

Final Self – Governance Modification Report

CMP342: Clarification of VAT for Securities in the CUSC

Overview: This modification seeks to clarify, and confirm the position that National Grid ESO (NGESO) has always applied, that when calculating the amount Users are required to secure under the CUSC, the amount of applicable Value Added Tax (VAT) is to be included.

Modification process & timetable



Have 5 minutes? Read our Executive summary

Have 15 minutes? Read the full Final Self-Governance Modification report

Have 20 minutes? Read the full Final Self-Governance Modification report and annexes

Status summary: The CUSC Panel have, by majority, determined that this should be implemented.

This modification is expected to have a: **Low impact on all Users.**

Governance route¹	This modification has proceeded straight to Code Administrator Consultation and the Panel has made the decision on whether it should be implemented.	
Who can I talk to about the change?	<p>Proposer: Nick George, National Grid ESO</p> <p>Nick.George@nationalgrideso.com</p>	<p>Code Administrator: Paul Mullen</p> <p>paul.j.mullen@nationalgrideso.com</p> <p>07794 537 028</p>

¹ The CUSC Panel in May 2020 had unanimously agreed that CMP342 should follow the self-governance route and proceed to Code Administrator Consultation. At July 2020 Panel, the Code Administrator shared that there had been a challenge on material impacts of the proposed change from a respondent to the Code Administrator Consultation. Therefore, the Panel agreed to defer decision on the appropriate governance route to the August 2020 Panel. At the August 2020 Panel, Panel agreed by majority to maintain their decision that CMP342 should follow the self-governance route.

Appeals window	If you want to appeal this decision, please send your appeals form and relevant documentary evidence to industrycodes@ofgem.gov.uk by 5pm on 2 October 2020 and ensure you copy in cusc.team@nationalgrideso.com
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Executive Summary

CMP342 intends to clarify the position on VAT and securities, confirming the approach that NGENSO has always taken when calculating the amount to be secured.

This will ensure that there is no ambiguity when interpreting the CUSC and that the amount Users are required to secure, will include Value Added Tax (VAT).

What is the issue?

The CUSC includes requirements for Users to provide security for certain charges. NGENSO includes the applicable VAT when calculating the amount to be secured, as the amount payable by a User to NGENSO includes payment of VAT. A User has queried NGENSO's right to request security for the VAT element of the charges.

What is the solution and when will it come into effect?

Proposer's solution:

Amend the relevant sections of the CUSC to clarify that the security calculation is based on the relevant charge including the applicable VAT.

Implementation date:

9 October 2020 (5 working days after the appeals window closes) providing no appeals are received by 5pm on 2 October 2020.

Panel recommendation:

The CUSC Panel have, by majority, determined that this should be implemented.

What is the impact if this change is made?

Who will it impact?

This modification may have a low impact on all Users.

Interactions

None.

Final Self – Governance Modification Report

This document is the CMP342 **Final Self–Governance Modification Report**. This document outlines:

- **What is the issue?**
- **What is the solution?**
 - Proposer’s solution
 - Legal text
- **What is the impact of this change?**
- Code Administrator Consultation Summary
- Panel Determination Vote
- **When will the change taken place?**
- Acronym table and reference material

What is the issue?

What is the issue?

The CUSC includes requirements for Users to provide security for certain charges. The intention and practise is that NGESO includes the applicable VAT when calculating the amount to be secured, as the amount payable by a User to NGESO includes payment of VAT. A User has queried NGESO’s right to request security for the VAT element of the charges. To ensure current and future parties fully understand their obligations, NGESO believe a modification to the code to clarify this provision is appropriate.

The relevant provisions of code that need amending are:

- Section 2, Part III - security for Terminations Amounts, relating to Connection Charges
- Section 3, Part III – security for BSUOS and TNUOS Demand Charges
- Section 15, Part Three – security for Cancellation Charges for generators terminating pre-connection
- Schedule 2, Exhibit 3 – security for Final Sums for demand customers terminating pre-connection

Why is it an issue?

The security requirements provide financial security from Users for all or a proportion of charges, reducing the financial risk on all other Users from a User defaulting on payment obligations. In the event of a User defaulting, the VAT must still be paid to HMRC, and therefore it is important when calculating the amount that a Customer secures that it includes the applicable VAT. This has always been NGESO’s practice (for the avoidance of doubt, including its predecessor, National Grid Electricity Transmission plc).

What is the solution?

Proposer's solution:

The changes set out in the Final Legal Text below, are made to clarify that the amounts Users are required to secure shall include the applicable VAT.

Final Legal text

The final legal text for this change can be found below:

- In CUSC paragraph 2.21.2(a), insert “(inclusive of any applicable **Value Added Tax** that would be due)” immediately after “in respect of **Termination Amounts**”
- In CUSC paragraph 3.23.2, insert a new sub-paragraph (e):
“(e) any applicable **Value Added Tax** that would be due on the amounts referred to in this Paragraph 3.23.2”
- In CUSC Section 15, Part Three, insert new paragraph 3.4:
“3.4 The **Cancellation Charge Secured Amount** shall be calculated using the **Cancellation Charge** inclusive of any applicable **Value Added Tax** that would be due.”
- In CUSC Schedule 2 Exhibit 3, Part 2:
 - In Clause 9A.1.4, insert “(inclusive of any applicable **Value Added Tax** that would be due)” immediately after “The security to be provided shall be in an amount not greater than such sums payable on termination”
 - In Clause 9B.2.1, insert “(inclusive of any applicable **Value Added Tax** that would be due)” immediately after “in respect of **Final Sums** and **The Company Engineering Charges** and other expenses in relation to seeking **Consents** referred to in Clause 2.4 of this **Construction Agreement**”

What is the impact of this change?

Who will it impact?

This modification may have a low impact on all Users.

What are the positive impacts?

This modification confirms the current position on securities, which are in place to ultimately protect consumers.

The Proposer's view is that this modification will have a positive impact on the CUSC applicable objectives A, B and D. This is because the modification clarifies the position on securities, allowing NGENSO to efficiently administer the securities processes and

ensure all Users secure on a consistent basis, protecting other Users, and ultimately consumers.

Impact of the modification on the Code objectives:	
Relevant Objective	Identified impact
(a) The efficient discharge by the Licensee of the obligations imposed on it by the Act and the Transmission Licence;	Positive
(b) Facilitating effective competition in the generation and supply of electricity, and (so far as consistent therewith) facilitating such competition in the sale, distribution and purchase of electricity;	Positive
(c) Compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency *; and	None
(d) Promoting efficiency in the implementation and administration of the CUSC arrangements.	Positive
*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).	

Code Administrator Consultation Summary

The Code Administrator Consultation was issued on the 19 June 2020 and closed on 10 July 2020. One response was received, and a summary can be found in the table below, the full response can be found in Annex 2.

Code Administrator Consultation summary	
Question	
Do you believe that the CMP342 Original Proposal better facilitates the Applicable CUSC Objectives?	No The CUSC and CMP 192 do not provide for the levying of VAT on top of the Cancellation Charge Secured Amounts. Increasing Cancellation Charge Secured Amounts by 20% will have a detrimental effect on consumers costs and have a distortive effect on developer competition.
Do you support the proposed implementation approach?	No This modification should have been progressed via a standard governance route rather than Self-Governance route

	<p>The Criteria for self-governance is not met due to the material effect on existing and future electricity consumers, competition and commercial activities in generation and the impact increased costs has on sustainable development.</p> <p>This change will merely increase the costs to Users of providing financial security on a more cost-reflective basis, undermining the key objectives of CMP192 and, in respect of cash deposits, result in a positive cashflow advantage to NGESO by levying a provisional amount for VAT which may never become due without any resultant benefit such as reduced TNUoS charges.</p>
Do you have any other comments?	No
Legal text issues raised in the Consultation	
No legal text issues raised in the Consultation.	

Panel Determination Vote

The CUSC Panel met on the 28 August 2020 to carry out their determination vote.

The CUSC Panel in May 2020 had unanimously agreed that CMP342 should follow the self-governance route and proceed to Code Administrator Consultation. At July 2020 Panel, the Code Administrator shared that there had been a challenge on material impacts of the proposed change from a respondent to the Code Administrator Consultation. Therefore, the Panel agreed to defer decision on the appropriate governance route to the August 2020 Panel. At the August 2020 Panel, Panel agreed by majority to maintain their decision that CMP342 should follow the self-governance route.

August 2020 Panel then assessed whether a change should be made to the CUSC by assessing the proposed change and any alternatives against the code objectives. The full vote can be found below.

CUSC non-charging objectives

- (a) The efficient discharge by the Licensee of the obligations imposed on it by the Act and the Transmission Licence;
- (b) Facilitating effective competition in the generation and supply of electricity, and (so far as consistent therewith) facilitating such competition in the sale, distribution and purchase of electricity;
- (c) Compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency *; and
- (d) Promoting efficiency in the implementation and administration of the CUSC arrangements.

*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).

CMP342 Vote

Vote 1: Does the Original facilitate the objectives better than the Baseline (the current CUSC arrangements)?

Panel Member: Andy Pace

	Better facilitates ACO (a)?	Better facilitates ACO (b)?	Better facilitates ACO (c)?	Better facilitates ACO (d)?	Overall (Y/N)
Original	Yes	Neutral	Neutral	Yes	Yes
Voting Statement					
<p>This modification clarifies the application of VAT when calculating the amount to be secured by a User. There is no impact to CUSC parties that result from this change other than making the current long-standing process clearer within the CUSC. We therefore consider that this mod better meets standard CUSC objectives (a) and (d). We are voting in favour of this modification as it clarifies existing processes. However, we expect the ESO to continue to engage with stakeholders to ensure any issues with how VAT is applied are addressed.</p>					

Panel Member: Cem Suleyman

	Better facilitates ACO (a)?	Better facilitates ACO (b)?	Better facilitates ACO (c)?	Better facilitates ACO (d)?	Overall (Y/N)
Original	N/A (Abstained)				
Voting Statement					
N/A (Abstained)					

Panel Member: Garth Graham

	Better facilitates ACO (a)?	Better facilitates ACO (b)?	Better facilitates ACO (c)?	Better facilitates ACO (d)?	Overall (Y/N)
Original	Yes	Neutral	Neutral	Yes	Yes
Voting Statement					
<p>Having reviewed the Draft Final Modification Report along with the response to the Code Administrator consultation and taking into account the helpful discussions held at the July and the two August Panel meetings (including with the party who has raised an important matter worthy of due consideration) I have concluded that based on the ESO's statements in the documentation and</p>					

to the Panel that CMP342 does better facilitate, in particular, Applicable Objectives (a) and (d); whilst being, in my view, neutral with respect to (b) and (c); for the reasoning set out in the proposal form.

Panel Member: Grace March

	Better facilitates ACO (a)?	Better facilitates ACO (b)?	Better facilitates ACO (c)?	Better facilitates ACO (d)?	Overall (Y/N)
Original	Yes	Neutral	Neutral	Yes	Yes
Voting Statement					
This Modification clarified existing arrangements in the CUSC, ensuring all Users are treated on a consistent basis and can understand the process fully.					

Panel Member: Jon Wisdom

	Better facilitates ACO (a)?	Better facilitates ACO (b)?	Better facilitates ACO (c)?	Better facilitates ACO (d)?	Overall (Y/N)
Original	Yes	Yes	Neutral	Yes	Yes
Voting Statement					
<p>The proposal clarifies and formalises existing practice on the treatment of VAT in respect of User Commitment requirements as per CUSC Section 15.</p> <p>As such it is positive against Applicable CUSC Objectives A, B and D for the following reasons;</p> <p>1) this clarification allows NGENSO and generators to be more confident in the treatment of VAT and so account for this in processes, internal decision making and for this ultimately to be reflected in lower risk associated with new generation connections.</p> <p>2) Any shortfall in the amount recovered at termination (for example, non-payment of termination amounts by a terminating generator) will be recovered from other generators and consumers. By not including VAT in the value secured, this will increase the amount that will need to be recovered from other parties (by 20%). As such this modification promotes effective competition by ensuring costs caused by a party are recovered from that party as per the relevant methodology rather than being socialised.</p> <p>3) The trigger for termination amounts (and so the applicability of VAT) is outside of the control of all parties except the terminating generator. Therefore there is no other efficient mechanism (which avoids the risk identified in point 2) of ensuring VAT is recovered from the appropriate party than recovering the VAT before termination. As the VAT amount due changes through the lifetime of the</p>					

project (in accordance with the User Commitment methodology in CUSC Section 15) it is prudent that the amount of security held (in the event of termination), including the applicable rate of VAT, is also reviewed periodically and increased or decreased as appropriate.

There is no interaction between CMP342 and European Regulation 2009/714/EC and so CMP342 is neutral against Applicable CUSC Objective C.

Panel Member: Joseph Dunn

	Better facilitates ACO (a)?	Better facilitates ACO (b)?	Better facilitates ACO (c)?	Better facilitates ACO (d)?	Overall (Y/N)
Original	Yes	Neutral	Neutral	Yes	Yes
Voting Statement					
My voting aligns with the proposer's justification for ACOs (A), (C) and (D) but I consider the proposal to be neutral to ACO (B) as it does not change how the inclusion of VAT currently operates within the various areas considered and therefore does not change the facilitation of competition.					

Panel Member: Mark Duffield

	Better facilitates ACO (a)?	Better facilitates ACO (b)?	Better facilitates ACO (c)?	Better facilitates ACO (d)?	Overall (Y/N)
Original	Yes	Neutral	Neutral	Yes	Yes
Voting Statement					
By clarifying the CUSC to accurately reflect the legal framework surrounding the payment of VAT with respect to Cancellation Charges this better facilitates the applicable CUSC objectives. The fact that the VAT payable in connection with Cancellation Charges has always been included by NGESO / NGET when calculating securities for such amounts means that the existing practice is being clarified rather than there being a material change. While the VAT does not become payable until such time as a cancellation charge is levied, it is clear to me that the VAT will become automatically due at that time. Therefore in order to provide credit for the total amount due it is appropriate to include VAT when calculating the Cancellation Charge Secured Amount.					

Panel Member: Paul Jones

	Better facilitates ACO (a)?	Better facilitates ACO (b)?	Better facilitates ACO (c)?	Better facilitates ACO (d)?	Overall (Y/N)
Original	Yes	Neutral	Neutral	Yes	Yes
Voting Statement					
Clarification of process with respect to VAT helps improve efficiency of the arrangements.					

Panel Member: Paul Mott

	Better facilitates ACO (a)?	Better facilitates ACO (b)?	Better facilitates ACO (c)?	Better facilitates ACO (d)?	Overall (Y/N)
Original	No	No	Neutral	Neutral	No
Voting Statement					
The question to ask ourselves to help think about this is, if the security is called, who is liable to pay the 20% - ESO, or the party that defaults ? The latter is the answer. In that case we are increasing the security for the benefit of the ESO under the current approach – the ESO doesn't need this protection as it doesn't pay the VAT; we are making parties over-secure; it seems not to be logical. We shouldn't be securitising via ESO for HMRC that they will be paid, as their payment comes from the party, not from ESO.					

Vote 2 – Which option is the best?

Panel Member	BEST Option?
Andy Pace	Original
Cem Suleyman	n/a - Abstained
Garth Graham	Original
Grace March	Original
Jon Wisdom	Original
Joseph Dunn	Original

Mark Duffield	Original
Paul Jones	Original
Paul Mott	Baseline

Panel conclusion

The CUSC Panel, by majority, determined that the Original better facilitated the CUSC Objectives than the Baseline and should be implemented.

When will this change take place?

Implementation date:

9 October 2020 (5 working days after the appeals window closes) providing no appeals are received by 5pm on 2 October 2020.

Implementation approach:

NGESO seeks implementation of the modification as soon as possible, to ensure that there is no ambiguity possible when interpreting the CUSC and it can take prompt action where a User defaults in providing the required security amount, including for any applicable VAT.

It is proposed that the CMP342 is implemented 5 working days after the appeals window closes, providing no objections have been raised.

Acronym table and reference material

Acronym	Meaning
NGESO	National Grid Electricity System Operator
VAT	Value Added Tax

Reference material:

None

Annexes

Annex	Information
Annex 1	CMP342 Self-Governance Statement
Annex 2	CMP342 Code Administrator Consultation Response