



Please use this Pro-Forma when responding to the Interim Report and Consultation of the second Balancing Services Charges Task Force.

The Taskforce will take all responses into its consideration when producing the final report. When providing a response please supply a rationale, particularly in respect of any specific questions detailed below.

Please send your responses to [chargingfutures@nationalgrideso.com](mailto:chargingfutures@nationalgrideso.com) by 5pm on **26 August 2020**. Please note that any responses received after the deadline or sent to a different email address may not be taken into account by the Taskforce.

If you have any queries on the content of this consultation, please contact us at [chargingfutures@nationalgrid.com](mailto:chargingfutures@nationalgrid.com).

Question	Response
<p>1. Do you agree with the Task Force's recommendations on who should pay Balancing Services Charges (Deliverable 1)? Please state your reasoning and evidence behind your answer.</p>	<p>Yes, we agree with the Task Force's recommendation that BSUoS costs should be recovered only from final demand.</p> <p>The first BSUoS Task Force concluded that it's not feasible to charge any components of BSUoS in a way that would influence behaviour to reduce total system costs. As such BSUoS should be treated as a cost-recovery charge.</p> <p>In light of the first BSUoS Task Force conclusion, BSUoS costs should be interpreted in the same way as network residual charges – they are costs which need to be recovered in a way which minimises distortions. As part of the TCR, Ofgem deemed these should be recovered from final demand only.</p>

	<p>Applying this principle to BSUoS costs would alleviate a number of market distortions. Currently a distortion exists between transmission and distributed generators where transmission connected generators pay BSUoS costs and embedded generators receive a BSUoS benefit. Another distortion is between GB generators and interconnected generators, where generators in other countries only pay a very small (if any) amount of balancing costs. These market distortions harm competition and can lead to inefficient dispatch which increases costs for end consumers.</p> <p>The Figure on Page 11 of the interim report shows how BSUoS costs are passed through various different markets and mechanisms before ultimately being recovered from the end consumer. Whilst difficult to quantify, economic theory would suggest that this is inefficient and would attract a series of transaction costs. Given BSUoS should be treated as purely a cost recovery mechanism and considering Ofgem's TCR principles, BSUoS should be recovered from final demand only.</p> <p>There have been suggestions that moving BSUoS costs onto suppliers would increase costs for end consumers; we do not agree with this. As mentioned above, generators pass BSUoS costs through various markets with the final cost ultimately borne by the end consumer. Due to competitive market pressure, if generators were not liable for BSUoS then the wholesale price and ancillary services market prices would fall to reflect the removal of BSUoS from a generators cost stack. This is supported by the CMA in their 2016 Energy Markets Investigation which stated that, <i>"We have considered a range of aspects of electricity wholesale market design and operation. Generally we have found that the wholesale electricity market appears to be working well"</i> and <i>"generating plant appears to be dispatched in merit order, minimising</i></p>
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	<i>short-term generating costs”.</i>
<p>2. The Task Force have discussed how the recommendation on Deliverable 1) for Final Demand only to pay Balancing Services Charges could impact on large energy users and the potential for ‘grid defection’. Do you think ‘grid defection’ is a possibility and to what extent would the Task Force’s recommendations impact on your answer?</p>	<p>We believe there is a risk of grid defection which needs to be considered particularly for larger demand users. Ongoing changes through the TCR coupled with changes to the BSUoS methodology could have a significant impact on bills for some consumers.</p> <p>Both a volumetric charge and p/site/day charge could encourage some grid defection. A volumetric charge incentivises consumers to reduce their demand by using Behind-the-Meter (BtM) generation. This “partial” grid defection would lead to others picking up some of the cost. Conversely, a p/site/day charge cannot be avoided without full grid defection. A p/site/day charge is therefore more likely to result in full grid defection particularly amongst large users who have already invested in BtM generation assets. Such full grid defection, would lead to those costs being picked up by other users who haven’t disconnected from the grid.</p> <p>However, the risk of grid defection is difficult to quantify, as it would depend on how much the cost saving would be on individual consumers’ bills. If a similar p/site/day approach was used as under the TCR, it would be highly dependent on which band a consumer was allocated to and how much money is to be recovered from that band.</p>
<p>3. Do you agree with the Task Force’s recommendations that an ex ante fixed charge would deliver overall industry benefits? Please state your reasoning and evidence behind your answer.</p>	<p>Yes, BSUoS is volatile and difficult to forecast. Adopting an ex ante fixed charge would go some way to addressing this issue.</p> <p>Market participants attempt to forecast BSUoS but given the uncertainty there is additional risk premia factored into wholesale market trades and retail contracts which is ultimately borne by end consumers. Due to it being commercially sensitive and risk appetite varying across market participants, the risk premia is difficult to quantify. However, it is assumed</p>

	<p>to be a significant amount in aggregate across the sector. Fixing BSUoS for a reasonable amount of time, with a suitable lead time, would materially reduce that risk premia and thus dramatically reduce this additional cost to the end consumer.</p> <p>Due to the volatility of BSUoS, there will be times when market participants incorrectly forecast BSUoS and as a result will be unable to recover the cost. Market participants will also rely on different BSUoS forecasts. The vagaries of these approaches, when combined with the current BSUoS methodology, results in inefficient allocation of costs across all market participants including consumers, and also leads to inefficient dispatch. Ultimately those effects distort competition.</p> <p>To summarise, BSUoS charge volatility causes uncertainty in the markets, can have a negative impact on competition and increases costs for consumers. Fixing the charge on an ex ante basis would alleviate these negative and avoidable outcomes.</p>
<p>4. How long do you think the fixed period should be and what in your opinion is the optimal notice period in advance of the fixed charge coming into effect? Please state your reasoning and evidence behind your answer.</p>	<p>We believe that a 12-month notice and 12-month fixed period is the optimal solution.</p> <p>If the notice and fixed period is “too long” then this increases the ESO’s financing costs and will likely lead to large step changes in charges between periods due to over/ under recovery, which is not efficient for the ESO or the market. On the other hand, if the notice and fixed period are “too short”, then this will not overcome the current issues as it will not enable suppliers to accurately price BSUoS into contracts due to its volatility and contracting timescales. Similar to the status quo this would inevitably result in the application of significant risk premia, the cost of which is ultimately borne by consumers.</p> <p>It’s common practice for suppliers to offer fixed contracts up to 4 years in duration</p>

	<p>and up to 12 months in advance. While there will always be some risk, fixing BSUoS with 12-month notice for 12-months will significantly help suppliers price BSUoS into contracts and manage the risk of changes between fixed periods. We do not believe this would be too burdensome for the ESO and we would support provision for this being included in their price control to provide them with additional certainty.</p>
<p>5. Which approach discussed by the Task Force (TDR banded £/site/day or volumetric £/MWh) do you feel is most appropriate for Balancing Services Charges? Please consider your answer against the TCR principles and state your reasoning and evidence to support your answer.</p>	<p>Both options have advantages and disadvantages but on balance we believe a volumetric BSUoS charge is most appropriate.</p> <p><b><u>Method: TCR p/site/day</u></b></p> <p>Fundamentally, Use of System (TNUoS, DUoS) costs are driven by the size of a customer's connection and at what voltage level they connect, so the TCR banded approach for recovering Use of System residual costs is intuitive in that context. A network users contribution towards BSUoS costs are not driven by the size of a user's connection. As such, recovering BSUoS costs as per the TCR banded p/site/day approach is not appropriate.</p> <p>Using a TCR style p/site/day approach to recover BSUoS costs would have a large distributional impact with a greater proportion of costs likely falling onto large consumers compared to the status quo. Also, as noted in our response to question 2, a p/site/day charge implicitly incentivises full grid defection, which would have a material impact on other parties if it happened at scale. Additionally, any banded approach would require some form of dispute process to be established so consumers are able to challenge their band allocation.</p> <p>On the other hand, this method would ensure that the BSUoS charging methodology didn't incentivise customers to use BtM generation, we explore this in</p>

	<p>more detail below.</p> <p><b><u>Method: volumetric</u></b></p> <p>A volumetric approach would provide a benefit to customers with BtM generation that isn't available to others. Through using BtM generation a network user could avoid BSUoS costs which would lead to the avoided cost being socialised across other users. This approach could also introduce a distortion between BtM generators and all other generators who are competing in the wholesale and ancillary services markets. However, we note BSC modification P375 is looking at metering behind the boundary point and this could potentially be used to distinguish a customer's demand volume from that of their BtM generation. If that modification is approved, then it may be possible to implement a volumetric BSUoS charge that doesn't create an undue benefit to BtM generation.</p> <p>Using the volumetric approach would be easier and less costly for suppliers to implement. The TCR p/site approach is yet to be implemented and suppliers have frequently expressed their concerns around systems and implementation.</p> <p><b><u>In conclusion</u></b></p> <p>In accordance with the broader TCR principles, we believe a volumetric charge is marginally "fairer" and more greatly "reduces harmful distortions" compared to a banded p/site/day charge. We also believe a volumetric charge is more "practical and proportionate" to implement compared to a banded p/site/day charge.</p> <p>Notwithstanding that conclusion, any impact assessment from Ofgem needs to carefully consider these two charging options with relevant supporting analysis to inform the decision.</p>
6. The Task Force noted	Should a p/site/day approach be taken forward it may not be appropriate for it to

<p>limitations of the approaches covered in Q5, what other aymethodologies or improvements to the ones in Q5 could you recommend to tackle them? Please consider your answer against the TCR principles and state your reasoning and evidence to support your answer.</p>	<p>be identical to the approach taken in the TCR. The TCR banding system uses a consumers capacity and voltage level to determine the amount of residual costs they should be liable for, BSUoS costs are not driven by the connection size of a network user and so banding in this way to recover BSUoS costs wouldn't be appropriate.</p>
<p>7. Is 2years' notice of the changes prior to an implementation date appropriate? Please state your reasoning and evidence behind your answer.</p>	<p>Yes, as a minimum. It's common practice for suppliers to offer fixed contracts up to 4 years in duration and up to 1 year in advance. Given the magnitude of this change, we believe that a minimum of 2 years' notice is necessary to ensure that BSUoS can be accurately priced into consumer contracts and wholesale market activity. Without sufficient implementation lead-time there would be a negative impact on competition. This is due to potential windfall gains for generators and losses for suppliers, the magnitude of which will vary between different parties based on their hedged / contracted position. What's more, an insufficient lead time could incentivise suppliers to remove longer duration contracts and longer lead-time contracts to the detriment of consumer choice.</p> <p>We share the same concerns as other generators regarding the market distortions currently caused by BSUoS but believe that an April 2023 implementation is a pragmatic and fair compromise given the serious implementation concerns of suppliers. We would welcome certainty on the implementation timing as soon as possible.</p>
<p>8. Should the Task Force consider any interim measures? Please provide details of any suggested interim solution including how it may deliver benefits to consumers or help to mitigate specific challenges facing</p>	<p>No, we do not believe it is appropriate for the Task Force to consider interim measures. This would delay the conclusions of the Task Force and increase the uncertainty that currently exists regarding BSUoS charges. The Task Force should focus on determining the most optimal enduring BSUoS solution that can be implemented as soon as</p>

market participants, whilst limiting any windfall gains or losses between industry participants.	<p>practicable allowing for adequate lead-time.</p> <p>The open governance CUSC arrangements would be the appropriate mechanism should parties wish to raise an interim solution.</p>
9. Do you feel that there any interactions with the Supplier Price Cap that need to be considered? Please state your reasoning and evidence behind your answer.	We are not active in the domestic supply market and so have no comment.
10. The Task Force's initial recommendation is that Final Demand only will pay BSUoS. If this is the case, is the current RCRC mechanism is still appropriate? Please state your reasoning and evidence behind your answer.	We do not have a view on this currently and do not believe interactions with RCRC need to be considered by the Task Force. That said, should Ofgem direct that changes are made to BSUoS, it would be appropriate to look at RCRC as part of the modification process to ensure it remains fit for purpose.
11. Is there anything further you think the Task Force needs to consider?	No.
12. Please use this box to add any further comments that you may have	N/A.