

**CUSC Workgroup Consultation Response Proforma****CMP357 'Clarification of Transmission Licensee revenue recovery and the treatment of revenue adjustments in the Charging Methodology'**

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 **5pm on 8 January 2021**. 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.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 (charging) 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; and*
- e. *Promoting efficiency in the implementation and administration of the system charging methodology.*

*\*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 regarding the Workgroup Consultation in the right-hand side of the table below, including your rationale.

CMP357 - Standard Workgroup Consultation questions		
1	Do you believe that the CMP357 Original Proposal or the potential alternative options better facilitates the Applicable Objectives?	<p><u>In summary (with detailed comments under question 5.)</u></p> <p><i>(a) facilitating effective competition</i> Positive. The proposal improves the effectiveness of competition in generation as it increases the accuracy of TNUoS charges, reducing the potential for unduly increased or reduced TNUoS tariffs being applied to Users.</p> <p><i>(b) resulting in cost-reflective charges</i> Positive. The proposal promotes greater accuracy of the Security Factor and this will improve the cost-reflectivity of the value of the security factor used within TNUoS tariffs applied to Users.</p> <p><i>(c) properly takes account of developments in TOs' transmission businesses</i> Neutral.</p> <p><i>(d) being compliant with EU regulations</i> Positive. It is a legal requirement of Directive 2009/72(EU) Recital 36 that transmission tariffs in GB "are non-discriminatory and cost-reflective" and this proposal, by ensuring more accurate transmission tariffs are in place in GB for the forthcoming Price Control period will mean that compliance with the Electricity Regulation and any relevant legally binding decision etc. (in terms of the duties placed upon the NRA – Ofgem - in Article 37(1)(a) according to Recital 36) is achieved as without accurate transmission tariffs there will be (i) discrimination in those tariffs (as some will pay more and some less than they should for no justified reason) and (ii) they will not be accurately cost-reflective.</p> <p><i>(e) Promoting efficiency in the implementation and administration of the system charging methodology</i> Neutral.</p>
2	Do you support the proposed implementation approach for CMP357?	Yes, we support implementation in the forthcoming charging year (starting with the TNUoS tariffs for 1 <sup>st</sup> April 2021 onwards that are produced by the 31 <sup>st</sup> January 2021), and for the full duration of the price control. This change proposal is about improving the accuracy of the Security Factor as of the start of the new price control. We do not support a phased introduction

		of the change, the process for which would create delay and extend the uncertainty about this measure.
3	Do you have any other comments?	<p>Our additional comments are as follows:</p> <p><i>On the ongoing practice of rounding</i></p> <p>The ESO advised that one decimal place had been used for the Security Factor based on the assumption that industry was happy with this level of accuracy. We disagree that industry was in fact content, and this was clearly demonstrated when the ESO put the issue to industry in the autumn of 2020. Following expressions of discontent at the TCMF in September, the ESO was prompted to more formally consult on the issue. This resulted in 13 response, of which the majority favoured the use of eight decimal places.</p> <p>We also note that in the 2004 Charging Statement which was cited in the Workgroup Consultation, explicit mention was made of rounding for the Expansion Factor, but <u>not</u> for the Security Factor. In our view, this highlights an inconsistency of practice rather than an argument in support of it.</p> <p><i>On the margin calculation</i></p> <p>The consultation refers to a Workgroup member's suggestion that setting the intercept for the margin calculations at zero could result in improved accuracy. We consider that both past and current calculations clearly show the intercept not to be zero. However, more importantly, we consider that changing the calculation in this way would constitute a change in the calculation methodology and is therefore not in scope of this modification proposal.</p>
4	Do you wish to raise a Workgroup Consultation Alternative Request for the Workgroup to consider?	No.
<b>Specific Workgroup Consultation Questions</b>		
5	Do you have any further analysis/evidence to support your conclusions under Question 1?	[See below for our response to this question, where we discuss tariff stability, data accuracy and good practice, distributional impacts and tariff predictability.]
6	Will the CMP357 Original Proposal	Yes, for the duration of the new RIIO T2 price control, by paying increased Wider Tariffs that arise from applying a 1

	<p>or the potential alternative options impact on your business. If so, how?</p>	<p>decimal place approach to expressing the Security Factor (which do not reflect the likely investment that can be expected to be made by the TOs) then our business will be adversely affected.</p> <p>We have set out the adverse distributional impacts of not making the proposed change (to 8 decimal places) under question 5 (see below).</p>
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5. Do you have any further analysis/evidence to support your conclusions under Question 1?

*Objective (a) – facilitating effective competition*

The ESO have identified tariff predictability, tariff stability and cost reflectiveness as assessment criteria when they recently considered the decimal places for the Security Factor (which is the defect CMP357 seeks to address). Therefore, we have examined them in our response here as to whether this modification is better than the baseline CUSC against the objectives.

*Tariff stability*

We do not agree that rounding the Security Factor (SF) to 8 decimal places (dps) creates instability, but rather the opposite: that fixing the SF for the duration of the price control creates stability. The argument that rounding to 1dp creates more stability may apply if the SF itself is fairly stable. When presented to 3dp+, the SF for the next price control is very close to 1.751. If for the next price control, the SF reduced marginally, e.g. to 1.749, then using the approach of rounding to 1dp, the SF would be rounded to 1.7. Or to put it another way, using this simple example<sup>1</sup> a 0.114% change in the calculated SF would create a 5.6% change in the utilised SF. Rounding to 1dp can therefore exaggerate change and create a step change in the utilised SF and resulting TNUoS tariffs, and create instability, even when the actual calculated SF may have changed very little in value before being rounded.

*Objective (b) – cost reflectivity*

As set out above (objective (a)), rounding to 1dp either exaggerates or prevents change which is clearly at the expense of accuracy and hence cost reflectivity of the TNUoS tariffs that are paid by Users.

*Accuracy and good practice*

Modelling in SECULF requires the same inputs as those for TNUoS tariff setting and the five-year forecast, i.e. Contracted TEC, Peak demand from the Wk24 data provided by DNOs, and the Network Topology from each TO as shown in the Electricity Ten Year Statement. This same data is also used by the System Operator to plan the future transmission system and justify investment through the Network Options Assessment (NOA) as well as to set Price Control Allowed Revenues.

The SECULF model calculates a MW/km value to 13dp for each node, for each year

<sup>1</sup> 1.751 to 1.749

for an intact network as well as for a secure network again. A line of best of fit is then produced to a high level of accuracy (at  $R^2 = 0.9946$  as per the ESO's analysis, p.10). Therefore, it is very clear that detailed calculations to numerous decimal places are currently used throughout the process when calculating the SF, using transparent data inputs used in other Industry processes.

The accuracy of the SF is unnecessarily reduced at the end of this SF calculation process by the application of the step of rounding to 1dp (which in itself creates spurious accuracy) rather than to multiple decimal places. Please note the CUSC does not require NGENSO to undertake this rounding step, and although previous SFs have, without explanation or record as to method, been quoted to 1dp, it is unclear why rounding took place.

We are, however, clear that rounding to 1dp would have a significant and material effect on the cost reflectivity of the SF for the next price control and hence on the cost reflectivity of the TNUoS tariffs paid by Users that are based on the SF (along with other items) for the next five charging years.

Incidentally, another key parameter reviewed for each price control, the Expansion Constant, is produced to 8dp, and final TNUoS tariffs are provided by NGENSO to 6dp. Using 1dp for the SF is therefore inconsistent with other inputs and outputs used by NGENSO to determine the TNUoS tariffs paid by Users. Moving to 8dp removes that inconsistency and clearly improves cost reflectivity.

There has been a trend of the SF reducing since its inception. In 2004, for England and Wales only, the SF was set at 1.9. When Scotland was introduced into the model as part of BETTA, the SF immediately reduced to 1.8.

Allowed Revenues for 2013/14 from the Five-year forecast<sup>2</sup> and Allowed Revenues for 2021/22 from the November draft<sup>3</sup> are shown in the table below.

	<b>13/14</b>		<b>21/22</b>	
NGET	1587		NGET	1919.9
SHET	172		SHET	390.6
SPT	271	<b>443</b>	SPT	539.7
	<b>2030</b>	22%	<b>2850.2</b>	<b>930.3</b> 33%

We can see a large percentage rise in Scottish Allowed Revenues as a proportion of overall Allowed Revenues. The change between 2004 (1.9) and 2005 (1.8) in the SF indicates that Scotland has a lower level of transmission network redundancy. When coupled with the change in Allowed Revenues we would expect the SF to continue to show this downward trend and to reduce for this forthcoming price control.

This aligns with the move to the UK Government's Net Zero goals and the connection of a number of small (in terms of their proportion to conventional)

<sup>2</sup> <https://www.nationalgrid.com/sites/default/files/documents/5772-Initial%20View%20of%20Network%20Use%20of%20System%20%28TNUoS%29%20tariffs%20from%202013-14%20to%202017-18.pdf>

<sup>3</sup> <https://www.nationalgrideso.com/document/181956/download>

intermittent generation. Circuit outages etc., are therefore less likely to cause a loss of supply of 1500MW or unacceptable frequency conditions.

The reduced SF better reflects transmission investment and the increased number and variety of Balancing Services Providers available to NGENSO.

It would therefore have been surprising to see no change in the SF, especially as we have seen a substantial change in the Charging Methodology since the last SF review ahead of the 2012 price control with, for example, the changes associated with Project Transmit and the introduction of the economy background into the SQSS and the model, on which the SF was based for this year.

#### *Distributional impacts*

Without the CMP357 proposed change, generators in Scotland will be paying for a higher level of transmission network redundancy (1.8) in their TNUoS tariffs and generators in the South will be paid more via TNUoS tariffs for redundancy – both of which does not exist in reality. Rather than considering that there will be winners and losers resulting from whether this change is approved or not it is more instructive to see that this mod better aligns the TNUoS tariffs paid by Users to the likely incremental cost of additional transmission investment.

#### *Predictability*

NGESO discussed the SF at TCMF meetings in the later part of last year and consulted on the way ahead. **If** rounding to 1dp was standard practice and predictability the overarching driver, there would have being no need to (i) raise it at TCMF or (ii) go out to consultation.

NGESO have been partially transparent throughout this process which we welcome. This transparency highlighted a defect (which may have existed in previous calculations of the SF unbeknown to industry) which the majority of industry responders to the NGENSO consultation supported removing, by moving to a greater number of decimal places.

NGESO did not announce their conclusions until 21<sup>st</sup> December 2021, and this modification (CMP357) was subsequently raised the next day. Industry therefore could not have predicted with any certainty what the SF would be for 2021/22 until just before Christmas and that even if one deems this to be an indication of certainty it only lasted a day. The SF has not always been at 1.8. It was 1.9 in 2004/5 so change does happen and given that the ESO had announced nothing about the SF ahead of the September TCMF it is not plausible to claim that 1.8 was an expected value. It is not a fixed constant and the fact that it was to be reviewed ahead of every price control has been known for many years. It was clear when the security factor calculation for 2021/22 was announced that there was uncertainty whether 1 or more decimal places would be used.

The ESO could not and has not to date provided any evidence that rounding to 1 decimal place was “custom” for this calculation. The claim that 1 decimal place is the more stable outcome is not supported by the indication given by the ESO at the November 2020 TCMF that the SF would be expressed to 2 decimal places or the

presentation at the September TCMF which showed the numbers to 4 decimal places.