecedented Covid event.

WACM3 is neutral in terms of Applicable Objective (d).

WACM3 is neutral in terms of Applicable Objective (e).

WACM4 - Deferral of costs of ODFM and nuclear Contract(s) to October 2020 – January 2021/February 2021 with weekly reporting

WACM4 is not better at facilitating Applicable Objective (a) as it **does not address** the core element of the CMP345 defect (as noted on page 5 of the proposal and reproduced under 'WACM1' above) and therefore will not better facilitate effective competition in the generation and supply of electricity and (so far as is consistent therewith) not facilitate competition in the sale, distribution and purchase of electricity.

WACM4 is neutral in terms of Applicable Objective (b).

WACM4 is not positive in terms of Applicable Objective (c) as it does not ensure that the BSUoS methodology properly takes account of the developments in transmission licensees' transmission businesses arising from the unprecedented Covid event.

WACM4 is neutral in terms of Applicable Objective (d).

WACM4 is neutral in terms of Applicable Objective (e).

WACM5 - Cost Deferral of £250m to 2022/23.

WACM5 is positive in terms of Applicable Objective (a) by ensuring that BSUoS paying market participants are not adversely impacted by the costs incurred by the ESO to manage the transmission system during the unprecedented Covid event. It will better facilitate 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.

However, compared to the Original, WACM5 has the added attribute of affording more time for market participants to more fully recover the Covid costs (in a similar fashion to how other, non BSUoS, Covid related cost deferrals are being treated (such as those associated with Ofgem's 2<sup>nd</sup> June 2020 open letter and the LCCC).

In this regard we are mindful of the voting statement from one of the Workgroup members<sup>1</sup> which noted that:

- "...these [CMP345] changes could exacerbate future problems. As other reliefs end (delayed payment of CfDs, DUoS, etc.) and bills fall due (ROCs, etc.) there is a risk of multiple party failures creating substantial costs for the remaining parties added to the deferred BSUoS costs. While helping companies in the short term is sensible, storing up too many price shocks does not seem sensible."

Given the case that is being made here by the Workgroup member and others in the Workgroup Consultation responses that there are a number of other (non BSUoS) Covid related costs that are being deferred to 2021/22; and that storing up too many price shocks into one Charging Year (2021/22) does not seem sensible; there is a case to be made that a deferral of the Covid related costs within BSUoS should be delayed by

<sup>1</sup> Lisa Waters, see pages 29-30 of Annex 11.

a further Charging Year to 2022/23 (from 2021/22 as, for example, is proposed in the Original).

In addition, we believe that deferring to 2022/23 is supported by consideration of the following issues:

- Within the non-domestic sector, the majority of customers contract on fixed term tariffs which do not permit adjustments for unforeseen additional costs, including Covid related BSUoS costs;
- Continued uncertainty regarding Covid related BSUoS costs means it is impossible for suppliers to determine how to appropriately price this risk either when contracting with new, or recontracting with existing customers, typically for a fixed term period;
- Supplier approaches will depend on their risk appetite and view of the certainty of BSUoS costs, which are even more unpredictable, given Covid, than usual;
- Some suppliers may factor in a premium to accommodate the additional uncertainty they attribute to Covid related risk which would be recovered from a smaller customer group, to the detriment of those customers. This could be as much as an additional £6-8MWh based on the ESO's latest BSUoS forecast;
- 2022/23 deferral will reduce the likelihood of supplier risk premia increasing in the current and for future years – therefore a benefit to all consumers;
- Covid issue may not be gone by end of 2020/21 – the hardship of increasing other Covid costs to consumers in 2021/22 may be additive to ongoing consumer pain – therefore longer deferral is a benefit to all consumers;
- Suppliers may decide to take an unsustainable approach to pricing which will have adverse consequences for the entire market, and, ultimately, all customers, if Covid related BSUoS costs do outturn at the expected additional ~£500m, which is not yet certain, and there is no deferral. This is because they will, quite simply, be unable to absorb all of these additional costs within the current or even the next financial year and this could lead to an increased risk to the market of supplier failures; and
- Suppliers are being afforded relief on the recovery of distribution network charges during the financial year 2020/21. This flexibility, which is intended to provide suppliers with some breathing space during this

challenging period, will be of limited benefit if Covid related BSUoS costs are not also deferred beyond 2020/21.

WACM5 is neutral in terms of Applicable Objective (b).

WACM5 is positive in terms of Applicable Objective (c) as it will ensure that the BSUoS methodology properly takes account of the developments in transmission licensees' transmission businesses arising from the unprecedented Covid event.

WACM5 is neutral in terms of Applicable Objective (d).

WACM5 is neutral in terms of Applicable Objective (e).

#### WACM6 – Extended Payment Terms (5 months) for 30% BSUoS Charges

WACM6 is not better at facilitating Applicable Objective (a) as it **does not address** the core element of the CMP345 defect (as noted on page 5 of the proposal and reproduced under 'WACM1' above) and therefore will not better facilitate effective competition in the generation and supply of electricity and (so far as is consistent therewith) not facilitate competition in the sale, distribution and purchase of electricity

WACM6 is neutral in terms of Applicable Objective (b).

WACM6 is not be positive in terms of Applicable Objective (c) as it does not ensure that the BSUoS methodology properly takes account of the developments in transmission licensees' transmission businesses arising from the unprecedented Covid event.

WACM6 is neutral in terms of Applicable Objective (d).

WACM6 is neutral in terms of Applicable Objective (e).

#### WACM7 – Within Year Cost Deferral of £250M

WACM7 is not better at facilitating Applicable Objective (a) as it **does not address** the core element of the CMP345 defect (as noted on page 5 of the proposal and reproduced under 'WACM1' above) and therefore will not better facilitate effective competition in the generation and supply of electricity and (so far as is consistent therewith) not facilitate competition in the sale, distribution and purchase of electricity

WACM7 is neutral in terms of Applicable Objective (b).

WACM7 is not be positive in terms of Applicable Objective (c) as it does not ensure that the BSUoS methodology properly takes account of the developments in transmission licensees' transmission businesses arising from the unprecedented Covid event.

WACM7 is neutral in terms of Applicable Objective (d).

WACM7 is neutral in terms of Applicable Objective (e).

#### WACM8 – Cost Deferral of up to £500m to 2022/23

WACM8 is, like the Original upon which it is based, positive in terms of Applicable Objective (a) by ensuring that BSUoS paying market participants are not adversely impacted by the costs incurred by the ESO to manage the transmission system during the unprecedented Covid event. It will better facilitate 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.

However, compared to the Original, WACM8 has the added attribute of affording more time for market participants to more fully recover the Covid costs whilst also taking account of other, non BSUoS, Covid related cost deferrals (such as those associated with Ofgem's 2<sup>nd</sup> June 2020 open letter and the LCCC).

In this regard we are mindful of the voting statement from one of the Workgroup members<sup>2</sup> which noted that:

- "...these [CMP345] changes could exacerbate future problems. As other reliefs end (delayed payment of CfDs, DUoS, etc.) and bills fall due (ROCs, etc.) there is a risk of multiple party failures creating substantial costs for the remaining parties added to the deferred BSUoS costs. While helping companies in the short term is sensible, storing up too many price shocks does not seem sensible."

Given the case that is being made here by the Workgroup member and others in the Workgroup Consultation that there are a number of other (non BSUoS) Covid related costs that are being deferred to 2021/22; and that storing up too many price shocks into one Charging Year (2021/22) does not seem

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<sup>2</sup> Lisa Waters

sensible; there is a case to be made that a deferral of the Covid related costs within BSUoS should be delayed by a further Charging Year to 2022/23 (from 2021/22 as, for example, is proposed in the Original).

In addition, we believe that deferring to 2022/23 is supported by consideration of the following issues:

- Within the non-domestic sector, the majority of customers contract on fixed term tariffs which do not permit adjustments for unforeseen additional costs, including Covid related BSUoS costs;
- Continued uncertainty regarding Covid related BSUoS costs means it is impossible for suppliers to determine how to appropriately price this risk either when contracting with new, or recontracting with existing customers, typically for a fixed term period;
- Supplier approaches will depend on their risk appetite and view of the certainty of BSUoS costs, which are even more unpredictable, given Covid, than usual;
- Some suppliers may factor in a premium to accommodate the additional uncertainty they attribute to Covid related risk which would be recovered from a smaller customer group, to the detriment of those customers. This could be as much as an additional £6-8MWh based on the ESO's latest BSUoS forecast;
- 2022/23 deferral will reduce the likelihood of supplier risk premia increasing in the current and for future years – therefore a benefit to all consumers;
- Covid issue may not be gone by end of 2020/21 – the hardship of increasing other Covid costs to consumers in 2021/22 may be additive to ongoing consumer pain – therefore longer deferral is a benefit to all consumers;
- Suppliers may decide to take an unsustainable approach to pricing which will have adverse consequences for the entire market, and, ultimately, all customers, if Covid related BSUoS costs do outturn at the expected additional ~£500m, which is not yet certain, and there is no deferral. This is because they will, quite simply, be unable to absorb all of these additional costs within the current or even the next financial year and this could lead to an increased risk to the market of supplier failures; and
- Suppliers are being afforded relief on the recovery of distribution network charges during the financial year

		<p>2020/21. This flexibility, which is intended to provide suppliers with some breathing space during this challenging period, will be of limited benefit if Covid related BSUoS costs are not also deferred beyond 2020/21.</p> <p>WACM8 is neutral in terms of Applicable Objective (b).</p> <p>WACM8 is positive in terms of Applicable Objective (c) as it will ensure that the BSUoS methodology properly takes account of the developments in transmission licensees' transmission businesses arising from the unprecedented Covid event.</p> <p>WACM8 is neutral in terms of Applicable Objective (d).</p> <p>WACM8 is neutral in terms of Applicable Objective (e).</p>
2	Do you support the proposed implementation approach?	<p>We note the various proposed implementation approaches for the Original and eight WACMs set out in the consultation document and support them (although, as noted in our response to Q1 above, we do not necessarily support, per se, all the WACMs themselves).</p>
3	Do you have any other comments?	<p>We have reviewed the industry responses to the Workgroup consultation and have identified several criticisms of the CMP345 proposal (to the Original as well as some or all of the WACMs). We would like to take this opportunity to address these criticisms and we therefore make the following comments about those issues (shown below underlined) that have been raised in the discussions to date.</p> <p><u>Disputed Claim: Increased BSUoS embedded benefit not a windfall gain, as offset by lower power prices and other financial pressures</u></p> <p>It seems highly improbable that the embedded generator beneficiaries of the Covid related higher BSUoS price would have forecast the extra ~£500M revenue level (that came to light on 15<sup>th</sup> May 2020). Instead, this is now likely to arise in a timescale of relevance to standard business planning as a result of the much higher BSUoS prices. It is believable that some small increase in revenue may have been forecast, but not anything like the whole amount by a long way as the pandemic and its effects on the GB electricity system was broadly not predictable until March 2020 at the earliest when, for example, the ESO looked into this scenario.</p>

Therefore, the argument that the Covid related higher BSUoS price is not a windfall gain for embedded generators is undermined principally by the fact that the increase in the embedded benefit revenue was not forecastable and it is not delivered by action by those parties collecting the revenue. Hence, by definition, the Covid related higher BSUoS price is a windfall gain for embedded generators.

Many of the cost pressures cited in this criticism are not relevant to the case for a windfall gain for embedded generators as these costs are similarly faced by Transmission connected generators who will not receive a windfall gain but will, by having to pay the Covid related higher BSUoS price themselves, face a windfall loss and are in direct competition with embedded generators.

Additionally, some of the effect of reduced revenue through power prices is offset, for embedded generators (but not transmission connected generators) by access to and income from the brand new Optional Downward Flexibility Management (ODFM) product the ability to offer – a windfall gain for them as they could not have predicted that such a significant new revenue stream would emerge (only as a result of Covid) within less than ten days in early May 2020.

Disputed Claim: Retrospective or sudden change to the rules in response to unforeseen events undermines investor and innovator confidence in the market

The increase in the Covid related cost of BSUoS (as forecast by the ESO at up to ~£500M) has arisen, in our view, as a direct consequence of Government<sup>3</sup> intervention to a global public health emergency. This is a view, we think, that is shared by others, such as Tata Steel who in their Workgroup consultation response at Q8 noted that “*We understand the current issues are caused by a wide-spread societal issue*”.

In our view investor confidence is undermined more if the industry does not demonstrate the ability to respond appropriately, proportionately, reasonably and quickly where unprecedented circumstances demand it.

Furthermore, as BOC noted in their answer to Q3 in the Workgroup consultation<sup>4</sup> there are potentially unintended

<sup>3</sup> As with the consultation document, where we refer to ‘Government’ in this response we mean the UK Government as well as the Scottish and Welsh Governments, all three of which have a direct bearing on the societal response to the Covid pandemic in GB.

<sup>4</sup> “I&C demand is lower, but still present as baseload overnight & at weekends. Outsize BSUoS costs (which can be qualitatively expected if not accurately forecast) at high renewables/low demand are diluting and at times reversing the signal to shift power consumption to low system demand periods – and therefore adding to system cost. This is happening now.”

consequences, in terms of further extra BSUoS costs (and system security implications?) if exceptional and unprecedented levels of BSUoS occur and are not quickly addressed as this could lead to further demand suppression (in response to the very high level of BSUoS at weekends / overnights) which further exacerbates the system management issues for the ESO.

There is now a precedent that deferral of Covid related costs to be funded by future taxpayers which has been set throughout much of the Government's response to Covid as it made significant interventions in the economy (e.g. increase in public borrowing to fund furlough schemes, Treasury-backed loans, additional testing & PPE costs etc., etc.).

Risk premia are likely to rise to the detriment of future consumers if investors do not have the confidence that exceptional (and unpredictable) costs arising from global public health interventions can be mitigated by allowing those Covid related costs (of up to ~£500M) only to be recovered at a later date; whilst allowing them to focus on running day to day to aid society's response to the intervention (and continue to pay ~£1,500M of the non Covid related BSUoS costs in 2020/21).

Disputed Claim: The change is an attempt to grab and transfer value from embedded generators to T-generators and Suppliers

BSUoS is a cost recovery mechanism as concluded by the 1<sup>st</sup> BSUoS Taskforce. The CMP345 Original (along with WACMs 2, 5 and 8) simply aims to ensure that the additional BSUoS costs arising from Government led societal response to Covid can be recovered from consumers rather than having to be borne by producers and suppliers. Their role in this is to recover costs incurred by the ESO (in managing the GB electricity system in these uncertain time) rather than incorporate exceptional and unprecedented BSUoS costs arising from a global public health emergency into the underlying basis of their business proposition to consumers.

The Covid effect on the GB electricity system arises from multiple direct Government interventions requiring a societal response to manage a global public health emergency. The rise in BSUoS costs related to Covid are unprecedented and unforecastable with generators and suppliers being unable to revise the prices at which they sell in order to recover these exceptional increases in BSUoS costs. No mechanism exists for generators and suppliers to risk manage BSUoS costs effectively for global public health emergency events.

Disputed Claim: Deferral of costs does not target or expose the correct set of Suppliers (consumers) or Generators; I&C demand is suppressed currently but would have to pay in the future; new actors (both Gen and Sup) would be exposed to historic costs unrelated to their participation in the market

The 1<sup>st</sup> BSUoS Taskforce concluded that BSUoS should be a cost recovery mechanism for costs to manage the system; rather than a cost reflective incentive mechanism. In this context, a debate about who pays when is less pertinent than ensuring that the exceptional Covid related costs of managing the GB system are recovered from those who ultimately benefit from the system's continued functioning – namely consumers.

The increased future level of BSUoS created by deferral of the Covid related costs will be faced by all actors in the market who will be fully aware of them and able to pass them through in their prices. This does not disadvantage new entrants as market prices (which the new entrants and incumbents alike will enjoy) will reflect the increased costs which will be recovered by being passed on to consumers. This is analogous to the other Covid related costs which are being covered through Government borrowing and which will ultimately be paid by future tax-payers.

Consumers will ultimately pay for those system management Covid related costs in a way that is not directly related to their use of energy during the crisis period. This is no different to future taxpayers paying for the substantial Government intervention for those Covid related costs for public goods and services. It is an appropriate societal response to a global public health emergency to deal with the matter at hand by exceeding spending limits in order to cope with the consequences and pay for it another day.

Most Industrial and Commercial (I&C) consumers have not been forced to switch-off their electricity demand entirely during the Covid event but face the Covid related higher BSUoS cost. This was, for example, highlighted by UK Steel in their answer to Q3 in the Workgroup consultation where they stated that "*The additional BSUoS cost is significant and unduly penalising Energy Intensive Industries, such as the steel sector*".

Very large I&C consumers (including, for example, BOC, who produce critical gases for medical purposes and who responded to the Workgroup consultation) are directly exposed to BSUoS prices, have been vital to the response to Covid and have continued to operate at the same or similar

levels of demand. Failure to defer the significant system management costs arising from the Covid event both penalises those consumers for their continued operation and support to the country's effort to manage the pandemic; and perversely incentivises them to switch off, thus exacerbating the issue of artificially suppressed demand (and, in the case of BOC as an example, undermining the public health response).

Disputed Claim: Concern that Code Modification process is acting to undermine policy or establish policy measures in an inappropriate place

This CMP345 modification does not seek to put in place an enduring solution to BSUoS charging. Instead, it aims to provide a one-off mechanism in the 2020/21 charging year that allows previously unidentified Covid related costs only to be managed and recovered. The bulk of BSUoS in 2020/21, at ~£1,500M, and the policy that underpins it, will be unaffected by CMP345.

It is not evident therefore that this undermines existing policy or establishes new policy. The enduring solution remains under the vires of the BSUoS Taskforce, which can take account of the solution to the one-off Covid related costs arising from an Authority decision on CMP345.

Equally, the CMP345 proposal simply uses the existing open governance process available to all Code Parties to raise and make a case for change; it is out with the remit of this change to reform the interaction between policy and Industry Codes, which is subject to a separate BEIS/Ofgem joint review.

Disputed Claim: Concern that smaller players in the market have had insufficient access and/or time to engage in the debate in the time allotted

The response to Covid has necessitated a number of changes to the industry arrangements, including the introduction of a new balancing service ODFM (without any stakeholder consultation) and a change to the emergency arrangements (GC0143, which did not involve any Workgroup) which were progressed far quicker than CMP345: which has involved seven Workgroup meetings and two industry consultations (unlike ODFM or GC0143). Similar changes have also been progressed under the gas UNC.

As part of the open governance process, all parties were able to offer candidates to join the CMP345 Workgroup; and hear and participate in the debate. For those that didn't it was a conscious choice not to.

The timescale is a function of the urgency of the issue at hand. The Code modification process, by agreement of the governing authorities, has deemed it appropriate to allow for certain issues to be expedited where the issues meet certain, published, urgency criteria determined by the Authority. Ofgem determined that an urgent timetable was appropriate for this CMP345 issue.

Disputed Claim: Suggestion by some respondents that costs were clearly indicated and forecasted by NGESO some months prior

- Historically, we have observed significant volatility between actual and forecast BSUoS costs which we have had to absorb as a supplier and generator.
- In a business as usual context we consider the ESO's forecasting to be sub-optimal and lacking in transparency. This position is severely exacerbated as a result of the Covid pandemic, where we now have a huge increase in costs, at extremely short notice, which we will be unable to recover from our existing customers or the market.
- Suppliers and generators are expected to shoulder these costs under existing cost recovery rules.
- As yet, there has been little, if any, scrutiny of whether these costs have been efficiently incurred, nor any indication as to the route for market participants to discuss this in an open and transparent forum.

A careful examination of the ESO's forecast and timelines refutes the suggestion that these Covid related costs were clearly indicated and forecast by the ESO some months prior.

Examining the evidence from the ESO's forecast and timelines we observe the following:

- The ESO April forecast published on 17<sup>th</sup> April 2020 stated that an adjustment to electricity demand has been made to account for the Covid lockdown suppressed demands. No significant change was made to the (ESO) forecast of Constraints;
- The adjustment resulted in approximately 53p increase over the months till August 2020, including attributed to demand reduction;
- The ESO May forecast was published on 15<sup>th</sup> May 2020. This contained £427m 'Additional Costs' with no breakdown of how the costs are accumulated;

- On 21<sup>st</sup> May, six days later (and two days after CMP345 was raised) the ESO published an explanatory note<sup>5</sup> of the 15<sup>th</sup> May forecast;
- The explanatory note identified approximately £50m additional costs associated with the 'New services' but also approx. £370m over the Summer associated with Covid Low demand scenarios (primarily attributed to additional Constraint costs); and
- The additional Constraint related costs add approximately £3.50 to the Baseline + new Services BSUOS over the summer months, additional to the 53p BSUOS added in the ESO's April-20 forecast.

As stated above, we have observed significant volatility between actual and forecast BSUoS costs which we have had to absorb as a supplier and generator in a business as usual context.

The graph at the end of this Q3 shows the distribution of out-turn of BSUoS for May 2020 as compared to May 2019. This clearly shows the extent to which May 2020 BSUoS was outside the distribution expected (based on May 2019).

The average for May 2019 was £2.586 per MWh whereas the average BSUoS for May 2020 was over 133% higher at £6.043 per MWh. This difference will increase as the settlement runs progress. The data so far analysed does not include some significant costs that the ESO incurred over May 2020. It is difficult to see how such a variation of BSUoS in May 2020 could be seen to be within the range of possibility by market participants. This is in line with the variation in the ESO's own BSUoS forecasts (May 2020 vs April 2020 and preceding periods) where the jump in the expected level of BSUoS is substantially beyond what has been seen previously and which is described by the ESO as being as a result of the GB societal response to the Covid pandemic which is widely acknowledged as being unprecedented.

Specific Covid related measures (and costs) arising from the exceptionally low electricity demand in GB could not have been well signalled and forecast months in advance as, for example, neither the ~£50M nuclear contract<sup>6</sup> nor ODFM contracts (as a minimum) had been put in place nor anticipated.

<sup>5</sup> <https://data.nationalgrideso.com/backend/dataset/c0376ed7-3205-4fe2-9496-28496f1f287a/resource/9f20b9cb-1fd3-4a8f-98ee-fcd38d2d8345/download/bsuos-forecast-explainer.pdf>

<sup>6</sup> As per press reports from early May 2020.

This criticism conflates the ESO's general view that Summer demands would be reducing in certain weather conditions due to distributed generation, with the additional and unprecedented suppression of demand caused by direct Government intervention to shut down significant parts of the economy in response to a global public health emergency. They are consequences that arise from entirely different circumstances and one should not be used to justify the foretelling of the other. That is to say – the impact of low summer demand was already included in the ESO's pre Covid BSUoS forecast (and these costs therefore fall within the ~£1,500M BSUoS costs in 2020/21 that would be unaffected by CMP345) and the impact of Covid is a separate additional impact not knowable until the demand impact of the societal response to Covid was evident.

Notwithstanding this, the effect of weather conditions on any pre-Covid forecast of GB electricity demand has been directly impacted by the unanticipated positive environmental changes arising from the worldwide Covid pandemic response, as The Times 'Weather Eye' article of Saturday 9<sup>th</sup> May set out:

- "...solar power generation is booming in sparkling clear skies free of large amounts of air pollution. With the drastic cut in road traffic, industry and aircraft [due to Covid] the air is so much cleaner that it has helped to boost solar power generation and set records in the UK, Germany and Spain"; and
- "Air pollution not only cuts down sunlight with a thick haze, but also makes the solar panels dirtier and less efficient. Aerosols from gases such as sulphur dioxide also seed more cloud cover, cutting solar output further".

Therefore, the effects on electricity demand in GB of the increase in embedded solar generation output that is forecast (by the ESO in its 15<sup>th</sup> May BSUoS document) during May-August 2020 compared to the pre-Covid ESO forecast can also be attributed to the effects of Covid on solar generation output. It is entirely appropriate that these extra, Covid related, costs in terms of BSUoS are recognised as being exceptional (and not part of the ~£1,500M 'business as usual' BSUoS costs for 2020/21, which would be unaffected, for example, by CMP345 Original or WACMs 5 and 8).

Disputed Claim: Cumulative effects of other support mechanisms being discussed (and in certain cases already agreed) within the industry may provide excessive relief and defer too much risk (e.g. of Supplier failure at a future point when deferred liabilities under support schemes are due to be repaid).

None of these support mechanisms address the specific defect being addressed by CMP345 Original (along with WACMs 2, 5 and 8). That is, the impossibility of the cost recovery of the excess BSUoS, arising only from Covid, forecast by the ESO over the period April 2020 to August 2020, as a large part of the means of recovering these costs (i.e. through retail prices and through wholesale electricity market prices) is not open to the payers of BSUoS due to the nature of sales profiles that are commonplace in the Electricity Industry.

Many of those support mechanisms limit who can apply, creating a discrimination and distortion effect between different classes of parties (and even within classes of parties). Cumulative effects are therefore overplayed (or non-existent) for most players in the market.

This CMP345 Original proposal (along with WACMs 2, 5 and 8) does not discriminate in the same way; it defers the Covid related costs for all of today's BSUoS payers to a future date that enables them to recover those costs through prices.

It is not clear how it would be in either consumers' or society's interests to allow businesses operating within a critical infrastructure industry to fail in a time of crisis; either in terms of a failure or interruption to service to customers; or in terms of the unnecessary diversion of industry expertise and effort to manage the ensuing impacts (e.g. SoLR events, forced trade sales, management of default events, management of default contagion etc.)

Disputed Claim: Risk of affecting BAU BSUoS costs by not identifying Covid costs correctly; Covid costs should be carefully defined and limited to known costs, e.g. Sizewell, ODFM contracts; use of <18GW threshold creates uncertainty looking forward to 2020 into 2021 as to what will or will not be included in BSUoS prices for respective periods

We believe that the definition of Covid related costs provided for in the Business Rules (Annex 5 of the consultation document, at paragraph 3 and incorporated, for example, in the legal text for the Original and WACM8) is appropriate. It is consistent with the definition utilised by the ESO to construct its forecast of those costs (based on inclusion of new and specific contract costs and application of a low demand threshold of 18GW). It should be possible therefore to identify ongoing Covid related costs on a similar basis to the construct used by the ESO for forecasting BSUoS on 15<sup>th</sup> May 2020.

Disputed Claim: Reform of CUSC is not the appropriate route to address the issue – more appropriate to rely on direct Government support for affected Suppliers, or another mechanism that doesn't interfere in the wholesale market

It is not clear that any such support is available for Generators. The support available to Suppliers has been limited in its application as outlined in the Ofgem open letter of 2<sup>nd</sup> June. This flexibility, via relief on network charges recovery is intended to provide suppliers with breathing space during this challenging period but will be of limited benefit if BSUoS costs are not deferred beyond 2020/21.

It is, in our view, preferable for industry to provide its own response to the societal impact of the global public health emergency where possible; to ease the burden on Governmental schemes which can be better deployed in other (non-critical) sectors of the economy in those efforts to recover the UK economy; and CMP345 seeks to do just that.

In that regard, Ofgem, in its collection of information from suppliers and network companies, is uniquely placed to consider the risks faced by all market participants.

Disputed Claim: BSUoS forecasts provided by NGENSO are pessimistically high

Forecasts generally may be considered as prudent. They are the only publicly available view as to what the ESO thinks it will take to manage the unprecedented low electricity demands in GB that are arising from the societal response to the Covid event. Our proposed solution (in the Original and WACM8) would accommodate any prudence bias by the ESO in its forecasting by only deferring realised Covid defined costs, as well as applying an overall cap (up to £500M).

Disputed Claim: Not clear how BSUoS costs will evolve after August 2020 – little merit in deferring the Covid costs to a later period in anticipation that costs will be lower or less volatile in that later period

The absolute level or volatility of Covid related costs within the period that costs are deferred to is less important than the ability to allow those costs to be recovered by the affected parties. The key aim of the CMP345 Original (along with WACMs 2, 5 and 8) proposal is to ensure that unforeseeable,

Covid only related costs that could not have been reasonably predicted within a sensible timeframe can be taken into account within future prices and therefore recovered from the primary beneficiaries of system management activities, namely consumers. To be clear, the vast bulk of BSUoS costs in 2020/21 pre and post August 2020 (~£1,500M) would be unaffected by this proposed change.

If the costs related to Covid extend, unexpectedly, beyond August 2020 then with, for example, the Original and WACM8 there is the possibility that the applicable date for Covid related cost deferral (arising within 2020/21) can be extended, with the Authority's agreement, up to the end of the charging year (31<sup>st</sup> March 2021) if necessary.

Disputed Claim: Detrimental impact on the efficiency of the wholesale market by removing certain costs from one period and recovering them on a different basis in another

The CMP345 Original (along with WACMs 2, 5 and 8) proposal is a proportionate measure to address the consequences of a Government-led, societal response to a global public health emergency. The role of the market in terms of BSUoS charges is to (on behalf of the ESO) recover the costs of managing the GB electricity system from consumers who are the principal beneficiaries; the proposed change (which deals only with Covid related costs) allows market participants to fulfil that role by being able to recover unprecedented and exceptional BSUoS costs arising from a global public health emergency.

Disputed Claim: No analysis has been provided as to who the winners and losers are, and to what extent they may be winning or losing - assertions made about Generators and Suppliers entering administration as a result of these charges

Whilst quantitative analysis has not been possible in the limited time available, qualitative assessment has been conducted by the Workgroup and is set out in the report (see, for example, the impacts for the potential alternatives / WACMs on pages 11-17 as well as the overall impacts, in terms of parties, on pages 21-26 of the consultation document).

Notwithstanding this, the aim of the BSUoS charge is to recover the costs of managing the electricity system incurred by the ESO on an equitable basis, as concluded by the 1<sup>st</sup>

BSUoS Taskforce. Suppliers and Generators (currently) act as revenue collectors on behalf of the ESO to achieve this; but have been unable to fully execute this function as a result of the unprecedented and exceptional costs arising from the Covid global public health emergency event.

We challenge the view that assertions have made about the impact on Suppliers and Generators entering administration. We have highlighted in raising this modification that some actors within the market run the **risk of failure** owing to their inability to recover exceptional and significant costs arising from the suppression of electricity demand (due to the UK's response to Covid pandemic and environmental improvements arising from Covid related aspects) and the system management costs required to manage it. We have also highlighted the subsequent **contagion risk** that could ensue from multiple business failures, within the supplier and / or generation sectors, arising from an inability to financially cope with the exceptional Covid related BSUoS costs identified by the ESO in its 15<sup>th</sup> May forecast of BSUoS.

Over and above these general criticisms of CMP345 we are also mindful that Citizen's Advice made some additional points (to those noted above) and we wish to make the following observations on these points.

Disputed Claim: There is a conflict in what problem the modification is really trying to address. The modification seeks to recover costs from consumers without parties accepting any risk in fluctuating BSUoS costs.

The Original proposal (along with WACMs 2,5 and 8) mitigates the impact of the subset of fixed price contracts that extend into 2021/22 (or 2022/23).

We are also mindful that suppliers and generators would remain exposed to the risk of increases above the £500M cap propose in the Original and WACM8 as well as for the bulk (~£1,500M) of BSUoS in 2020/21.

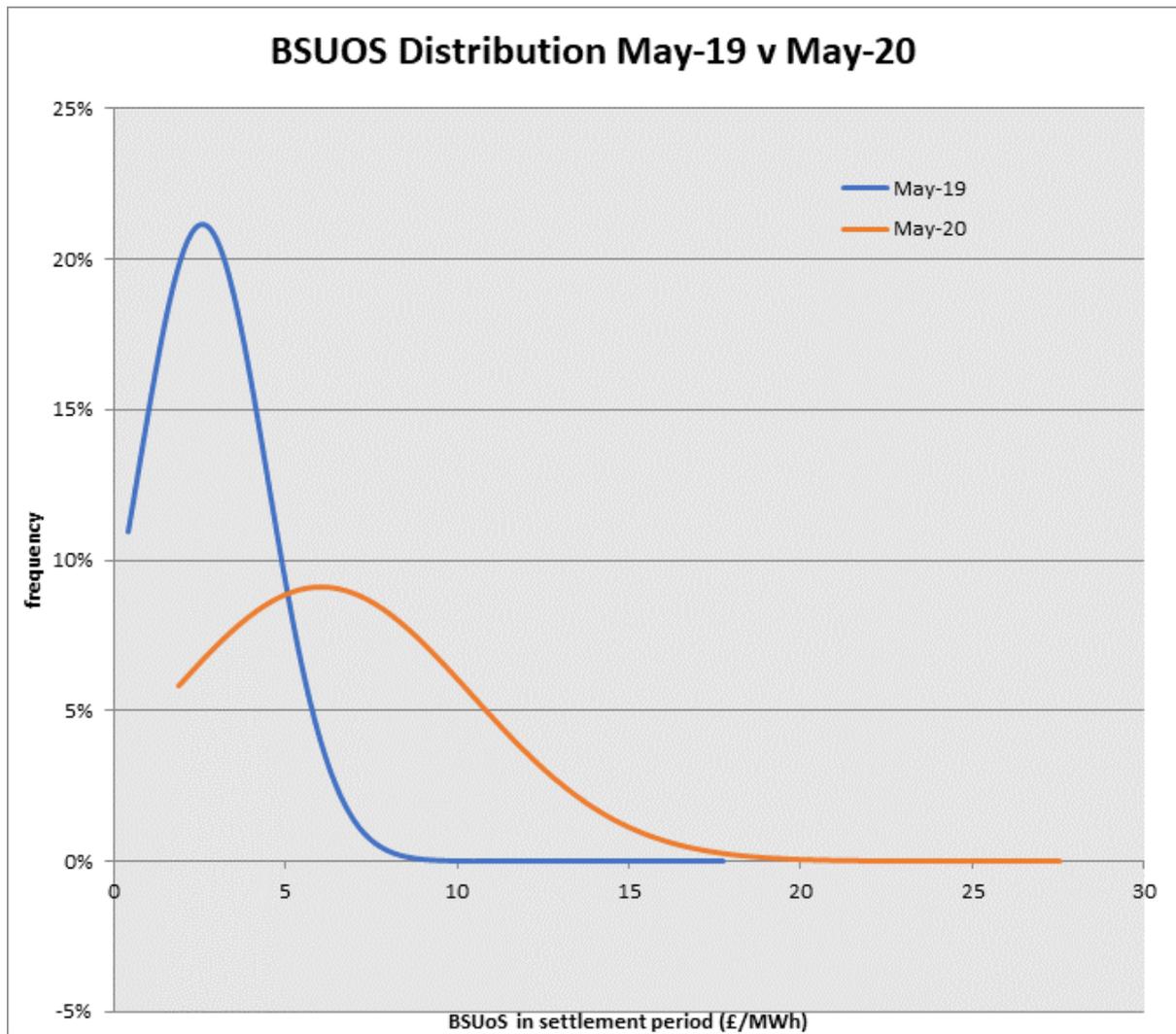
Disputed Claim: Suppliers are already selling, and have already sold, fixed priced tariffs that stretch into the recovery period. They will not be able to recover any unexpected new costs.

CMP345 Original and WACM 2, 5 and 8 do not enable Suppliers to recover unexpected new costs, but this is not a reason in itself to not support the Modification. Implementation of CMP345 does not

	<p>preclude further changes that would allow further unexpected new costs to be deferred and hence recovered (if considered appropriate by Ofgem at that time).</p> <p><u>The duration of the pandemic is uncertain and therefore it is unknown whether market participants will be better able to pay the deferred debts on their new due date</u></p> <p>We recognised that the duration of the Covid pandemic may last for some time; hence why we have included within the CMP345 Original and WACM8 the ability for the date, over which Covid related costs are identified (within 2020/21) for deferral into a future charging year; to be extended, with the agreement of the Authority.</p> <p>The status quo would see suppliers (and generators) paying the Covid related costs in BSUoS broadly speaking as they fall due during 2020/21, even though they do not have the ability to pass those on in tariffs. This gives rise to the highest possibility of supplier default (if that is to occur). The deferral of the costs to a later charging year gives suppliers (and generators) the best possibility of being able to pay the debt as it falls due as they will be able to incorporate the recovery of Covid related costs in BSUoS within their tariffs and market prices. This gives rise to the lowest possibility of supplier default (if that is to occur) compared to the status quo.</p>
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As noted above in our answer to Q3, the following graph shows the distribution of out-turn of BSUoS for May 2020 as compared to May 2019. This clearly shows the extent to which May 2020 BSUoS was outside the distribution expected (based on May 2019).

The average for May 2019 was £2.586 per MWh whereas the average BSUoS for May 2020 was over 133% higher at £6.043 per MWh. This difference will increase as the settlement runs progress as the data so far analysed does not include some significant costs that the ESO incurred over May 2020. It is difficult to see how such a variation of BSUoS in May 2020 could be seen to be within the range of possibility by market participants. This is in line with the variation in the ESO's own BSUoS forecasts (May 2020 vs April 2020 and preceding periods) where the jump in the expected level of BSUoS is substantially beyond what has been seen previously and which is described by the ESO as being as a result of the GB societal response to the Covid pandemic which is widely acknowledged as being unprecedented.



[end]