

CUSC Modification Proposal Form		At what stage is this document in the process?												
<h1 style="color: #00a651;">CMP344</h1> <h2>Clarification of Transmission Licensee revenue recovery and the treatment of revenue adjustments in the Charging Methodology</h2>	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="text-align: center; border: 1px solid black; border-radius: 5px;">01</td> <td style="background-color: #00a651; color: white; border: 1px solid black; border-radius: 5px;">Proposal Form</td> </tr> <tr> <td style="text-align: center; border: 1px solid black; border-radius: 5px;">02</td> <td style="border: 1px solid black; border-radius: 5px;">Workgroup Consultation</td> </tr> <tr> <td style="text-align: center; border: 1px solid black; border-radius: 5px;">03</td> <td style="border: 1px solid black; border-radius: 5px;">Workgroup Report</td> </tr> <tr> <td style="text-align: center; border: 1px solid black; border-radius: 5px;">04</td> <td style="border: 1px solid black; border-radius: 5px;">Code Administrator Consultation</td> </tr> <tr> <td style="text-align: center; border: 1px solid black; border-radius: 5px;">05</td> <td style="border: 1px solid black; border-radius: 5px;">Draft CUSC Modification Report</td> </tr> <tr> <td style="text-align: center; border: 1px solid black; border-radius: 5px;">06</td> <td style="border: 1px solid black; border-radius: 5px;">Final CUSC Modification Report</td> </tr> </table>		01	Proposal Form	02	Workgroup Consultation	03	Workgroup Report	04	Code Administrator Consultation	05	Draft CUSC Modification Report	06	Final CUSC Modification Report
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<p><b>Purpose of Modification:</b> This modification proposal clarifies that the allowed revenue for Transmission Owners recovered from Transmission Users under the Charging Methodologies is fixed for each onshore price control period for onshore transmission licensees and at the point of asset transfer for OFTOs.</p> <ul style="list-style-type: none"> <li>- This means that once the revenue recovery is set at the start of the relevant period there can be no additional adjustments to this revenue (apart from under or over recovery factors) that are applied to Transmission Users for that price control period.</li> </ul> <p>This modification proposes that revenue adjustments associated with actual costs incurred and costs saved for a Transmission Licensee that occur within price control periods from unforeseen or unforeseeable events, including Income Adjusting Events (IAEs), are recovered from Transmission Users by adjusting the Demand Transmission Residual.</p> <ul style="list-style-type: none"> <li>- These revenue adjustments to the Demand Residual will relate to the actual costs incurred and costs saved set out in the direction from the Authority in relation to the specific unforeseen or unforeseeable event. There will be no further cost recovery from Users in relation these costs.</li> </ul>														
	<p><b>The Proposer recommends that this modification should be:</b></p> <ul style="list-style-type: none"> <li>assessed by a Workgroup</li> </ul> <p>This modification was raised <i>21 May 2020</i> and will be presented by the Proposer to the Panel on <i>29 May 2020</i>. The Panel will consider the Proposer’s recommendation and determine the appropriate route.</p>													
	<p><b>High Impact:</b> Transmission Owners, Transmission Users including Generation and Suppliers</p>													

 **Medium Impact National Grid ESO.**

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<b>Timetable</b>		
<p><i>The Code Administrator will update the timetable once the modification has been prioritised by the CUSC Panel.</i></p>		
<b>The Code Administrator recommends the following timetable:</b>		
Initial consideration by Workgroup		29 June 2020
Workgroup Consultation issued to the Industry		To Be Confirmed
Modification concluded by Workgroup		To Be Confirmed
Workgroup Report presented to Panel		To Be Confirmed
Code Administration Consultation Report issued to the Industry		To Be Confirmed
Draft Final Modification Report presented to Panel		To Be Confirmed
Modification Panel decision		To Be Confirmed
Final Modification Report issued the Authority		To Be Confirmed
Decision implemented in CUSC		1 April 2021

**Any questions?**

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**Proposer Details**

<b>Details of Proposer:</b> (Organisation Name)	Bill Reed RWE Supply & Trading GmbH
Capacity in which the CUSC Modification Proposal is being proposed: (i.e. CUSC Party, BSC Party or "National Consumer Council")	CUSC Party
<b>Details of Proposer's Representative:</b> Name: Organisation: Telephone Number: Email Address:	Bill Reed RWE Supply & Trading GmbH 07795 355 310 Bill.reed@rwe.com
<b>Details of Representative's Alternate:</b> Name: Organisation: Telephone Number: Email Address:	Raoul Thulin RWE Supply & Trading GmbH 07795 354334 Raoul.thulin@rwe.com
<b>Attachments (Yes/No): No</b> <b>If Yes, Title and No. of pages of each Attachment:</b>	

**Impact on Core Industry Documentation.**

*Please mark the relevant boxes with an "x" and provide any supporting information*

<b>BSC</b>	<input type="checkbox"/>
<b>Grid Code</b>	<input type="checkbox"/>
<b>STC</b>	<input type="checkbox"/>
<b>Other</b>	<input type="checkbox"/>

(Please specify)

No impact on other Core Industry Documents

## 1 Summary

**Mandatory for the Proposer to complete** Please provide a summary of the modification proposed – i.e. **what** is the identified defect/change in the existing code that needs to be rectified, **why** this change needs to be made, and **how**.

### Defect

#### Treatment of the Maximum Allowed Revenue (MAR)

Section 14 of the CUSC defines the basis on which Transmission Licensees recover the allowed revenue from Users. Section 14.14.1 sets out the nature of the cost to be recovered from Users. Section 14.14.2 specifies that Transmission Network Use of System Charges (TNUoS) are set to recover the Maximum Allowed Revenue (MAR) as set by the Price Control (where necessary, allowing for any Kt adjustment for under or over recovery in a previous year net of the income recovered through pre-vesting connection charges). From this it is clear that the intent of Section 14 is to recover the costs of the MAR established at the start of the price control and TNUoS tariffs are set to recover the MAR.

The arrangements for recovery of the MAR for Offshore Transmission Owners (OFTOs) was set out in a letter issued by National Grid in July 2017<sup>1</sup> which stated that “*as the offshore local circuit and substation tariffs are set at the point of asset transfer any changes in revenue (positive or negative) for the OFTO, for example due to an income adjusting event, are not reflected in the relevant offshore generator’s tariffs.*”

The CUSC does not specify how changes in revenue are taken into account with respect to the offshore local circuit and substation tariffs are set. The letter indicates that the changes in revenue are “not reflected in the relevant offshore generator’s tariffs”.

The July 2017 letter also states that “*Adjustments for the current price control (RIIO-T1) will take effect from 2021/2022 and will be spread over the duration of the next price control period (RIIO-T2). These tariffs will also include allowed OFTO revenue forecasts for the new price control period (RIIO-T2)*”.

Neither the letter nor the CUSC describe how changes in revenue (positive or negative) for the OFTO that could occur for example due to an income adjusting event should be treated.

It is understood that these costs are initially recovered through adjustments to the wider residual. Subsequently, at the start of the next onshore transmission price control period there is a reconciliation process that takes into account previously socialised revenue in setting local circuit charges payable by the offshore generator for the relevant OFTO in relation to the IAE. However these arrangements are not clearly set out in the CUSC.

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<sup>1</sup> See <https://www.nationalgrideso.com/document/94076/download> (the July 2017 Letter)

This modification proposal sets out that offshore local circuit and substation tariffs are set at the point of asset transfer for the basis of the recovery of allowed revenue for OFTOs under the CUSC and forms part of the MAR.

This modification proposal sets out that changes in revenue (positive or negative) for the OFTO, for example due to unforeseen or unforeseeable events such as an income adjusting event does not form an adjustment to allowed revenue that is taken into account in the MAR at the start of the next onshore price control.

### **Treatment of revenue adjustments associated with unforeseen and unforeseeable actual costs incurred and costs saved during a price control period for a Transmission Licensee**

Section 14 of the CUSC does not clearly set out the basis on which revenue adjustments associated with actual costs incurred and costs saved for a Transmission Licensee that occur within price control periods are treated. Within price control revenue adjustments can occur as a result of, for example, IAEs.

The issue of the recovery of revenue adjustments was highlighted at the TCMF in May 2016<sup>2</sup>. National Grid indicated that *“unforeseen adjustment to OFTO’s annual revenue (e.g. Performance incentives) are not seen by the local offshore generators” and “these unforeseen adjustments are picked up through wider residual tariffs, and affect other network Users”*.

This Modification Proposal confirms the general approach identified in 2016. It also addresses the issue of the treatment of income adjusting events in the CUSC identified in Ofgem’s Income Adjusting Event policy document published in November 2018<sup>3</sup>.

In this document Ofgem observed that *“A number of respondents considered that, where paragraph 15(c) of Amended Standard Condition E12-J3 (Restriction of Transmission Revenue: Allowed Pass-through Items) (the IAE Condition) allowed costs to be passed through, costs should not be borne primarily by offshore generators, and instead should be socialised. They considered that placing this risk onto offshore generators would result in: the generator becoming the ‘insurer of last resort’; an increase in development costs; a windfall loss to wind farm developers (as they would bear the loss for both generation revenues and the cost of the Offshore Transmission Owners (OFTO’s) repair); detrimental outcomes for consumers; and new investors being deterred”* (Paragraph 4.1).

Ofgem noted that: *Two respondents stated that generators should not be required to cover the risks of an asset they have no control over. One respondent considered that greater socialisation of these costs would ensure consistency with the framework for onshore Transmission Owners (TOs) and ensure there was no discrimination between onshore and offshore connected generators. Three respondents were of the view that generators would increase Contract for Difference (CfD) bid prices to protect themselves against these types of events* (Paragraph 4.2).

Ofgem concluded that: *“the TNUoS charging methodology is outside of the scope of the IAE policy consultation”* (Paragraph 4.3). However, they stated that *“We note that*

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<sup>2</sup> See <https://www.nationalgrideso.com/document/94076/download>

<sup>3</sup> See “Policy – Income Adjusting Events in Offshore Transmission Owner Licences”, Ofgem 2018, at [https://www.ofgem.gov.uk/system/files/docs/2018/11/iae\\_response\\_-\\_final\\_0.pdf](https://www.ofgem.gov.uk/system/files/docs/2018/11/iae_response_-_final_0.pdf).

*parties to the CUSC can propose a CUSC amendment if they do not agree with the TNUoS charging methodology contained in the CUSC and believe that the proposed modification would better facilitate the relevant objectives under Standard Condition C5(5) of National Grid Electricity Transmission (NGETs) electricity transmission licence. Section 8 of the CUSC sets out how the CUSC can be amended. Nothing in this document should be taken as prejudicing or fettering the Authority's discretion in the event that a proposed code modification were brought before the Authority" (Paragraph 4.6). This is that CUSC Modification.*

This modification specifically proposes that revenue adjustments associated with unforeseen and unforeseeable actual costs incurred and costs saved for a Transmission Licensee are recovered through the Demand Residual only.

The arrangements in the CUSC for the recovery of actual costs associated with unforeseen or unforeseeable events on the GB transmission system that relate to "offshore circuits" are not clearly specified. These actual costs or savings, where permitted, are initially recovered from Users in adjustments to the Wider Residual. However, it is understood that these the costs are then subject to adjustments to specific local changes at the start of the next onshore transmission price control period and that there is a reconciliation process that takes into account previously socialised revenue. This could result in user specific changes that relate to the unforeseen and unforeseeable event.

Note that in the CUSC Section 14 there are no specific terms that relate to this reconciliation process for the wider residual or local charges. The costs of unforeseen or unforeseeable events that relate to "onshore circuits" are recovered from Users through adjustments to the wider residual<sup>4</sup>.

The arrangements for the actual costs incurred or saved for unforeseen and unforeseeable events that relate to "onshore circuits" are therefore different from the arrangements for "offshore circuits".

The CUSC arrangements for OFTO revenue that relate to the wider residual and subsequent reconciliation process related to unforeseen and unforeseeable events, gives rise to the following concerns:

- i) The lack of transparency over the process means there is a risk of double charging Users in relation to the wider residual charges and the user specific charges;
- ii) It is unclear whether those Users paying wider residual charges that relate to the initial wider residual adjustment will also be subject to lower wider residual charges as a result of corresponding adjustment to offshore local tariffs at the start of the next price control period. Indeed over the period of the price control (up to five years) Users subject to actual costs incurred and costs saved at the start of the period may be different to those Users at the end of the period; and

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<sup>4</sup> See for example: determination and notice under special condition j3 – restriction Of transmission charges: transmission investment for renewable Generation of the electricity transmission licence of Scottish Hydro electric transmission limited (SHETL), Ofgem, 25 January 2010 at [https://www.ofgem.gov.uk/sites/default/files/docs/2010/01/tirg-determination-and-notice-income-adjusting-event-and-asset-value-adjusting-event-for-sloy\\_0.pdf](https://www.ofgem.gov.uk/sites/default/files/docs/2010/01/tirg-determination-and-notice-income-adjusting-event-and-asset-value-adjusting-event-for-sloy_0.pdf)

- iii) It is difficult for Users subject to the actual costs incurred and costs saved to verify that the costs allocated to them are justified.

The modification proposes to address these concerns by recovering the costs associated with unforeseen or unforeseeable events on the GB transmission system through adjustments to the Demand Residual.

The proposed approach to revenue recovery is compliant with relevant EU legislation, consistent with the objectives of the Target Charging Review/Significant Code Review (TCR/SCR). The proposal results in an approach that cost reflective to the extent possible, non-discriminatory, fair, proportionate and non-distortive,

## What

This modification proposes the following changes to the CUSC:

- i) Changes to Section 14.14.2 to clarify that the MAR is set for each onshore price control period for onshore transmission licensees and at the point of asset transfer for OFTOs and is not subject to any further modification for the duration of the Price Control Period except for where necessary, allowing for any Kt adjustment for under or over recovery in a previous year net of the income recovered through pre-vesting connection charges;
- ii) A new section of the Charging Methodology which ensures that any revenue adjustments associated with actual costs incurred and costs saved for a Transmission Licensee that occur during the price control period are recovered through adjustments to the Demand Residual as may be permitted in the final determination of the adjustment by the Authority (Ofgem).
- iii) Further changes in Section 14 to allow the pass through of the revenue adjustment through the demand residual.

## Why

Section 14 of the CUSC does not set out clearly that TNUoS tariffs are set to recover the MAR established at the start of regulatory price control period and that the MAR applies for the duration of the price control period except for any Kt adjustment related to under or over recovery in a previous year net of the income recovered through pre-vesting connection charges.

This modification proposal will therefore ensure that Transmission Licensees will recover the MAR for the duration of the price control period. This will ensure that the arrangements are cost reflective to the extent possible at the start of the price control period and will exclude unforeseen and unforeseeable events including income adjusting events as part of this price setting process.

For OFTOs the offshore local circuit and tariffs set at the point of asset transfer will be applied and any changes in revenue (positive or negative) for the OFTO, for example due to an income adjusting event, will not be reflected in the relevant offshore generator's tariffs.

Section 14 does not set out the basis for the recovery of revenue adjustments associated with actual costs incurred and costs saved for a Transmission Licensee that may occur during the price control period. National Grid identified that such adjustments are reflected in adjustments to the wider residual. This modification confirms this

general approach and proposes adjustments to the demand residual to reflect actual costs incurred or cost savings associated with unforeseen and unforeseeable events in a manner that is non-discriminatory and consistent with the approach adopted in the TCR/SCR i.e. fair, proportionate and non-distortive.

Setting out the basis for the recovery of revenue adjustments will have the following benefits:

- i) It will enable Transmission Licensees to ensure that they can recover their allowed revenue for the duration of the price control;
- ii) It will enable Transmission Licensees to recover revenue adjustments related to actual costs incurred and costs saved through adjustment to the demand residual in a manner that is fair, proportionate and non-distortive manner;
- iii) Reduce the risks (and cost of capital) associated with revenue recovery for Transmission Licensees and in particular offshore transmission Licensees; and
- iv) Reduce the risk for Users connected to the transmission system, particularly Offshore Generators by ensuring that unforeseen or unforeseeable events that impact transmission revenues are recovered from Users in a fair proportionate and non-distortive manner.

Furthermore the recovery of costs through the Demand Residual where a cost is incurred or saved for an unforeseen or unforeseeable event as may be permitted by Ofgem has the following benefits:

- It is consistent with the allocation of charging for onshore IAEs<sup>5</sup>;
- It is consistent with the commercial arrangements of the offshore regime i.e. the generator has sold the assets via a transparent heavily scrutinised process overseen by the independent regulator;
- It allows detailed due diligence of the assets to be conducted by the purchasing OFTO;
- It enables the OFTO can take out insurance for the assets and seeks indemnity where issues are identified prior to the sale of the assets; and
- It is consistent with principles of construction law – any defects arising after the assets are sold is the responsibility of the Purchaser.

With regard to the impact of the current arrangements it is noted that:

- It is not fair or proportionate to hold the generators to account for IAEs where they would not have any responsibility under normal commercial arrangements following the sale of large scale infrastructure;
- It is not fair or proportionate for the generator to be an insurer of last resort for the OFTO especially as this was not indicated up-front;

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<sup>5</sup> See for example: determination and notice under special condition j3 – restriction Of transmission charges: transmission investment for renewable Generation of the electricity transmission licence of Scottish Hydro electric transmission limited (SHETL), Ofgem, 25 January 2010 at [https://www.ofgem.gov.uk/sites/default/files/docs/2010/01/tirg-determination-and-notice-income-adjusting-event-and-asset-value-adjusting-event-for-sloy\\_0.pdf](https://www.ofgem.gov.uk/sites/default/files/docs/2010/01/tirg-determination-and-notice-income-adjusting-event-and-asset-value-adjusting-event-for-sloy_0.pdf)

- Developers are significantly financially impacted by all outages that occur, it is therefore unfounded to suggest that they are not motivated to develop quality transmission systems.

Clarification of these arrangements will enable the Government to meet its net zero target by 2050.

## How

Changes to Section 14 of the CUSC are required as follows:

*14.14.1 Transmission Network Use of System charges reflect the cost of installing, operating and maintaining the transmission system for the Transmission Owner (TO) Activity function of the Transmission Businesses of each Transmission Licensee. These activities are undertaken to the standards prescribed by the Transmission Licences, to provide the capability to allow the flow of bulk transfers of power between connection sites and to provide transmission system security.*

*14.14.2 A Maximum Allowed Revenue (MAR) defined for these activities and those associated with pre-vesting connections is set by the Authority at the time of the Transmission Owners' price control review for the succeeding price control period **and at the point of asset transfer for OFTOs**. Transmission Network Use of System Charges are set to recover the Maximum Allowed Revenue as set **at the start of the Price Control will apply for the duration of the Price Control Period** (subject to where necessary, allowing for any Kt adjustment for under or over recovery in a previous year net of the income recovered through pre-vesting connection charges).*

*14.14.2[a] Any adjustment to the Maximum Allowed Revenue within the price control period associated with actual costs incurred and costs saved for a Transmission Licensee that is permitted as a result of a determination by the Authority will result in a change to the Demand Residual for the period set out in the final determination of the adjustment published by the Authority.*

*Section 14 of the CUSC does not refer to any specific adjustments to the residual that allow for changes to the residual that reflect any unforeseen or unforeseeable additional cost adjustments to the demand residual. Therefore further changes in Section 14 are required to allow the pass through of the revenue adjustment through the demand residual.*

## 2 Governance

### Justification for Normal Procedures

Note that this is not an urgent Mod but it is linked to the implementation of the RIIO-2 for the Transmission Licensees Price controls from April 2021.

### Requested Next Steps

This modification should:

- be assessed by a Workgroup

Note that since this change impacts on the Demand Residual it should be subject to assessment in a work group. .

### 3 Why Change?

Transmission Licensees including OFTOs can seek to adjustments to allowed revenue that occurs as a result of unforeseen or unforeseeable events. For example, the current standard OFTO licences contain provisions that enable OFTOs to apply to the Authority for additional revenue related to Income Adjusting Events which relate to

*“(a) an event or circumstance constituting force majeure under the STC;*

*(b) an event or circumstance resulting from an amendment to the STC not allowed for when the Allowed Transmission Owner Revenue (OFTOt) of the licensee was determined for the Relevant Year t; and*

*(c) an event or circumstance other than listed above which, in the opinion of the Authority, is an Income Adjusting Event and is approved by it as such in accordance with paragraph 21 of this licence condition*

*where the event or circumstance has, for Relevant Year t, increased or decreased costs and/ or expenses by more than £1,000,000 (the "threshold amount")<sup>6</sup>.*

Paragraph 21 of Standard condition E12–J3 sets out that the Authority shall determine (after consultation with the licensee and such other persons as it considers desirable):

*“(a) whether any or all of the costs and/or expenses given in a notice pursuant to paragraph 14 were caused or saved by an Income Adjusting Event;*

*(b) whether the event or circumstance has increased or decreased the costs and/or expenses given in the notice pursuant to paragraph 14 by more than the threshold amount; and*

*(c) if so, whether the amount of the proposed revenue adjustment ensures that the financial position and performance of the licensee are, insofar as is reasonably practicable, the same as if that Income Adjusting Event had not taken place, and if not, the Authority shall determine what revenue adjustment would secure that effect.*

*(d) the periods, if any, over which the revenue adjustment determined by the Authority should apply”.*

These licence provisions allow the Transmission Licensees to recover costs through revenue adjustments. However, the CUSC does not currently set out the basis for such adjustments. National Grid indicated in May 2016 that revenue adjustments are recovered through changes to the wider residual. However, this is not clearly defined in the CUSC.

The current ambiguous CUSC text creates the following uncertainties for CUSC Parties:

1. It is unclear how Transmission Licensees recover actual costs incurred and costs saved associated with revenues adjustments that occur during a price control period. This uncertainty creates risks for Transmission Licensees and potentially

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<sup>6</sup> Standard condition E12–J3, (15), Generic Offshore Transmission Owner (OFTO) Licence at [https://www.ofgem.gov.uk/system/files/docs/2019/07/generic\\_ofto\\_licence\\_tr6\\_v1\\_change\\_marked\\_for\\_publication.pdf](https://www.ofgem.gov.uk/system/files/docs/2019/07/generic_ofto_licence_tr6_v1_change_marked_for_publication.pdf) where "Income Adjusting Event" has the meaning set out in paragraph 15 of amended standard condition E12–J3 (Restriction of Transmission Revenue: Allowed Pass-through Items).

- increases the cost of capital and increased risk premiums in bid prices for OFTO licences;
2. Uncertainties associated with the treatment of within year adjustments create additional risks for Users connected to the transmission system. For example, Offshore power stations connected to the transmission system face additional risks associated with the uncertain treatment of these charges which impacts on the cost of capital and could increase bid premiums for CFDs; and
  3. Users subject to residual charges may face costs as a result of uncertainties over the treatment of within year revenue adjustments. It may be difficult to recover such costs from Users, increasing market participant risks.

This modification proposal makes it clear that;

1. TNUoS tariffs will recover the MAR set at the time of the price control review for the period of the review subject to where necessary, allowing for any Kt adjustment for under or over recovery in a previous year net of the income recovered through pre-vesting connection charges ; and
2. Within price control period revenue adjustments associated with actual costs incurred and costs saved for a Transmission Licensee will be recovered through the demand residual in a manner that is fair proportionate and non- distortive. There will be no further cost recovery from Users associated with these costs.

It will address the risk for Users associated with the current uncertainty of treatment of the price control MAR and within price control revenue adjustments.

## 4 Code Specific Matters

### Technical Skillsets

Experience of the RliO-2 price controls, the charging methodologies set out in Section 14 and the arrangements for the treatment of within year revenue adjustments for Transmission Licensees and Users is required.

### Reference Documents

Offshore Transmission: Generic OFTO Licence and Guidance for TR6, Publication date 30th November 2018 at <https://www.ofgem.gov.uk/publications-and-updates/offshore-transmission-generic-ofto-licence-and-guidance-tr6>

Generic Offshore Transmission Owner (OFTO) Licence at [https://www.ofgem.gov.uk/system/files/docs/2019/07/generic\\_ofto\\_licence\\_tr6\\_v1\\_change\\_marked\\_for\\_publication.pdf](https://www.ofgem.gov.uk/system/files/docs/2019/07/generic_ofto_licence_tr6_v1_change_marked_for_publication.pdf)

National Grid Letter 27 July 2017, “Reflecting variations in Offshore Transmission Owner (OFTO) revenue in Offshore Local TNUoS Tariffs” at <https://www.nationalgrideso.com/document/94076/download>

TCMF Slides May 2016, at <https://www.nationalgrideso.com/document/48481/download>

## 5 Solution

Changes to Section 14 of the CUSC are required as follows:

*14.14.1 Transmission Network Use of System charges reflect the cost of installing, operating and maintaining the transmission system for the Transmission Owner (TO) Activity function of the Transmission Businesses of each Transmission Licensee. These activities are undertaken to the standards prescribed by the Transmission Licences, to provide the capability to allow the flow of bulk transfers of power between connection sites and to provide transmission system security.*

*14.14.2 A Maximum Allowed Revenue (MAR) defined for these activities and those associated with pre-vesting connections is set by the Authority at the time of the Transmission Owners' price control review for the succeeding price control period **and at the point of asset transfer for OFTOs**. Transmission Network Use of System Charges are set to recover the Maximum Allowed Revenue as set **at the start of the Price Control will apply for the duration of the Price Control Period** (subject to where necessary, allowing for any Kt adjustment for under or over recovery in a previous year net of the income recovered through pre-vesting connection charges).*

*14.14.2[a] Any adjustment to the Maximum Allowed Revenue that is permitted within the price control associated with actual costs incurred and costs saved for a Transmission Licensee as a result of a determination by the Authority [definition may be required] will result in a change to the Demand Residual for the period set out in the final determination of the adjustment published by the Authority.*

*Section 14 of the CUSC does not refer to any specific adjustments to the residual that allow for changes to the residual that reflect any unforeseen or unforeseeable additional cost adjustments to the demand residual. Therefore changes in Section 14 are required to allow the pass through of the revenue adjustment through the demand residual.*

## 6 Impacts & Other Considerations

- i. **Who (i.e. which industry code) is impacted** – CUSC Section 14;
- ii. **Which processes are impacted** – Charging methodologies, calculation of Demand Residual
- ii. **Systems impacted** – ESO Charging Process for Demand Residual
- iv. **Industry costs associated with the changes** - None
- v. **Any savings that may be made by industry as a result of the proposed changes** – reduced risk for Transmission Licensees and Users; and
- vi. **Any impact on the environment as a result of the changes** – Reduced risk will facilitate deployment of new Users of the system including renewable technologies.

### Does this modification impact a Significant Code Review (SCR) or other significant industry change projects, if so, how?

This modification is linked to the implementation of the RIIO-2 price controls for the Transmission Licensees with effect from April 2021.

## Consumer Impacts

The treatment of within price control adjustment to allowed revenue for Transmission licensees is currently unclear. This proposal will clarify arrangements and make it clear that any determination associated with actual costs incurred and costs saved will be recovered by changes to the demand residual. Under the TCR/SCR arrangements, such adjustments will be recovered through changes to fixed charges applied to customers. The proposed change will:

- i) Ensure that customers and suppliers understand the costs recovery process for within price control period adjustments to allowed revenue associated with actual costs incurred and costs saved for transmission Licences;
- ii) Reduce the risk for Transmission Licensees and Users, with an overall benefit of reduced cost of capital;
- iii) Facilitate deployment of low carbon generation projects and help to ensure that the Government's commitment of net zero by 2050 is met.

## 7 Relevant Objectives

### Impact of the modification on the Applicable CUSC Objectives (Charging):

Relevant Objective	Identified impact
(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;	Positive
(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);	Positive
(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;	None
(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	None

(e) Promoting efficiency in the implementation and administration of the CUSC arrangements.	Positive
*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).	

**Charging Objective (a):** This modification addresses ambiguities associated with the treatment of the MAR under the price control and the basis for the recovery of revenue adjustments. This ensures that transmission Licensees can effectively and efficiently recover allowed revenues. It will ensure that Users of the system, particularly off shore generators have greater certainty over the treatment of unforeseen and unforeseeable events. Recovery of actual costs incurred and costs saved through the demand residual result in non-discriminatory treatment of these costs in arrangements that are fair, proportionate and non-distortive approach consistent with the objectives of the TAR/SCR. Consequently the proposal will deliver effective competition in the generation and supply of electricity and (so far as is consistent therewith) and facilitates competition in the sale, distribution and purchase of electricity (Objective (a)).

**Charging Objective (b):** The modification clarifies cost recovery associated with the MAR during the price control and revenue adjustments associated with actual costs incurred and costs saved for a Transmission Licensee that could occur during a price control period. This will result in wider and local tariffs that reflect costs to the extent possible at the start of price control periods, excluding the costs of unforeseen or unforeseeable events.

The modification proposes that the actual costs incurred and costs saved associated with unforeseen or unforeseeable events are socialised through the demand residual. These actual costs incurred or saved are not therefore, recovered, from Users through adjustments to wider locational charges or through changes to local charges.

However, since the actual costs incurred or saved are unforeseen and unforeseeable and relate to events on the GB transmission system outside the control of Users connected to the GB Transmission System then it is appropriate that the costs are socialised. Users are not responsible for these events.

Furthermore, if the arrangements were to result in actual costs incurred and costs saved for specific Users then the arrangements would introduce discriminatory treatment of Users. Those Users subject to specific charges are being treated differently from other Users connected to the GB Transmission System in relation to unforeseen and unforeseeable events.

For example, actual costs incurred and costs saved may occur as a result of unforeseen and unforeseeable faults on a subsea transmission cable. If the cable is part of the MITS then the actual costs incurred or saved are socialised. A similar fault on a local

offshore circuit that forms parts of NETS could be applied exclusively to the generator connected to that circuit.

To ensure non-discriminatory treatment it is essential that all Users that are subject to actual costs incurred and costs saved are treated in the same way.

This modification proposes to ensure non-discrimination by ensuring that actual costs incurred and costs saved that are related to unforeseen or unforeseeable events are socialised in the adjustment to the Demand Residual.

This proposal removes any potential for undue discrimination in the application of the arrangements for within year cost adjustments associated with actual costs incurred and costs saved arising for unforeseen or unforeseeable events on the GB transmission system in a manner that is fair, proportionate and non-distortive.

The recovery of costs through the Demand Residual where a cost is incurred or saved which may be permitted by Ofgem should apply because it is non-discriminatory.

Furthermore the recovery of costs through the Demand Residual where a cost is incurred or saved for an unforeseen or unforeseeable event as may be permitted by Ofgem has the following benefits:

- It is consistent with the allocation of charging for onshore IAEs;
- It is consistent with the commercial arrangements of the offshore regime i.e. the generator has sold the assets via a transparent heavily scrutinised process overseen by the independent regulator;
- It allows detailed due diligence of the assets to be conducted by the purchasing OFTO;
- It enables the OFTO can take out insurance for the assets and seeks indemnity where issues are identified prior to the sale of the assets; and
- It is consistent with principles of construction law – any defects arising after the assets are sold are the responsibility of the Purchaser.

With regard to the impact of the current arrangements it is noted that:

- It is not fair or proportionate to hold the generators to account for IAEs where they would not have any responsibility under normal commercial arrangements following the sale of large scale infrastructure;
- It is not fair or proportionate for the generator to be an insurer of last resort for the OFTO especially as this was not indicated up-front;
- Developers are significantly financially impacted by all outages that occur, it is therefore unfounded to suggest that they are not motivated to develop quality transmission systems;

Under this proposal, all Users connected to the GB transmission system are treated equally irrespective of whether unforeseen or unforeseeable costs incurred or savings relate to parts of the Main Interconnected Transmission System (MITS) or parts of the National Transmission System (NETS).

These proposal better results in a use of system charging methodology which reflects, as far as is reasonably practicable, the actual costs incurred by transmission licensees

in their transmission businesses (Objective (b)). The proposed approach is compliant with relevant EU legislation, consistent with the objectives of the Target Charging Review/Significant Code Review (TCR/SCR). The proposal results in an approach that cost reflective to the extent possible, non-discriminatory, fair, proportionate and non-distortive,

**Charging Objective (d):** This modification ensure that to the extent possible the arrangements better meets compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency.

The modification proposal ensures that the CUSC better meets Regulation 2019/943 Article 18 (1) paragraph (i) which relates to:

*“Charges applied by network operators for access to networks, including charges for connection to the networks, charges for use of networks, and, where applicable, charges for related network reinforcements, shall be cost-reflective, transparent, take into account the need for network security and flexibility and reflect actual costs incurred insofar as they correspond to those of an efficient and structurally comparable network operator and are applied in a non-discriminatory manner. Those charges shall not include unrelated costs supporting unrelated policy objectives”.*

The modification proposal ensures that the CUSC better meets Regulation 2019/944 Article 6 (1) which relates to third-party access: *“Member States shall ensure the implementation of a system of third-party access to the transmission and distribution systems based on published tariffs, applicable to all customers and applied objectively and without discrimination between system users”.*

The Modification Proposal will ensure that transmission charges set at the start of the price control are cost reflective, transparent, take into account the need for network security and flexibility and reflect the actual costs incurred. Transmission tariffs will reflect the MAR set at the start of each price control.

The Modification Proposal will ensure **non-discriminatory** treatment for all transmission Users with respect to actual costs incurred or saved as a result of unforeseen or unforeseeable events that occur during a price control period.

Costs will be recovered in a fair proportionate and non-distortive manner through adjustments to the demand residual.

**Charging Objective (e):** This modification clarifies the treatment of the MAR under the price control for the duration of the price control and sets out the basis for the recovery of revenue adjustments associated with actual costs incurred and costs saved for a Transmission Licensee that occur during a price control. This improved clarity will

promote efficiency in the implementation and administration of the CUSC arrangements (Objective (e)).

## 8 Implementation

This modification proposal should be implemented for the RIIO-2 price control period from April 2021.

## 9 Legal Text

### Text Commentary

Changes to Section 14 of the CUSC are required as follows:

*14.14.1 Transmission Network Use of System charges reflect the cost of installing, operating and maintaining the transmission system for the Transmission Owner (TO) Activity function of the Transmission Businesses of each Transmission Licensee. These activities are undertaken to the standards prescribed by the Transmission Licences, to provide the capability to allow the flow of bulk transfers of power between connection sites and to provide transmission system security.*

*14.14.2 A Maximum Allowed Revenue (MAR) defined for these activities and those associated with pre-vesting connections is set by the Authority at the time of the Transmission Owners' price control review for the succeeding price control period **and at the point of asset transfer for OFTOs**. Transmission Network Use of System Charges are set to recover the Maximum Allowed Revenue as set **at the start of the Price Control will apply for the duration of the Price Control Period** (subject to where necessary, allowing for any Kt adjustment for under or over recovery in a previous year net of the income recovered through pre-vesting connection charges).*

*14.14.2[a] Any adjustment to the Maximum Allowed Revenue that is permitted within the price control associated with actual costs incurred and costs saved for a Transmission Licensee as a result of a determination by the Authority [definition may be required] will result in a change to the Demand Residual for the period set out in the final determination of the adjustment published by the Authority.*

*Section 14 of the CUSC does not refer to any specific adjustments to the residual that allow for changes to the residual that reflect any unforeseen or unforeseeable additional cost adjustments to the demand residual. Therefore Further changes in Section 14 are required to allow the pass through of the revenue adjustment through the demand residual.*

## 10 Recommendations

### Proposer's Recommendation to Panel

Panel is asked to:

- Refer this proposal to a Workgroup for assessment.

## 11 Modification guidance and using this template

### **Transmission Charging Methodology Forum**

Prior to raising a formal modification, we encourage Proposer's to bring their modification to the Transmission Charging Methodology Forum to gain industry views on the Proposal and enable the modification to be developed prior to being formally submitted.

If you would like more information, please contact The Code Administrator at [CUSC.Team@nationalgrideso.com](mailto:CUSC.Team@nationalgrideso.com)

### **Code Administrator Support**

The Code Administrator is available to help and support Proposers with the drafting of any modifications, including guidance on the completion of this template and the wider modification process.

The Code Administrator offers a service of informally reviewing draft modifications prior to them being formally submitted. This designed to assist individuals writing their modification proposal.

### **Completing this form**

Please complete all sections unless specifically marked for the Code Administrator. Green italic text is provided as guidance and should be removed before submission.