

### Purpose of this note

This note is a brief guide to Ofgem's Targeted Charging Review (TCR) final decision.

### Executive summary

Ofgem's TCR has considered:

- › How electricity network residual charges should be set in future, for both transmission and distribution
- › The differences between charges faced by smaller distributed generators and larger generators, also known as "Embedded Benefits"

Ofgem has used the outputs from a series of stakeholder workshops along with its analysis and industry consultation to reach a final decision.

Ofgem has decided that:

- › Residual charges will be levied in the form of fixed charges for domestic and commercial demand users only.
- › The Transmission Generation Residual will be set at zero therefore transmission generators will no longer receive the current negative residual charge.
- › Balancing Services Charges will be charged to Suppliers on a gross basis, which will remove the "Embedded Benefit" for distributed generators.
- › A Second BSUoS Task Force will take place to consider who should pay Balancing Services Charges and how should the charges be recovered.

**Ofgem has decided that the implementation date for the TCR is 1<sup>st</sup> April 2021 for changes to occur at the Transmission level and 1<sup>st</sup> April 2022 for the Distribution level.**

### What's driving change?

#### Residual Charges

Current network charges include forward-looking charges designed to encourage people to use the networks efficiently through price signals. They also include residual charges which are designed to recover remaining costs and are socialised among network users. Residual charges are not designed to provide incentives to use networks in any particular way. If residual charges provide strong incentives which change how the networks are

used and provide different signals to similar parties then it can distort competition between different network users and can potentially lead to unfair outcomes, particularly for consumers.

Demand residual charges are currently based on demand usage over Triads; three points of time in the year where demand is at its peak, separated by 10 clear days. Some users predict Triad periods and reduce their demand at these times to reduce their residual charges. Since the total costs to be recovered through residual charges remain the same, the charges falling on remaining consumers, who can't vary their use, will increase.

Ofgem believes that the residual charge should not provide a signal, and therefore it is unfair that some users are able to avoid these charges, whereas others cannot.

### **Embedded Benefits**

As part of the TCR, Ofgem also considered the differences in charging arrangements for transmission connected generators and embedded generators, also known as non-locational "Embedded Benefits". There were two areas which Ofgem considered:

- Today, Smaller Distributed Generators are not currently liable for paying balancing services charges (BSUoS) and can receive payments for reducing suppliers' liabilities for balancing service charges. However, generation connected at transmission must pay for balancing services charges. This difference between transmission and distribution has resulted in it being a focus area for Ofgem under the TCR.
- Separately, under current arrangements, there is a negative transmission generation residual (TGR). This is due to a European Regulation, which sets out that generation can only pay between €0 and €2.50 per MWh on average in transmission network charges. To ensure compliance with this regulation today, the residual is negative for transmission generators to keep them within the €0 – €2.50 range. As distributed generators do not receive this same negative residual, this was part of Ofgem's TCR scope.

## **How has Ofgem reached its decision?**

Ofgem evaluated options for potential changes against the following three principles:

- > 1. reducing distortions
- > 2. fairness
- > 3. proportionality and practical considerations.

In November 2017, Ofgem published a working paper setting out its initial thinking, and the plan for further work. Since releasing this paper, Ofgem has held a series of stakeholder workshops to allow industry an opportunity to feed their views into the process, and has conducted an analysis of potential changes to residual charges, the results of which it published in a minded-to decision in December 2018. This was followed by two industry consultations in June and September 2019 and a final TCR decision published on 21<sup>st</sup> November 2019.

Visit [www.chargingfutures.com](http://www.chargingfutures.com) for more information

The implementation date for TCR has been set for 1<sup>st</sup> April 2021 for Transmission with an implementation date of 1<sup>st</sup> April 2022 for the Distribution level.

## Ofgem's TCR decision

### **Residual Charges:**

Ofgem decided that residual charges are to be paid by final demand only. The charges will also no longer be based on Triads. Demand users will be allocated bands which will be based on consumption volume at each voltage level and be given a fixed charge based on their band. Domestic users will be placed in their own band and be charged their own fixed tariff. Users are also to remain in their band for the duration of each RIIO Transmission Owner 5 year price control period.

### **Non-locational Embedded Benefits**

Supplier's Balancing Services Use of System (BSUoS) charges are to be charged on gross imports of electricity at the Grid Supply Point instead of net imports. This will remove the benefit for embedded generators, who previously received a payment for reducing Supplier's overall BSUoS liability.

Ofgem decided that the Transmission Generation Residual will be set to zero, removing the negative charge which was paid to transmission generators. To ensure compliance with EU law is maintained, ESO will be carrying out this work alongside the existing code modification CMP317<sup>1</sup>.

### **Second BSUoS Task Force**

An ESO led BSUoS Task Force concluded in May 2019 that the current BSUoS charge does not provide any useful forward-looking signals to improve operation of the balancing market and that all BSUoS charges should be treated as cost recovery.

In order to develop this work further, Ofgem have decided a second ESO Task Force will be launched with the aims of finding out:

- › **Who should pay balancing services charges?**
- › **What should the structure of the charge be?** – What should the methodology and the frequency of the charge be?
- › **How can the three TCR principles be applied to BSUoS charges?**

The Task Force will publish its findings in an Interim Report with initial conclusions in April 2020. A Final Report containing final conclusions and recommendations will be published in June 2020.

## What are the next steps?

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<sup>1</sup> More information on CMP317 can be found on the ESO website [here](#).

A joint Project Initiation Document between ESO, the DNOs and Elexon, which outlines the steps industry is going to take to deliver TCR in greater detail, can be viewed [here](#).

As set out in the plan, the ESO and the DNOs will raise the necessary code modifications to enable change to existing frameworks to allow the implementation of the new arrangements set out by the TCR decision.

A Second BSUoS Task Force will commence work in January 2020 in order to carry out work into finding out who should pay balancing service charges and what the structure of the charge should be. They will publish their conclusions and recommendations in a Final Report in June 2020.

## How can you get involved or find out more?

### Contribute

- › You can take part in the code modification process by becoming involved in CUSC or DCUSA working groups by contacting [cusc.team@nationalgrideso.com](mailto:cusc.team@nationalgrideso.com) or [dcusa@electralink.co.uk](mailto:dcusa@electralink.co.uk) or by participating in consultations through responding to CUSC or DCUSA emails.
- › You can take part in BSUoS Task Force consultations. More information on the Task Force is available via the [Charging Futures Website](#) or via the Charging Futures mailing list. To join the mailing list please email Charging Futures at [chargingfutures@nationalgrideso.com](mailto:chargingfutures@nationalgrideso.com)

### Learn

- › You can read Ofgem's full published TCR decision [here](#).
- › You can hear Ofgem explain its decision in the Charging Futures webinar [here](#). The slides can be viewed [here](#).
- › You can watch ESO's webinar explaining what industry changes and transmission code modifications will take place [here](#).
- › You can catch up with the 12<sup>th</sup> March 2020 Charging Futures Forum Webinar [here](#). ESO discusses the current progress with industry code modifications and there is an update from the Balancing Services Task Force.
- › You can keep up to date with developments in TCR, as well as find other supporting materials on our [website](#).

### Ask

- › If you have a query on the TCR, please contact Ofgem at [TCR@ofgem.gov.uk](mailto:TCR@ofgem.gov.uk)
- › For general queries on Charging Futures and how you can get involved, email the ESO, Lead Secretariat for Charging Futures at [chargingfutures@nationalgrideso.com](mailto:chargingfutures@nationalgrideso.com) or visit [www.chargingfutures.com](http://www.chargingfutures.com)