

Workgroup Consultation

CMP344

Clarification of Transmission Licensee revenue recovery and the treatment of revenue adjustments in the Charging Methodology

Overview: 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.

Modification process & timetable

1	• Proposal form • 21 May 2020
2	• Workgroup Consultation • 2 November 2020 - 23 November 2020
3	• Workgroup Report • 27 November 2020
4	• Code Administrator Consultation • 30 November 2020 - 21 December 2020
5	• Draft Modification Report • 8 January 2021
6	• Final Modification Report • 12 January 2021
7	• Implementation • 1 April 2021

Have 5 minutes? Read our [Executive summary](#)

Have 20 minutes? Read the full [Workgroup Consultation](#) document

Have 30 minutes? Read the full Workgroup Consultation document and annexes

Status summary: The Workgroup are seeking your views on the work completed to date to form the final solution(s) to the issue raised.

This modification is expected to have a:

High impact on Transmission Owners, Transmission Users including Generation and Suppliers

Medium impact on National Grid ESO

Governance route

This modification will be assessed by a Workgroup and Ofgem will make the decision on whether it should be implemented.

Who can I talk to about the change?

Proposer: Bill Reed, RWE

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Code Administrator Chair:

Joseph Henry

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How do I respond?

Send your response proforma to cusc.team@nationalgrideso.com by **5pm on 23 November 2020**.

Executive Summary

This modification proposes to address the CUSC charging arrangements in two important areas; Recovery of “Maximum Allowed Revenue” (MAR) and Treatment of revenue associated with unforeseen or unforeseeable events.

What is the issue?

The defect in the current CUSC arrangements is as follows:

Recovery of “Maximum Allowed Revenue” (MAR)

- 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)¹

While it is clear that the intent of Section 14 is to recover the MAR of onshore and offshore transmission owners, this is not set out explicitly in the CUSC.

Treatment of revenue associated with unforeseen or unforeseeable events

- Section 14 of the CUSC does not 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, Income Adjusting Events (IAEs).

This modification proposal will set out the treatment of revenue adjustments related to unforeseen or unforeseeable events during a period subject to a price control.

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

Proposers solution:

This modification proposes the following changes to Section 14 'Charging Methodologies' of CUSC:

i) Changes to Section 14.14.2

- to clarify that the MAR is set for each price control period for onshore TOs and at the point of asset transfer for OFTOs.

ii) A new section of the Charging Methodology

iii) Further changes in Section 14

Implementation date:

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

The proposer has also stated that a retrospective application of this modification to April 2021 decision if an Ofgem decision is delayed beyond April 2021, and whether any

associated system changes will be required. This is due to the interactions with the price control.

The ESO note that If a decision is received after the final tariffs for Apr 2021 charging year are set, a retrospective implementation from Apr 2021 would mean tariffs would then no longer comply with the approved methodology (as the new method within CMP344 would mean Offshore & Demand tariffs would be adjusted). Ordinarily this may mean a mid-year tariff change is required, however, this would not be possible (without Ofgem direction) therefore an implementation date of April 2021 can only be achieved if a decision is received prior to the 25 January 2021.

Summary of potential alternative solution(s) and implementation date(s):

No alternative solutions were discussed by the Workgroup.

What is the impact if this change is made?

This modification is designed to clarify the arrangements that enable Transmission Owners both onshore and offshore to recover the costs allowed under the price control and the costs that occur as a result of unforeseen and unforeseeable events. It will impact:

- i) **Onshore TOs:** It will make it clear that onshore TOs are allowed to recover the costs that are set at each price control review and allow the recovery of costs related to unforeseen and unforeseeable events through adjustments to the demand residual. This will improve certainty over cost recovery for onshore TOs;
- ii) **OFTOs:** It will make it clear that OFTOs can recover the costs defined at the time of the asset transfer to the OFTO and allow the recovery of costs related to unforeseen and unforeseeable events through adjustments to the demand residual. This will improve certainty over cost recovery for OFTOs;
- iii) **Onshore network users:** It will ensure that onshore network users are not exposed to costs associated with the recovery of unforeseen or unforeseeable events as a result of changes to locational transmission charges. This will ensure certainty over transmission costs for onshore network users;
- iv) **Offshore Network Users:** It will make it clear that OFTOs can only recover the costs of the network through local charges from the date of the asset transfer and for the life of the OFTO “price control, period”. It will also ensure that offshore network users are not exposed to costs associated with the recovery of unforeseen or unforeseeable events as a result of changes to locational transmission charges. This will ensure certainty over transmission costs for offshore network users
- v) **Demand Users:** It will impact on demand users as adjustments associated with unforeseen and unforeseeable events will no longer be recovered via the User of the assets but through adjustments to the demand residual and end consumers tariffs, in the same way that other costs on the GB transmission system are allocated to demand users.

Overall the proposals will:

- 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 Licensees;
- Reduce the risk for Transmission Licensees and Users, with an overall benefit of reduced cost of capital by ensuring that network companies are able to recover all of the allowed costs of network provision, particularly in relation to income adjusting events for OFTOs through adjustments to the demand residual;
- Facilitate deployment of low carbon generation projects and help to ensure that the Government's commitment of net zero by 2050 is met by ensuring that users of offshore network have greater certainty over the costs of using the system
- This change will address ambiguity in relation to treatment of MAR under price control and OFTO arrangements and enable the efficient recovery of revenue adjustments arising from unforeseen and unforeseeable costs, ensuring effective competition in generation and supply of electricity.

Interactions

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

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 - Proposer's solution
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What is the issue?

The defect in the current CUSC arrangements is as follows:

Recovery of “Maximum Allowed Revenue” (MAR)

- 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)

While it is clear that the intent of Section 14 is to recover the MAR of onshore and offshore transmission owners this is not set out explicitly in the CUSC – this modification will address this defect.

Treatment of revenue associated with unforeseen or unforeseeable events

- Section 14 of the CUSC does not 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, Income Adjusting Events (IAEs).

This modification proposal will set out the treatment of revenue adjustments related to unforeseen or unforeseeable events during a period subject to a price control.

What is the solution?

Proposer’s solution:

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 price control period for onshore TOs and at the point of asset transfer for OFTOs. The MAR is not subject to any further modification for the duration of the Price Control Period for onshore TOs ¹ and after the asset transfer for OFTSs.

ii) A new section of the Charging Methodology

- to ensure that any revenue adjustments associated with unforeseen and unforeseeable events that result in actual costs incurred and costs saved for TOs and OFTOs outside the relevant price controlled periods² are recovered through adjustments to the Demand Residual³.

iii) Further changes in Section 14

- to allow the pass through of the revenue adjustment through the demand residual.

Workgroup Considerations

The Workgroup convened 2 times to discuss the perceived issue, detail the scope of the proposed defect, devise potential solutions and assess the proposal in terms of the Applicable Code Objectives. There was agreement from the Workgroup on the Proposer’s main points and this section of the report reflects this and further discussions.

Consideration of the proposer’s solution

OFTO licence and price control considerations

The Workgroup identified that specific reference to OFTO's in Section 14 is needed to establish when the costs are set. The Workgroup noted clarification was needed if the IAE¹ means that the MAR can't be affected, then how can demand be recovered. The Workgroup held a discussion around what is allowed to be recovered under the OFTO licence. Within the Policy Decision – Income Adjusting Events in Offshore Transmission Owner Licences from 2018, the IAE provisions are set out in paragraphs 14 to 24 of Amended Standard Condition E12-J3 (Restriction of Transmission Revenue: Allowed Pass-through Items) (the IAE Condition) of the OFTO Licence.

Paragraph 15 of the IAE Condition defines what constitutes an IAE, as follows:

An income adjusting event in 'relevant year t' may arise from any of the following:

- 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 allowed transmission owner revenues of the Licensee were 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 [£500,000]/[£1,000,000] (the "threshold amount").⁴

C is further assessed via these factors:

- 1) whether the OFTO knew of the event or circumstance before it arose or ought to have known of it
- 2) whether the risk of damage of that type was reasonably foreseeable (even if the particular way in which the damage has occurred may not have been)
- 3) whether there are nevertheless exceptional factors in the relevant case that mean that the event or circumstance, or its consequences, could not have been reasonably foreseeable, and
- 4) the ability of the OFTO to manage the risk or impact by putting in place and pursuing risk management arrangements such as insurance, commercial recourse against third parties and/or operating practices.

There are sections in the OFTO licence which direct to IAE's and where they are permitted and the IAE's for Onshore are permitted under the TO licences. It was confirmed under 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. Transmission Network Use of System Charges are set to recover the Maximum Allowed

¹ As detailed in The IAE provisions are set out in paragraphs 14 to 24 of Amended Standard Condition E12-J3 (Restriction of Transmission Revenue: Allowed Pass-through Items) (the IAE Condition) of the OFTO Licence

Revenue 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).

ESO's letter dated 27 July 2017

The Proposer's solution looks specifically at amending Section 14 'Charging Methodologies' of the CUSC. 14.14.1 and 14.14.2, as these sections set out the MAR. The CUSC currently doesn't have any arrangements for revenue adjustments and the solution seeks to change the MAR to ensure it is clear for both Onshore and Offshore TO's and what will need to be paid. If the price control settlement allows for revenue adjustment, then the MAR can be recovered by the Onshore TO's.

The MAR set at the time of the price control can be recovered, it is not the intention to defer anything as this should be recovered by the TO's. It was noted by the Workgroup that the IAE means that the MAR is unable to be affected, therefore not able to be recovered through demand. The Workgroup agreed that the ambiguity needs to be removed and the definition of costs clear.

The ESO revenue team attended workgroup meeting 2 to discuss the letter. The workgroup concluded post discussion that whilst the letter was useful when published, the need for the CUSC to be updated is still relevant. As such, the Original Solution was continued and is at the time of writing being developed further.

The Workgroup also considered Ofgem's policy decision on 28 November 2018 (Paragraph 4.6)² that industry needed to address this issue regarding Income Adjusting Events. This had not been undertaken until this proposal was raised and sent to be developed by this workgroup.

Recovery via the Transmission Demand Residual

The proposer used the example of the Sloy³ income adjusting event of 7 July 2009 (and subsequent determination). Whilst this was an IAE, this was recovered through Transmission Demand Residual. The recovery in this instance was not targeted at local users, and as such could be used as an example of a precedent, on which this modification follows.

Offshore local circuit tariffs

The Workgroup agreed with the Proposer's solution, that the methodology for Offshore local circuit tariffs should be brought in line with the methodology for Onshore local circuit tariffs as unforeseeable events are not included in the calculations. The proposer stated that these are costs associated with the total system, and as such should be recovered as part of the demand residual to avoid discriminatory treatment of particular users.

Interactions with current ongoing Transmission Demand Residual modifications

² <https://www.ofgem.gov.uk/publications-and-updates/offshore-transmission-generic-ofto-licence-and-guidance-tr6>

³ <https://www.ofgem.gov.uk/ofgem-publications/52604/tirg-sloy-determination-pdf>

The Workgroup took into consideration the interactions this modification has with current ongoing Transmission Demand Residual modifications. Workgroup members agreed that this does overlap with some of the TDR modifications as this modification would require a new parameter to be introduced into Section 14. If the baseline hadn't changed as a result of the TDR modification decision (which is still being considered by Ofgem at the time of publication), this extra parameter would still need to be added to the TDR.

This modification is consistent with the direction of travel of the TDR modifications which have come about as part of the Targeted Charging Review SCR. Whilst there will be an addition to Transmission Demand Residual recovery as part of this modification, it is neither contingent on nor impactful of the ongoing work in that area.

Draft Legal text

The draft legal text for this change will be developed by the Workgroup following the Workgroup Consultation.

What is the impact of this change?

This modification is designed to clarify the arrangements that enable Transmission Owners both onshore and offshore to recover the costs allowed under the price control and the costs that occur as a result of unforeseen and unforeseeable events. It will impact:

- i) **Onshore TOs:** It will make it clear that onshore TOs are allowed to recover the costs that are set at each price control review and allow the recovery of costs related to unforeseen and unforeseeable events through adjustments to the demand residual. This will improve certainty over cost recovery for onshore TOs;
- ii) **OFTOs:** It will make it clear that OFTOs can recover the costs defined at the time of the asset transfer to the OFTO and allow the recovery of costs related to unforeseen and unforeseeable events through adjustments to the demand residual. This will improve certainty over cost recovery for OFTOs;
- iii) **Onshore network users:** It will ensure that onshore network users are not exposed to costs associated with the recovery of unforeseen or unforeseeable events as a result of changes to locational transmission charges. This will ensure certainty over transmission costs for onshore network users;
- iv) **Offshore Network Users:** It will make it clear that OFTOs can only recover the costs of the network through local charges from the date of the asset transfer and for the life of the OFTO "price control, period". It will also ensure that offshore network users are not exposed to costs associated with the recovery of unforeseen or unforeseeable events as a result of changes to locational transmission charges. This will ensure certainty over transmission costs for offshore network users.
- v) **Demand Users:** It will impact on demand users as adjustments associated with unforeseen and unforeseeable events will no longer be recovered via the

User of the assets but through adjustments to the demand residual and end consumers tariffs, in the same way that other costs on the GB transmission system are allocated to demand users.

Overall the proposal will:

- 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 Licensees;
- Reduce the risk for Transmission Licensees and Users, with an overall benefit of reduced cost of capital by ensuring that network companies are able to recover all of the allowed costs of network provision, particularly in relation to income adjusting events for OFTOs through adjustments to the demand residual;
- Facilitate deployment of low carbon generation projects and help to ensure that the Government's commitment of net zero by 2050 is met by ensuring that users of offshore network have greater certainty over the costs of using the system
- This change will address ambiguity in relation to treatment of MAR under price control and OFTO arrangements and enable the efficient recovery of revenue adjustments arising from unforeseen and unforeseeable costs, ensuring effective competition in generation and supply of electricity.

Proposer's Assessment against Code Objectives

CUSC Charging objectives;

Impact of the modification on the Applicable Objectives:	
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 *; and	None
(e) Promoting efficiency in the implementation and administration of the system charging methodology.	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).	

Applicable 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 offshore 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 adopting an approach consistent with the objectives of the TCR/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)).

Applicable 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.

Applicable 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)).

Standard Workgroup Consultation question: Do you believe that CMP344 Original proposal better facilitates the Applicable Objectives?

When will this change take place?

Implementation date:

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

The proposer has also stated that a retrospective application of this modification to April 2021 decision if an Ofgem decision is delayed beyond April 2021, and whether any

associated system changes will be required. This is due to the interactions with the price control.

Date decision required by:

A decision is required **no later than 25 January 2021** to ensure implementation ahead of April 2021. This will allow the ESO to finalise tariffs ahead on 31 January 2021 tariff publications.

Implementation approach:

If approved by the Authority, this modification will amend CUSC Section 14 'Charging Methodologies'.

Standard Workgroup Consultation question: Do you support the implementation approach?

How to respond

Standard Workgroup Consultation questions:

1. Do you believe that CMP344 Original proposal better facilitates the Applicable Objectives?
2. Do you support the proposed implementation approach?
3. Do you have any other comments?
4. Do you wish to raise a Workgroup Consultation Alternative request for the Workgroup to consider?

The Workgroup is seeking the views of CUSC Users and other interested parties in relation to the issues noted in this document and specifically in response to the questions above.

Please send your response to cusc.team@nationalgrideso.com using the response pro-forma which can be found on the [CMP344 modification page](#).

In accordance with Governance Rules if you wish to raise a Workgroup Consultation Alternative Request please fill in the form which you can find at the above link.

If you wish to submit a confidential response, please note that information provided in response to this consultation will be published on National Grid ESO's website unless the response is clearly marked "Private & Confidential", we will contact you to establish the extent of the confidentiality. A response marked "Private & Confidential" will be disclosed to the Authority in full but, unless agreed otherwise, will not be shared with the CUSC Modifications Panel or the industry and may therefore not influence the debate to the same extent as a non-confidential response. Please note an automatic confidentiality disclaimer generated by your IT System will not in itself, mean that your response is treated as if it had been marked "Private and Confidential".

Acronyms, key terms and reference material

Acronym / key term	Meaning
Baseline	The code/standard as it is currently
CUSC	Connection and Use of System Code
IAE	Income Adjusting Events
OFTO	Offshore Transmission Owner
MAR	Maximum Allowed Revenue
TDR	Transmission Demand Residual
TO	Transmission Owner

Reference material:

1. 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>

2. 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
3. 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>
4. TCMF Slides May 2016, at <https://www.nationalgrideso.com/document/48481/download>
5. SLOY Determination <https://www.ofgem.gov.uk/ofgem-publications/52604/tirg-sloy-determination-pdf>

Annexes

Annex	Information
Annex 1	CMP344 Proposal Form
Annex 2	Terms of Reference