

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.

| Respondent details | Please enter your details |
|-------------------------|---------------------------|
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CMP345

For reference the applicable CUSC Charging objectives are:

| Relevant Objective |
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| (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 | | |
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| 1 | Do you believe that the CMP345 Original Proposal better facilitates the Applicable CUSC Charging Objectives? | <p>No.</p> <p>In particular, it will distort competition by creating windfall gains and losses (objective (a)).</p> <p>Forsa Energy (FE) notes that, given the BSUoS methodology, this modification is also negative to objective (b) as it reduces cost reflectivity and creates temporal distortion, which seems to be to the benefit of some stakeholders and detriment of others. In particular, any future changes that might be made to the BSUoS charging regime may result in material losses/gains as a result of the temporal shift of this proposed CMP345.</p> <p>Object (c) is not clear, as covid is not a change to the business of system balancing, but to the nature of the system the ESO must balance. High BSUoS (as a result of low demand) was already a market trend, so we would see this change as not taking account of developments so much as trying to avoid the developments.</p> <p>Finally, this seems to be an expensive mod to implement, with the ESO having to raise debt and then carry that for over a year (until March 2022). This is likely to impact their perceived value by shareholders as well adding costs to the market. Without robust evidence that the benefits outweigh the costs, this is negative against objective (e) as well.</p> |
| 2 | Do you support the proposed implementation approach for CMP345? | <p>No.</p> <p>If Ofgem were to implement this change, then it should not back date it, Parties such as FE will have been paid embedded benefits which will have already been spent or distributed as loan repayments etc. We do not believe it was unforeseeable since March that BSUoS would be higher than expected (and it was expected to be higher than 2019). When the UK entered lockdown the industry could reasonable assume that this would impact demand. Previous summers' already implied seasonal demand was reducing (with increased solar and wind generation too) resulting in rising BSUoS (hence the BSUoS Task Forces). So while parties may not have seen how high BSUoS could go, they should have reasonably planned for increasing costs. The fact</p> |

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| | | <p>that the suppliers have chosen to enter longer term, fixed price supply deals is not a defect in the CUSC.</p> <p>While we have sympathy with the situation suppliers may find themselves in, changes to the CUSC are not the way to address their issues. If Ofgem believes that suppliers need relief at the current time, then they need to assess all of the options open to them and consider which is cheapest and least distortionary.</p> |
| 3 | Do you have any other comments? | <p>It is not obvious that the “defect” is a defect in the CUSC, but rather an issue with the way that suppliers have contracted with their customers and/or generators have hedged, making them unable to increase their prices in line with their costs. We recognise that this contracting has created a cashflow issue for suppliers, but for other parties the issues with BSUoS are far wider than when the charges are incurred.</p> <p>Since this consultation was issued, Ofgem has also now set out clearly the support it sees as acceptable and helpful to suppliers in need. Ofgem rightly notes that many parties can access commercial loans and if they need them, they should seek help from the banks not from the monopolies. Where the monopolies are supporting the supplier in need, that support will be repaid by the end of this financial year and will be subject to interest payments of c8%. These points seem relevant when considering this proposal.</p> <p>One of the greatest risks with this proposal is that the deferred costs could be rebilled at a time when BSUoS may be as high, or higher. If charges are to be deferred, then it should be to a time or via a mechanism that limits this risk. Were Ofgem to want to approve any of the changes proposed, it should keep costs allocated to the right charging year as a way to minimise distortions. As a general principle, urgent code changes of this materiality just undermine investor confidence that the market is stable, and any charges well considered.</p> <p>We note that there are not yet any arrears for any parties in relation to the BSUoS uplift or for any other reason – this information is readily available on the BMRS website. It is therefore not obvious the suppliers are in need of a repayment holiday. Furthermore, were Ofgem to wish to help suppliers by deferring costs the deferral of other charges may be cheaper. For example, the TO can probably borrow money cheaper than the</p> |

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| | | <p>ESO (given its asset base) so deferral of TNUoS may be more economic route to offer them interim support. (But we note that neither the TO nor the ESO is designed to provide financing to parties who are in financial trouble. The entire premise is problematic in this regard, even if the TO is more able to undertake the function).</p> <p>The retrospection in the original proposal also creates issues for parties who have already paid or been paid. This potentially creates significant costs in terms of reallocation of funds. Retrospection is rarely considered to be desirable and we see no reason for the ESO to recoup monies already paid or pay monies already recouped. In this respect the proposal should run from 1st July at the earliest. This reduces the clear negative impacts of the temporal shift and also spreads the cost over a longer period.</p> <p>Another obvious problem with this proposal is the recharge will impact different parties in different ways, distorting the market and penalising some customers with bills rising from periods when they were not consuming, and bills being suppressed when costs of supply have increased. This also has behavioural implications & will also penalise parties that are actively helping the ESO to balance the system in times of low demand. The workgroup has not had time to fully consider these windfall gains/losses, but we suggest Ofgem will need to be before agreeing to a change that goes against the industry's aim to be cost reflective.</p> |
| 4 | Do you wish to raise a Workgroup Consultation Alternative Request for the Workgroup to consider? | No. Within this we make proposals to significant changes to the existing mod if any such mod is actually needed. |
| 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. | <p>Yes.</p> <p>FE believes that covid costs are the nuclear contract(s) and the use of ODFM. These are the two contracts that are genuinely new to the management of the system.</p> <p>The Super SEL contracts and creation of "footroom" were already used by the ESO, even if irregularly, and FE believes these products were widely expected to be used this coming summer.</p> <p>We disagree that the costs associated with low demand should be indiscriminately carved out for deferral to next</p> |

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| | | <p>year. The proposal seems to help a section of the market manage its business risk, but at the expense of others who would not expect Ofgem to agree to ad hoc for them were the tables turned.</p> <p>Furthermore, we reiterate that this change should not be retrospective & should apply from 1st July.</p> |
| 6 | <p>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.</p> | <p>See above.</p> <p>There is even a potential argument for ODFM costs to be excluded - we fully expect this product or something similar will endure past this summer to address system issues that have been emerging, independent of Covid. However, for the purpose of simplicity we are willing to concede that the timing of the implementation of ODFM makes it a logical contender for the deferral.</p> <p>We would also say that if the ODFM product is utilised past August, that the costs are excluded from any further cost deferral attempts that may come from September onward. At that stage, it is only the nuclear contract costs that could be considered special and specific to Covid, as the market would come to expect ODFM usage in low demand periods.</p> <p>We would note that it was unfortunate that the nuclear contract(s), given its unique nature, was not done via the Fuel Security Code. This would have given far greater flexibility in who paid and how, but also opened EdF's "costs" to scrutiny by experts outside the ESO.</p> |
| 7 | <p>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.</p> | <p>If Covid-related BSUoS costs are to be deferred, FE thinks it is obvious that to minimise the impacts on cost reflectivity, other distortions, and windfall winners and losers, that the costs should be smoothed over the rest of this charging year (to April 2021). Any other solution opens the market up to a wide variety of unintended consequences, including perhaps a revisit of the issue with a new mod to manage the impact of high BSUoS next year, exacerbated by this mod.</p> <p>Once we get into a future year the customers, suppliers, etc. may have all changed. CMP333 may have been implemented and some older plants shut, etc. This will mean that not only will there be winners and losers in the current year but next year as well. It will also increase the complexity of introduction of any future changes to the BSUoS regime, as they will clearly impact the portion of Covid 19 BSUoS being paid/received on top of the intended consequences of the new change being implemented.</p> |

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| 8 | <p>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 provide rationale to support your response.</p> | <p>It is most sensible to recoup the charges over colder months when BSUoS tends to be lower – thereby lessening the impact of any distortions. Making it a fixed charge per MW/hr would make it easier for all parties to manage and would minimise the distortive impacts of this mod.</p> <p>To reiterate though, FE are of the view that these charges should be collected this charging year – in no way should they be deferred to a future charging year, for the reasons outlined above.</p> |
| 9 | <p>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.</p> | <p>The simplest approach would be to codify the value of the nuclear turn down deal. As per above, we are open to including ODFM in this mod (noting we are against the mod in the first place) and these would run from 1st July 2020, and in this case the actual costs incurred daily would be accrued into a pot of deferred costs. The scale of covid costs should be reported on a daily basis so that parties could then plan for the scale of the cost recovery they need to plan for. There does not need to be a cap, as this should be cost related and not picking random numbers. Our definition of covid costs would see a far lower number than the original mod, so a cap should also be unnecessary. We note that the value of the nuclear deal is not public – but we aren't sure this confidentiality is a sufficient reason to not defer this cost. there is a need for greater transparency. The ESO is a monopsony and in the market for turn down of scale, EDF is a monopoly.</p> |
| 10 | <p>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?</p> | <p>In no way should any mod with such potential for market distortion be open to extension without due process. We also note that this should not be retrospective and should not apply before 1st July 2020.</p> <p>This mod has been raised as urgent, and the workgroup, and indeed responding parties, have had no time to complete even the simplest or most basic analysis to determine the extent of winners and losers & behavioural impact as a result of the deferral of Covid related BSUoS costs from the period they were incurred.</p> <p>It is for this reason that we are very nervous about the distortive impacts. It is also the reason that if any extension is granted, that there be a requirement that a</p> |

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| | | <p>full analysis is completed to ensure that the distortive impacts are in line with the CUSC objectives.</p> <p>Without analysis, this is simply a mod asking for the ESO to finance a deferral of costs to support one or more sets of parties without reference or relation to the actual need of those cost deferrals. Moving costs between years creates distortions and urgent interventions undermine market confidence. It is not the ESO's role support other companies, and it sets a dangerous precedent to change the market rules to make charges even less cost reflective, creating temporal distortions.</p> |
| 11 | <p>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 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.</p> | <p>As noted above, we do not believe the case has been made – no evidence has been provided that suppliers or generators are at risk of failure – that there will be a security of supply risk arising directly or indirectly from these Covid-related BSUoS charges. In a period of low demand generator failures would seem to create no risk of insufficient capacity. Likewise, the SoLR process, which is well tested, will manage the impact of a defaulting supplier to protect their customers. The security of supply arguments are simply bogus.</p> <p>Ofgem is the only party that would be aware of the plight of individual suppliers (if they aren't defaulting on BMRS). We assume that they are looking at wider measures, aligned with their statutory duties, to fairly and equitably help these parties. We know also that the government has loaned the LCCC funds to cover CfD costs for this summer – for the benefit of suppliers.</p> <p>It is at these levels that support should be provided – they are not distortive and are targeted to help parties in need of help. Further, these Government and Regulator initiatives do not rely on private entities (the ESO) providing financing and cost deferral to the wider market. Relying on the ESO to raise debt, possibly at short notice, is not an appropriate way to respond to the issues suppliers face.</p> <p>FE support the work of the BSUoS Task Force and think it unfortunate it has been furloughed. It should have been asked to meet to consider this mod against the wider work it has done already. The group needs to start to meet and to come up with a solution that could be implemented in a timely manner.</p> <p>The DRAB proposal could be considered as a sensible and proportionate response to the current issues, and</p> |

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| | | <p>may provide a steppingstone to a longer term solution, while keeping costs within the right charging year. Again, the Task Force could consider whether this would be an incremental change that would benefit the market. The ESO solution that involved provision of targeted loans to needy parties, or to defer the collection of Covid related BSUoS costs to this winter are also non-distortionary and acceptable options.</p> |
| 12 | <p>Do you agree with the financing options set out above? Is there another way? Please provide rationale to support your response.</p> | <p>We do not agree that it is appropriate to ask the ESO to fund the cost deferrals for other private entities.</p> <p>If specific market participants are struggling due to Covid-related market conditions, then it is the role of Ofgem or HMRT to provide assistance. The market and the ESO are not responsible to the financial well-being of other market participants.</p> <p>We note the ESO's willingness to try to help, given the alternates they have raised, and they should be thanked for that. However, we think the value and the time period make the original mod unacceptable.</p> |
| 13 | <p>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.</p> | <p>The impacts raised in this consultation are no more than vague cross cutting assertions. We think it is entirely inappropriate, and a poor precedent to set, to insert a distortive jolt into the market, without the benefit of a full cost benefit analysis.</p> |