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| CUSC Modification Proposal Form | At what stage is this document in the process? |
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CMP286

Mod Title: Improving TNUoS Predictability Through Increased Notice of the Target Revenue used in the TNUoS Tariff Setting Process.

| | |
|----|---------------------------------|
| 01 | Proposal Form |
| 02 | Workgroup Consultation |
| 03 | Workgroup Report |
| 04 | Code Administrator Consultation |
| 05 | Draft CUSC Modification Report |
| 06 | Final CUSC Modification Report |

Purpose of Modification: The purpose of this modification proposal is to improve the predictability of TNUoS demand charges by bringing forward the date at which the target revenue used in TNUoS tariff setting is fixed to allow customer prices to more accurately reflect final TNUoS rates.

| | |
|---|--|
|  | <p>The Proposer recommends that this modification should be:</p> <ul style="list-style-type: none"> assessed by a Workgroup and determined by the Authority <p>This modification was raised on 10 October 2017 and will be presented by the Proposer to the Panel on 20 October 2017. The Panel will consider the Proposer’s recommendation and determine the appropriate route.</p> |
|  | <p>High Impact: Suppliers, Generators, embedded generators and National Grid</p> |
|  | <p>Medium Impact: None</p> |
|  | <p>Low Impact: None</p> |

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| Draft Timetable | |  email address |
| The Code Administrator recommends the following timetable: | |  telephone |
| Initial consideration by Workgroup | w/c 27/11/2017 | |
| Workgroup Consultation issued to the Industry (15 WD) | 02/05/2018 | |
| Modification concluded by Workgroup | 18/07/2018 | |
| Workgroup Report presented to Panel | 27/07/2018 | |
| Code Administration Consultation Report issued to the Industry (15 WD) | 30/07/2018 | |
| Draft Final Modification Report presented to Panel | 23/08/2018 | |
| Modification Panel decision | 31/08/2018 | |
| Final Modification Report issued the Authority | 07/09/2018 | |
| Indicative Authority Decision Date | 05/10/2018 | |
| Decision implemented in CUSC | 01/04/2019 | |
| | |  email address |
| | |  telephone |
| | | Contact: Code Administrator |
| | |  email address |
| | |  telephone |
| | | Proposer: Insert name |
| | |  email address |
| | |  telephone |
| | | National Grid Representative: Insert name |
| | |  email address. |
| | |  telephone |

Proposer Details

| | |
|--|--|
| Details of Proposer: (Organisation Name) | npower |
| Capacity in which the CUSC Modification Proposal is being proposed: (i.e. CUSC Party, BSC Party or "National Consumer Council") | CUSC Party |
| Details of Proposer's Representative: Name: Organisation: Telephone Number: Email Address: | Daniel Hickman npower 0121 336 5256 daniel.hickman@npower.com |
| Details of Representative's Alternate: Name: Organisation: Telephone Number: Email Address: | George Douthwaite npower 0121 336 5322 george.douthwaite@npower.com |
| Attachments (Yes/No): If Yes, Title and No. of pages of each Attachment: | |

Impact on Core Industry Documentation.
Please mark the relevant boxes with an "x" and provide any supporting information

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

(Please specify)

This is an optional section. You should select any Codes or state Industry Documents which may be affected by this Proposal and, where possible, how they will be affected.

1 Summary

Defect

Final TNUoS tariffs are published with a notice period of only 2 months. Suppliers are particularly vulnerable to the short notice period and are reliant on forecasting TNUoS tariffs many months ahead to provide their customers with the fixed price contracts they require.

A typical domestic or business customer, whose meter is settled on non-half hourly data (NHH), and agrees a two-year fixed price contract with their supplier will have TNUoS costs reflected within their contract rates. This will comprise a best view forecast plus an element of risk based on volatility and unpredictability of this charge for the period where final tariffs have not yet been published. If we consider a NHH two-year contract starting in October, TNUoS tariffs are only known for a quarter of the contracted period, the remaining three-quarters being reliant on a forecast.

TNUoS tariffs are set by National Grid System Operator (SO) populating a number of inputs into the charging methodology models. Whilst there are some aspects of TNUoS forecasting which are manageable by suppliers and generators, many of these inputs are difficult to predict and are not finalised until shortly before final tariff publication. This creates uncertainty around the level of final tariffs. An example of this is the revenues used for final tariff setting (Target Revenue).

In recent years, we have observed large changes in these Target Revenue inputs between National Grid's forecasts over a short period of time. The impact of these input changes have shown significant shifts in the tariff level between National Grid's own quarterly forecasts, draft and final tariffs. While National Grid SO are not responsible for providing this information, the National Grid Quarterly Forecasts are a key source of information for these inputs. These shifts in Target Revenue causes uncertainty and price shifts across the market. This can result in customers' bills which are not reflective of the costs that suppliers have incurred. Given that market participants are trying to predict TNUoS costs as accurately as possible, large and late changes of Target Revenue inputs which significantly affect the calculation of TNUoS prices need to be avoided.

The following tables show the forecast of Target Revenue (Total to Collect from TNUoS) from the National Grid quarterly updates of the 17/18 Tariff forecast and also the variance between forecasts.

| 17/18 Forecast £m | Feb-15 | Feb 2016 Initial View | June 2016 Update | Oct 2016 Update | Dec 2016 Draft | Final |
|---------------------------------------|----------------|--------------------------------------|---------------------------------|--------------------------------|-------------------------------|----------------|
| National Grid | | | | | | |
| <i>Price controlled revenue</i> | 1,818.0 | 1,806.4 | 1,811.2 | 1,750.4 | 1,753.4 | 1,748.8 |
| <i>Less income from connections</i> | 48.3 | 46.5 | 46.5 | 44.1 | 44.0 | 41.9 |
| Income from TNUoS | 1,769.7 | 1,760.0 | 1,764.7 | 1,706.3 | 1,709.5 | 1,706.9 |
| | - | | | | | |
| Scottish Power Transmission | - | | | | | |
| <i>Price controlled revenue</i> | 368.5 | 347.1 | 341.0 | 327.7 | 333.5 | 333.7 |
| <i>Less income from connections</i> | 10.9 | 13.9 | 14.0 | 11.4 | 11.4 | 12.8 |
| Income from TNUoS | 357.6 | 333.1 | 327.0 | 316.3 | 322.1 | 321.0 |
| | - | | | | | |
| SHE Transmission | - | | | | | |
| <i>Price controlled revenue</i> | 347.6 | 328.5 | 327.3 | 305.8 | 312.6 | 304.7 |
| <i>Less income from connections</i> | 3.7 | 3.6 | 3.6 | (13.6) | (14.6) | 3.4 |
| Income from TNUoS | 344.0 | 324.9 | 323.7 | 319.4 | 327.2 | 301.4 |
| | - | | | | | |
| Offshore | 284.8 | 276.5 | 279.2 | 293.0 | 274.1 | 270.2 |
| Network Innovation Competition | 49.7 | 40.5 | 40.5 | 40.5 | 33.1 | 32.1 |
| Total to Collect from TNUoS | 2,805.8 | 2,735.0 | 2,735.1 | 2,675.6 | 2,666.0 | 2,631.5 |

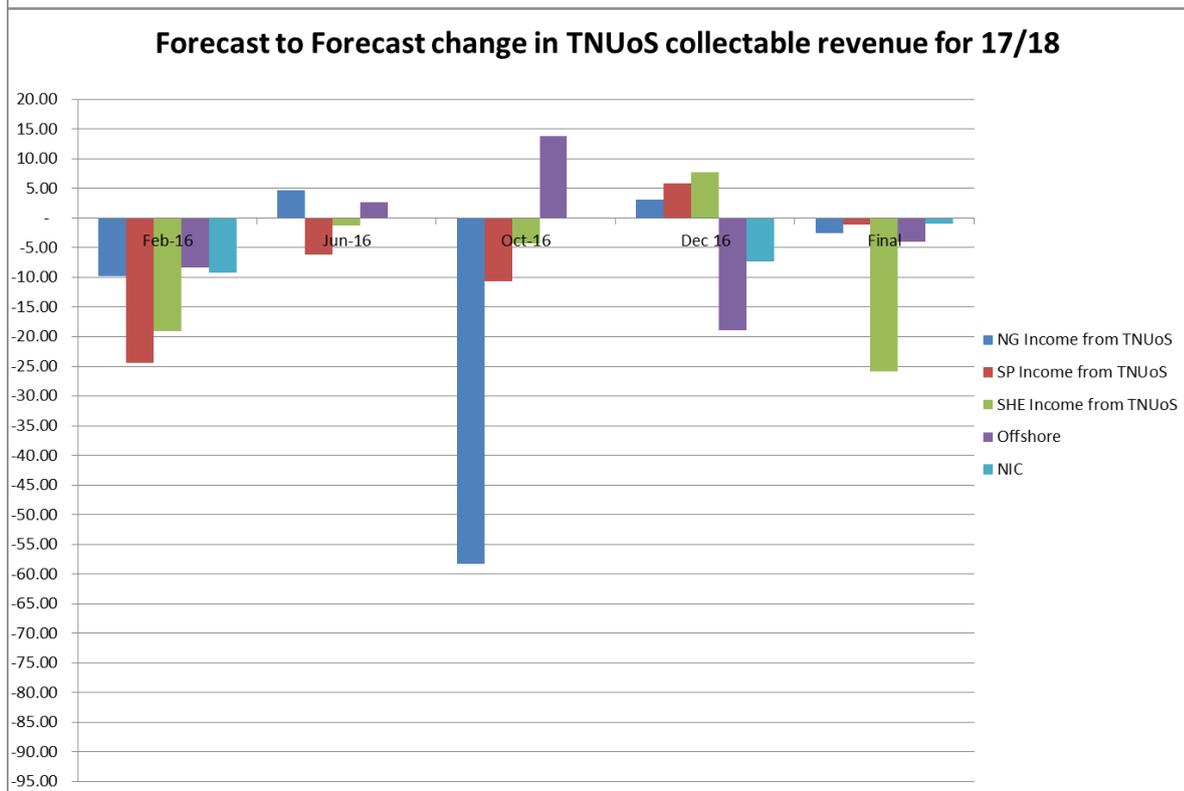
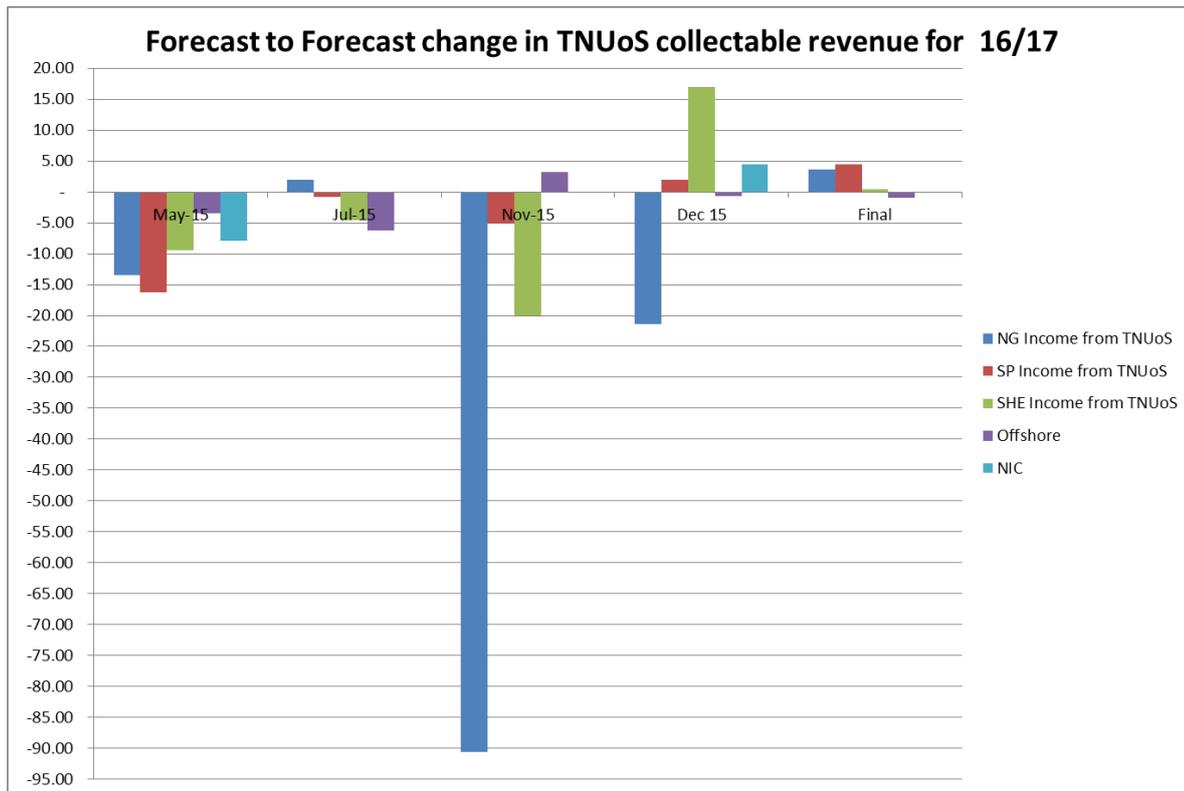
| forecast to forecast change £m | Feb 2016 Initial View | June 2016 Update | Oct 2016 Update | Dec 2016 Draft | Final |
|---|--------------------------------------|---------------------------------|--------------------------------|-------------------------------|---------------|
| National Grid | | | | | |
| <i>Price controlled revenue</i> | (11.5) | 4.8 | (60.8) | 3.0 | (4.6) |
| <i>Less income from connections</i> | (1.8) | - | (2.4) | (0.1) | (2.1) |
| Income from TNUoS | (9.7) | 4.8 | (58.4) | 3.1 | (2.6) |
| | | | | | |
| Scottish Power Transmission | | | | | |
| <i>Price controlled revenue</i> | (21.5) | (6.1) | (13.3) | 5.8 | 0.2 |
| <i>Less income from connections</i> | 3.0 | 0.1 | (2.6) | - | 1.4 |
| Income from TNUoS | (24.5) | (6.1) | (10.7) | 5.8 | (1.1) |
| | | | | | |
| SHE Transmission | | | | | |
| <i>Price controlled revenue</i> | (19.1) | (1.2) | (21.4) | 6.8 | (7.9) |
| <i>Less income from connections</i> | (0.1) | - | (17.2) | (1.0) | 18.0 |
| Income from TNUoS | (19.1) | (1.2) | (4.3) | 7.8 | (25.8) |
| | | | | | |
| Offshore | (8.3) | 2.7 | 13.8 | (18.9) | (3.9) |
| Network Innovation Competition | (9.2) | - | - | (7.4) | (1.0) |
| Total to Collect from TNUoS | (70.8) | 0.1 | (59.5) | (9.6) | (34.5) |

This issue is not confined to the forecast of 17/18 revenues similar volatility can be seen in the forecast of 2016/17 revenue as shown in the tables below.

| 16/17 Forecast £m | Jan-15 | May-15 | Jul-15 | Nov-15 | Dec 15 | Final |
|---------------------------------------|----------------|----------------|----------------|----------------|----------------|----------------|
| National Grid | | | | | | |
| <i>Price controlled revenue</i> | 1,953.8 | 1,937.0 | 1,938.8 | 1,848.9 | 1,827.5 | 1,828.2 |
| <i>Less income from connections</i> | 48.3 | 45.0 | 45.0 | 45.6 | 45.6 | 42.7 |
| Income from TNUoS | 1,905.5 | 1,892.0 | 1,893.9 | 1,803.3 | 1,781.9 | 1,785.5 |
| | | | | | | |
| Scottish Power Transmission | | | | | | |
| <i>Price controlled revenue</i> | 321.0 | 303.1 | 302.3 | 300.7 | 302.6 | 306.4 |
| <i>Less income from connections</i> | 10.5 | 8.9 | 8.9 | 12.4 | 12.4 | 11.8 |
| Income from TNUoS | 310.5 | 294.2 | 293.4 | 288.3 | 290.2 | 294.6 |
| | | | | | | |
| SHE Transmission | | | | | | |
| <i>Price controlled revenue</i> | 343.0 | 333.6 | 329.0 | 309.0 | 325.9 | 326.2 |
| <i>Less income from connections</i> | 3.6 | 3.5 | 3.5 | 3.5 | 3.5 | 3.4 |
| Income from TNUoS | 339.5 | 330.1 | 325.5 | 305.5 | 322.4 | 322.8 |
| | | | | | | |
| Offshore | 269.1 | 265.6 | 259.3 | 262.5 | 261.8 | 260.8 |
| Network Innovation Competition | 48.4 | 40.5 | 40.5 | 40.5 | 44.9 | 44.9 |
| Total to Collect from TNUoS | 2,873.0 | 2,822.4 | 2,812.6 | 2,700.1 | 2,701.2 | 2,708.7 |

| forecast to forecast change | May-15 | Jul-15 | Nov-15 | Dec 15 | Final |
|---------------------------------------|---------------|---------------|----------------|---------------|--------------|
| National Grid | | | | | |
| <i>Price controlled revenue</i> | (16.8) | 1.8 | (89.9) | (21.4) | 0.7 |
| <i>Less income from connections</i> | (3.3) | - | 0.6 | - | (2.9) |
| Income from TNUoS | (13.5) | 1.9 | (90.6) | (21.4) | 3.6 |
| | | | | | |
| Scottish Power Transmission | | | | | |
| <i>Price controlled revenue</i> | (17.9) | (0.8) | (1.6) | 1.9 | 3.8 |
| <i>Less income from connections</i> | (1.6) | - | 3.5 | - | (0.6) |
| Income from TNUoS | (16.3) | (0.8) | (5.1) | 1.9 | 4.4 |
| | | | | | |
| SHE Transmission | | | | | |
| <i>Price controlled revenue</i> | (9.4) | (4.6) | (20.0) | 16.9 | 0.3 |
| <i>Less income from connections</i> | (0.1) | - | - | - | (0.1) |
| Income from TNUoS | (9.4) | (4.6) | (20.0) | 16.9 | 0.4 |
| | | | | | |
| Offshore | (3.5) | (6.3) | 3.2 | (0.7) | (1.0) |
| Network Innovation Competition | (7.9) | - | - | 4.4 | - |
| Total to Collect from TNUoS | (50.6) | (9.8) | (112.5) | 1.1 | 7.5 |

The charts below show the variations to forecast Target Revenue (in £million) broken down by Transmission Operator, from one quarterly forecast update to the next update or final tariffs.



It clearly shows the volatility in TNUoS revenue forecasts provided by the TO's

What

Forecasts of Target Revenue that feed into the TNUoS tariff setting process are currently volatile and can have significant impact to commercial arrangements offered to customers. These Target Revenue forecast changes are a significant driver of unpredictable tariff volatility which can result in customers' bills which are not reflective of the costs that suppliers have incurred.

How

The date at which Target Revenue is fixed should be brought forward to align customer pricing timeline expectations. We would suggest that these inputs should be fixed 15 months ahead of tariffs going live (i.e. 31st December yy for tariff year yy+2/yy+3). This aligns with supplier / customer pricing timeline expectations and is consistent with the timescales committed to by DNOs. To facilitate this, we would also suggest the Annual Iteration Process that takes place between July and November of Year yy should be concerned with setting Mod term for tariff year yy+2/yy+3 rather than yy+1/yy+2.

2 Governance

Justification for Normal Procedures

This modification should follow the normal governance procedure.

Requested Next Steps

This modification should be assessed by a Workgroup

Requested Next Steps

This modification should:

- be assessed by a Workgroup

3 Why Change?

Forecasts of Target Revenue that feed into the TNUoS tariff setting process are currently volatile and can have significant impact to commercial arrangements offered to customers. These input changes are a significant driver of unpredictable volatility.

A typical domestic or business customer, whose meter is settled on non-half hourly data (NHH), and agrees a two-year fixed price contract with their supplier will have reflected within their contract rates TNUoS cost. This will comprise a best view forecast plus an element of risk based on volatility and unpredictability of this charge for the period where final tariffs have not yet been published. If we consider a NHH two-year contract starting in October, TNUoS tariffs are only known for a quarter of the contracted period, the remaining three-quarters being reliant on a forecast.

In recent years, we have observed large changes in these Target Revenue inputs between National Grid's forecasts over a short period of time. The impact of these input changes have been significant shifts in the tariff level between National Grid's own quarterly forecasts, draft and final tariffs. While National Grid SO are not responsible for

providing this information, the National Grid Quarterly Forecasts are a key source of information for these inputs. These shifts in Target Revenue cause uncertainty and price shifts across the market. This can result in customers' bills which are not reflective of the costs that suppliers have incurred. Given that market participants are trying to predict TNUoS costs as accurately as possible for customer pricing, large and late changes of Target Revenue inputs, which will significantly affect the calculation of TNUoS prices, need to be avoided.

Locking down the Target Revenue input into the TNUoS pricing process much earlier in the process removes this element of uncertainty and will allow suppliers to more accurately reflect the final TNUoS tariffs in customers' bills. It will reduce the risk premia.

4 Code Specific Matters

Mandatory for the Proposer to complete. Please provide any specialist information (that is Code-specific), such as technical skillsets required and any reference documents.

Technical Skillsets

Insert text here *Provide the required technical skillset that will be required to assess this modification.*

Reference Documents

Insert text here *Provide any reference documents that need to be considered.*

5 Solution

The date at which Target Revenue is fixed should be brought forward to align customer pricing timeline expectations. We would suggest that these inputs should be fixed 15 months ahead of tariffs going live (i.e. 31st December yy for tariff year yy+2/yy+3). This aligns with supplier / customer pricing timeline expectations and is consistent with the timescales committed to by DNOs. To facilitate this, we would also suggest the Annual Iteration Process that takes place between July and November of Year yy should be concerned with setting Mod term for tariff year yy+2/yy+3 rather than yy+1/yy+2.

6 Impacts & Other Considerations

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

We do not believe this modification impacts any areas within the scope of the current SCR

Consumer Impacts

Customer costs reduced through a reduction in supplier risk premia since there will be more certainty around TNUoS forecasts.

Customers' bills will be more reflective of the costs that suppliers incur.

7 Relevant Objectives

Mandatory for the Proposer to complete. Please delete the CUSC Objectives that is not applicable.

| 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. | None |
| *Objective (c) refers specifically to European Regulation 2009/714/EC. Reference to the Agency is to the Agency for the Cooperation of Energy Regulators (ACER). | |

Final TNUoS tariffs are published with a notice period of only 2 months. Suppliers are particularly vulnerable to the short notice period and are reliant on forecasting TNUoS tariffs many months ahead to provide their customers with the fixed price contracts they require.

This modification will give more certainty to inputs into the TNUoS Charging Methodology that market participants cannot forecast, thereby making the costs that customers pay more reflective of the final charge and consequently reduce the risk premia charged by suppliers. This will reduce the price distortions in the competitive market thereby facilitating effective competition in retail energy supply.

8 Implementation

As soon as practicably possible.

9 Legal Text

Legal text changes to be developed by the working group

10 Recommendations

Proposer's Recommendation to Panel

Panel is asked to:

- Agree that Normal governance procedures should apply
- Refer this proposal to a Workgroup for assessment.