Workgroup Consultation

CMP361 & CMP362: BSUoS Reform: Introduction of an ex ante fixed BSUoS tariff & Consequential Definition Updates

Overview:
CMP361 seeks to introduce an ex ante fixed volumetric BSUoS tariff set over a total fixed and notice period of 15 months. This will deliver the recommendations of the Second BSUoS Task Force.

CMP362 facilitates the implementation of BSUoS Reform by introducing and updating required definitions into CUSC section 11 from CMP308 and CMP361.

Modification process & timetable

1. **Proposal Form** 11 February 2021
2. **Workgroup Consultation** 01 September 2021 – 24 September
3. **Workgroup Report** 18 November 2021
4. **Code Administrator Consultation** 03 December 2021 – 07 January 2022
5. **Draft Modification Report** 20 January 2022
6. **Final Modification Report** 07 February 2022
7. **Implementation** 01 April 2023

Have 5 minutes? Read our Executive summary

Have 20 minutes? Read the full Workgroup Consultation

Have 30 minutes? Read the full Workgroup Consultation 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 Suppliers, Generators, Final Demand and 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:** Jennifer Doherty, National Grid ESO Jennifer.Doherty@nationalgrideso.com Phone: 07771 938569	**Code Administrator Chair**: Jennifer Groome Jennifer.Groome@nationalgrideso.com Phone: 07966 130854
How do I respond?	Send your response proforma to cusc.team@nationalgrideso.com **by 5pm on 24 September 2021.**	

Contents

Executive summary

CMP361 seeks to introduce an ex ante fixed volumetric BSUoS tariff set over a total fixed and notice period of 15 months. This will deliver the recommendations of the Second BSUoS Task Force.
CMP362 introduces and updates required definitions into CUSC section 11 from CMP308 and CMP361.

What is the issue?

CMP361: Section 14 of the CUSC currently refers to the Balancing Service Use of System (BSUoS) tariff being set on a half-hourly basis, changing in each settlement period. This approach does not provide certainty, stability or transparency of BSUoS charges, as identified through the BSUoS Task Force, and therefore the methodology should be updated to enable a fixed tariff.
CMP362: These modifications will require new definitions in CUSC Section 11.

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

Proposer's solution
CMP361: To implement an ex-ante fixed BSUoS tariff with a 3-month notice period, and 12-months fixed period, with a 1 in 100-year probability (P99) of tariffs needing to be re-set within the fixed period (based on historical performance of BSUoS).
CMP362: This modification seeks to ensure alignment of definitions across CUSC Section 14 and CUSC Section 11.

Implementation date: 1 April 2023 - alongside other proposed (but not yet formally approved by the Authority) wider BSUoS Reforms.

Summary of potential alternative solution(s) and implementation date(s):
Elements of alternatives have been discussed (implementation date 1 April 2023):

Variations on notice and fixed periods:

- 9-month notice period and 6-month fixed period
- 12-month notice period and 3-month fixed period[1]

Variations on financing options:

- BSUoS Fund with a more than 1 in 100-year likelihood of needing to re-set tariffs
- No BSUoS Fund

What is the impact if this change is made?

CMP361 will contribute to CMP308's aim of removing competitive distortions between transmission, distribution and interconnected generation but should be considered as a stand-alone modification. The new proposed methodology simplifies BSUoS payers' charging methodology and unlocks process efficiencies for BSUoS payers. It is expected that CMP361 will result in lower consumer bills through reduced Generator and Supplier risk premia. This is achieved by increased certainty over BSUoS charges. Please note that if CMP308 is approved and implemented at the same time as this modification then the impact of CMP361 will solely be on Suppliers. If CMP308 is implemented in isolation, the absolute value in monetary terms of the risk premia will increase by around the same rate as that removed from Generators.

Interactions

These modifications are linked to CMP308. To ensure the interactions are considered it is recommended that the legal text is considered creating a holistic legal text solution.

[1] An alternative form has been submitted for this option, which can be found in Annex 8.

What is the issue?

CMP361: Section 14 of the CUSC currently refers to the Balancing Service Use of System (BSUoS) tariff being set on a half-hourly basis, changing in each settlement period and charged to both generation and demand.

This approach does not provide certainty, stability or transparency of BSUoS charges, as identified through the BSUoS Task Force, and therefore the methodology should be updated to enable a fixed tariff.

The current BSUoS methodology is no longer aligned with other cost recovery charges which are now based on or moving to Final Demand only. CMP308 'Removal of BSUoS charges from Generation' will change who pays BSUoS charges so they are paid for by Final Demand only. The CUSC must therefore also be updated to ensure that any change to the charging base works alongside the CUSC's new fixed BSUoS tariff methodology. Currently, due to the nature of tariffs being set on a settlement period basis, there is no enduring consideration of the ESO's ability to finance BSUoS as the risk to the ESO is low.

To enable a fixed tariff, where the ESO sets the tariff in advance and holds the associated risk, the CUSC must also be updated to ensure that the ESO financial position remains viable. This is by setting out in CUSC:

- how any additional working capital can be provided; and
- a process for exceptional circumstances

CMP362: Ofgem, in their response letter to the Second BSUoS Task Force final report on 10 December 2020, recommended that industry should develop refined solutions in line with the Task Force recommendations through the code modification process.

CMP308 will change who pays BSUoS charges so they are paid for by final demand only. CMP361 will create a fixed BSUoS tariff methodology. These modifications will create new definitions which are currently not reflected in CUSC Section 11 (definitions). This modification seeks to ensure alignment of definitions across CUSC Section 14 and CUSC Section 11.

Why change?

CMP361: BSUoS charges are the means by which the ESO recovers the costs associated with balancing the electricity transmission system. Ofgem have previously considered whether the current methodology for BSUoS charges needed to change in their Targeted Charging Review (TCR) Significant Code Review (SCR). Alongside this SCR, Ofgem had asked the ESO to lead two industry Task Forces.

The First BSUoS Task Force considered whether BSUoS should either send cost reflective signals or be treated as a cost recovery charge. The conclusion was that BSUoS should be a cost recovery charge as it was not considered feasible to positively influence BSUoS payers' behaviour through the charging methodology and lower costs for consumers.

In November 2019 the TCR concluded and Ofgem directed the ESO to raise CMP333 (BSUoS charged on gross demand) to remove the embedded benefit for distribution connected generators. This creates a more level playing field for generation, by charging suppliers on a gross volume basis. Alongside the TCR decision, Ofgem requested that the ESO lead a Second BSUoS Task Force to explore who should pay BSUoS and how it should be recovered.

The Second BSUoS Task Force published their recommendations in September 2020. The Task Force concluded that Final Demand should pay all Balancing Charges subject to there being enough notice given to industry before implementation. This recommendation is being developed through a separate modification CMP308 (Removal of BSUoS Charges from Generation).

In terms of how BSUoS should be recovered, the Task Force concluded that a volumetric fixed BSUoS charge would be likely to deliver an overall consumer benefit, and that the total length of the fixed and notice period should be around 14 to 15 months in length. Ofgem agreed that this work should proceed.

The current BSUoS Charging Methodology in the CUSC requires updating to enable the conclusions of the BSUoS Task Force to be taken forwards via this modification. This CMP will focus on elements of the change to the charging methodology not covered by CMP308. The introduction of a fixed BSUoS tariff decreases the impact of CMP308 on suppliers by giving suppliers more confidence on BSUoS costs during the fixed tariff period.

The ESO in the RIIO2 business plan commits to reviewing the possibility of a fixed BSUoS tariff. This is to reduce variability of BSUoS prices, create certainty for suppliers to support their pricing decisions, and should result in risk premia reductions and cost savings for consumers. These benefits were re-iterated in the Second BSUoS Task Force conclusions.

CMP362: To introduce this CUSC changes to the BSUoS Charging Methodology are required (CUSC Section 14) as well as consequential definition updates to CUSC Section 11.

CMP308 and CMP361 are separate stand-alone modifications but there is Industry expectation that if both are approved, they will be implemented at the same time.

What is the solution?

Proposer's solution

CMP361: To implement an ex-ante fixed BSUoS tariff with a 15-month combined fixed and notice period, the Proposer suggests the following solution:

Timescales and Process

Notice will be provided in December of the tariff which will be fixed for the following financial year (April to March) including known and forecast under/over recovery for preceding years. This provides industry with 3 months' notice of a tariff, and 12 months when it is fixed. This could benefit consumers as Generators and Suppliers will be able to remove risk premia from their wholesale prices and bills to the end consumer.

Setting Fixed Price BSUoS tariff

The total BSUoS pot to be recovered will be made up of all the relevant cost elements that make up BSUoS including financing costs, any over/under recovery adjustment (K factors) and BSUoS Fund requirements to insure against the need to reset tariffs within the fixed period (up to a 1 in 100 years likelihood (referred to in this document as a P99 level)). The ESO will forecast Final Demand volumes over the fixed period. These two inputs will be used to set the relevant fixed BSUoS tariff.

The BSUoS Fund requirement is the difference between the total available working capital for fixed BSUoS (ESO working capital anticipated to be £300m and any existing BSUoS fund), and the funds required to achieve a 1 in 100-year (to be determined based on consultation responses) likelihood of tariffs being reset within the fixed period. This requirement is re-calculated whenever tariffs are re-set, should the requirement reduce, then additional money in the BSUoS fund will be returned via the over-recovery mechanism in future tariffs. The BSUoS fund will be held in a separate ESO ringfenced account, and any interest accrued will be consolidated into the fund.

Applying fixed price BSUoS to charging base

The ESO will calculate each relevant User's BSUoS liability based on the current charging base (or Final Demand as determined by CMP308 if CMP308 is approved by the authority) and the fixed tariff as above. Any changes in the frequency of billing and the associated credit cover and data requirements will be considered through modifications to the CUSC and BSC which may be raised in due course.

ESO Working Capital and Capped Liability

There should be a cap on the ESO's total support via its working capital facility (WCF). This cap ensures that the ESO can finance fixed BSUoS.

Process for exceptional circumstances

Should the outturn of BSUoS result in there not being sufficient working capital to cover Balancing Service spend (i.e. both the ESO WCF and the BSUoS Fund are forecast to be used up), then tariffs would need to be re-set within the fixed period. This is envisaged to be an exceptional circumstance. The current proposal is that this is set as a 1 in 100-year (P99) likelihood of happening (with alternates expected on this level of probability and risk appetite of Industry). The ESO would have the automatic right to re-set tariffs should this be forecast to happen.

Data transparency

It is important for industry to have visibility of upcoming costs, and the potential for tariffs to be reset. Therefore, the ESO will provide:

- quarterly forecasts of the upcoming BSUoS tariff to industry

- monthly updates on the usage of funds available (ESO WCF & BSUoS Fund)
- should 80% of total funds available be used, the ESO will begin providing updates on each working day
- as today, balancing service cost monthly forecasts over a 2-year time horizon

Workgroup Consultation Question: Do you agree with the proposed data transparency approach set out in the Workgroup consultation?

Interaction with CMP308

The changes to the charging base created through CMP308 have to be considered in the fixed tariff application. The solutions, despite being able to be created independently, have to function on a holistic basis. If CMP308 is implemented then the Generator Charging base is removed, effectively ~ doubling the BSUoS charge levied on Suppliers.

CMP362: This modification will update CUSC Section 11 to reflect the required definitions as created through CMP308 and CMP361.

Workgroup considerations

The Workgroup convened 7 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.

The main elements of the solution discussed by the Workgroup are variations in length of the notice and fixed periods for the fixed volumetric BSUoS charge, and how the charge will be financed. These elements are where alternative modifications are expected to be raised and constitute most of this section of the document.

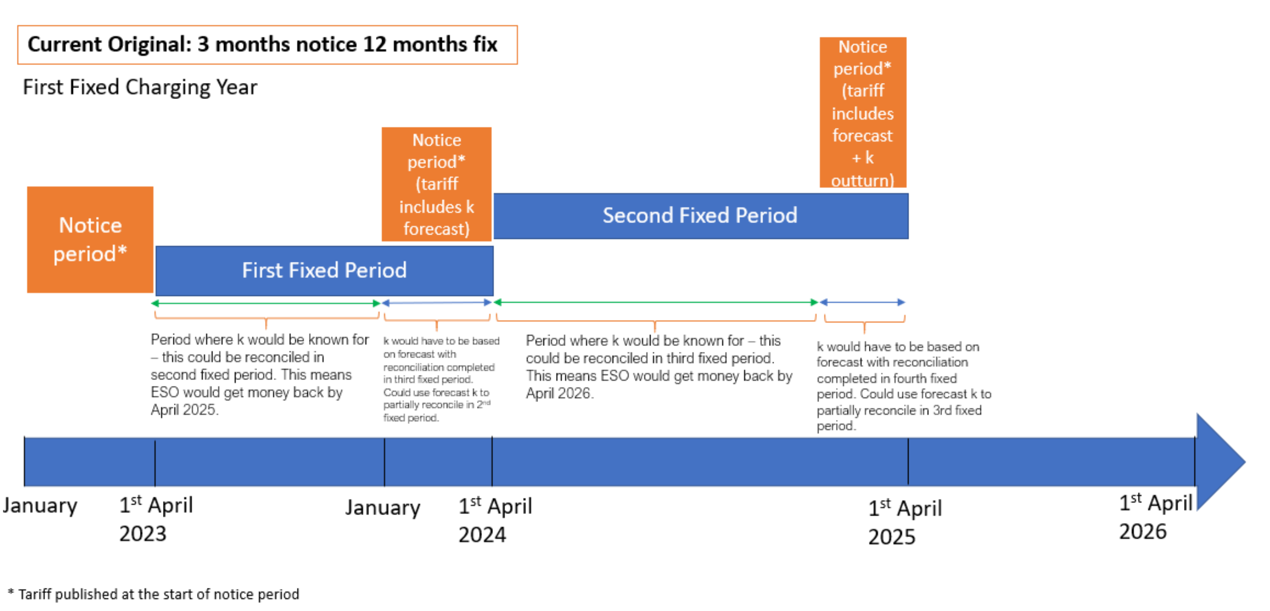
Notice and Fixed periods

The Task Force concluded that the total length of the fixed and notice periods for a volumetric fixed BSUoS charge should be around 14 to 15 months in length. The Workgroup considered the pros and cons of longer and shorter notice and fixed periods which included considerations such as accuracy of forecasts, the effect on over or under recovery, certainty of tariffs and alignment of the tariff with customer contracts. The Workgroup have discussed two alternative options for notice and fixed periods (all are 15 months length in total).

Original Proposal: 3-month notice period and 12-month fixed period

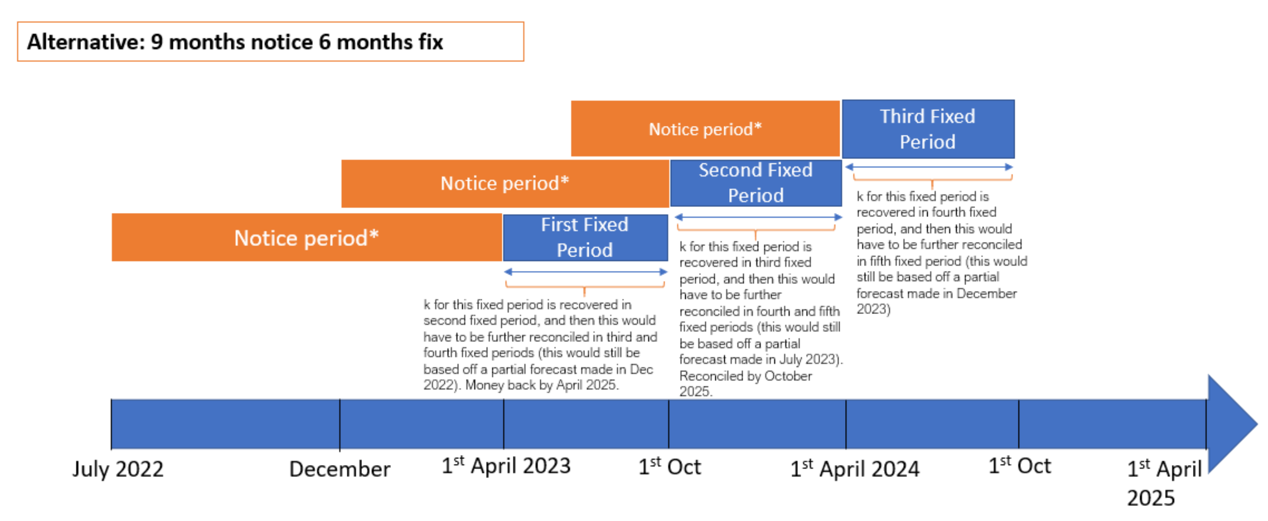
A 3-month notice period and 12-month fixed period allows for accurate forecasts to feed into the BSUoS tariff, due to future costs being clearer 3 months before they are fixed, compared to 12 months. In addition, this option would provide the greatest certainty over tariffs, as it would be fixed for 12 months, which could be simpler for BSUoS payers to understand. As tariffs would be fixed on a 12-month basis, the difference made by over / under recovery would be less spikey than alternatives which fix on shorter timescales. There were significant concerns raised by some work group members, that this does not provide Suppliers with sufficient notice to account for the fixed BSUoS price in their tariffs.

The Workgroup discussed that to ensure a full 3 months' notice, tariffs would need to be published in December. The Proposer agreed to incorporate into their solution that tariffs would be published in December.



9-month notice period and 6-month fixed period

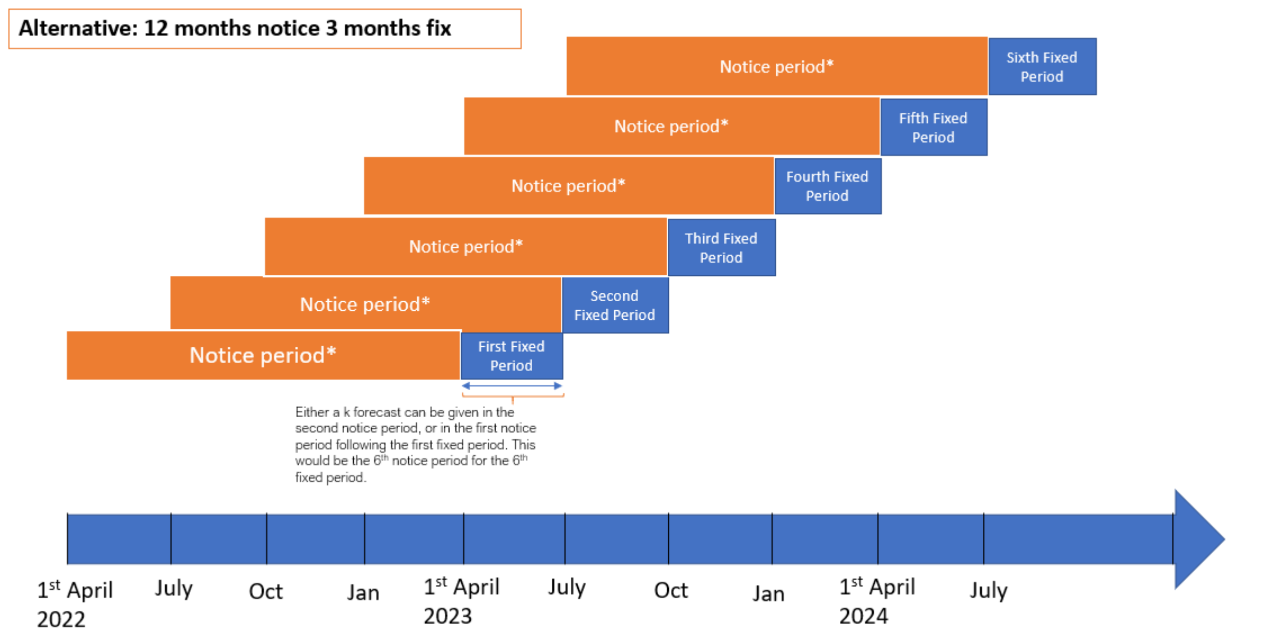
One Workgroup member presented an initial draft of a potential alternative solution, this being a 9-month notice period and 6-month fixed period. The benefits of this approach are that is provides a balance between the two other options.



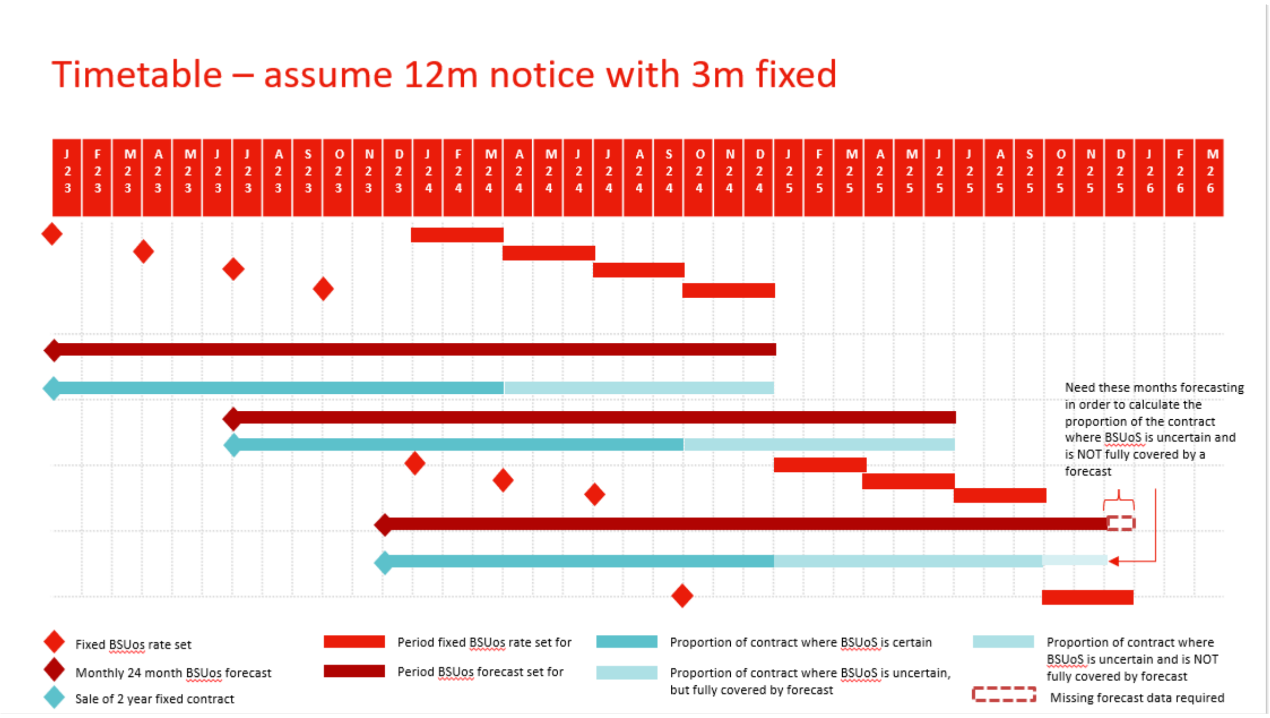
12-month notice period and 3-month fixed period

A Workgroup member shared analysis on their potential alternative proposal, which has a 12-month notice period and 3 months fixed period (an alternative form for this can be found in Annex 8). A longer notice period would allow Suppliers to better account for BSUoS in their tariffs and would provide future notice of tariffs for their business models. With the 3 months' notice and 12 months fixed solution, depending on when a Supplier takes on a new customer, especially for fixed term contracts, Supplier tariffs and Generator wholesale prices may still need to include significant risk premia as a year's fixed contract may include several months where BSUoS tariffs are not fixed. For non-fixed contracts, Suppliers do not want to change their tariffs on a consistent basis. Therefore, Suppliers may choose to accept any losses, or the end consumer may over pay depending on which direction the BSUoS charge goes.

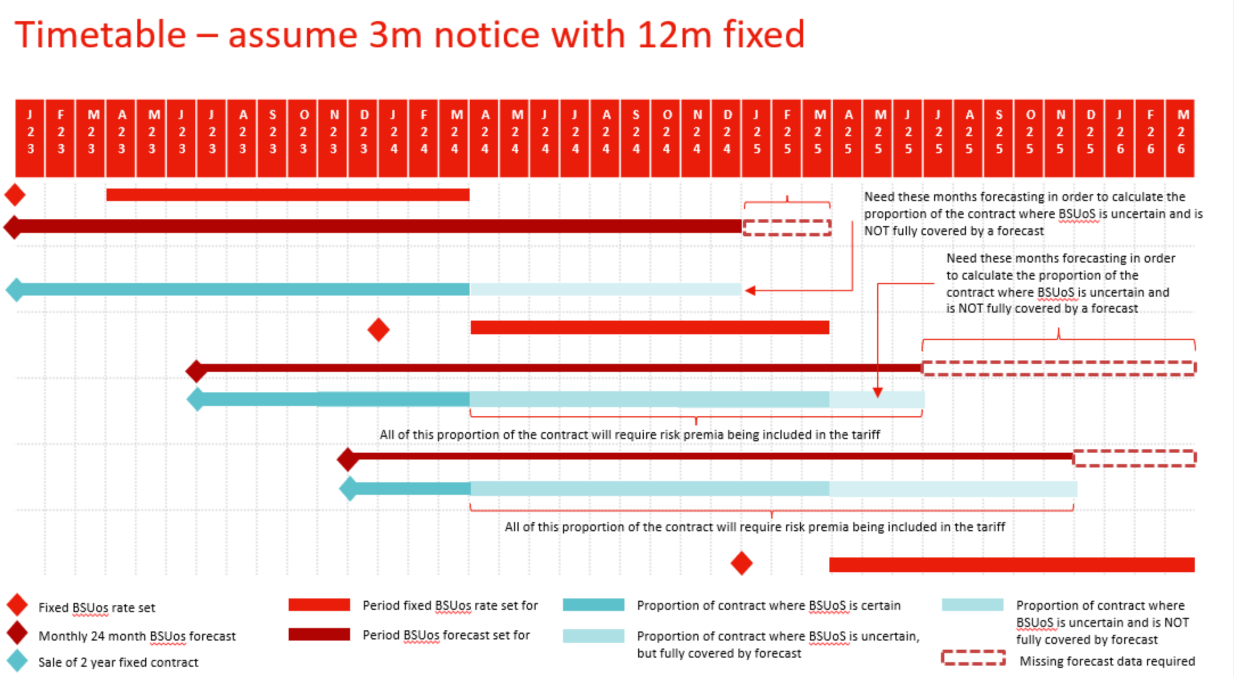
This solution therefore allows for a greater number of fixed priced Settlement Periods irrespective on when a customer was attained within the Financial Year. However, there were concerns raised by some Workgroup members that this will result in tariffs being less accurate, and that it could result in larger swings between each tariff as over / under recovery could be spikier on a quarterly basis each time the tariffs were fixed. It would be possible for Suppliers and Generators to partially remove this spikiness on the end tariff charges to their end consumer, but it would involve accurately forecasting consumption per quarter.



The timeline was considered from a Supplier's perspective. This diagram shows the impact on 2-year fixed contracts.



The diagram above shows how a supplier selling a 2 year fixed contract (very common for business customers) will be less exposed to uncertainty in BSUoS charge under a 12-month notice period and a 3-month fixed period and can therefore remove risk premiums that would be necessary under a 3-month notice period, 12-month fixed methodology. Under the proposed option (3-month notice, 12-month fixed), suppliers that sell a contract one month before the start of the notice period will have to price that contract based on 4 months of known BSUoS, 12 months of unknown BSUoS but which are totally covered by a ESO forecast and 8 months of unknown BSUoS which are only partially covered by an ESO BSUoS forecast. Alternatively, using a 12-month notice, 3-month fixed method means that suppliers can price the same contract with the certainty of 13 months of fixed BSUoS known, 9 months of BSUoS not fixed but covered by an ESO forecast and only 2 months of BSUoS not fixed, but only partially covered by an ESO forecast. This shows that there is more risk inherent for customers in the 3-month notice, 12-month fixed option as compared to the 12-month notice, 3-month fixed method. However, forecasting out 12 months compared to 3 months is more complex and does introduce more uncertainty for the ESO (see below).



Variability in BSUoS forecasts at different time horizons

Further analysis conducted by the ESO shows the variability of a BSUoS forecast as a function of forecast lead time. In an indicative case study using known information, the total variability in a forecast for a 12-month period is estimated to increase by around 50% when comparing forecasts made 3 months and 12 months ahead. In short, this is due to the potential increased variability of potential network changes and wholesale costs in a 12-month window compared to a 3-month window.

Additional background on this analysis can be found in the document 'ESO Response to Frontier Economics Draft Analysis', in annex 5.

Table 1

Quarterly cost variability (£m)						
Leadtime	Snapshot variability	ESO Policy	External Policy	Network changes	Wholesale costs	Total variability
3 months	125	0	0	0	1.13	141
1 year	125	5	0	35	1.31	216
2 years	125	27.5	27	70	1.41	352
3 years	125	43.75	54	105	1.52	498

Frontier Economics Analysis

In December 2020, Ofgem's open letter in response to the Task Force's proposals to reform BSUoS charges included a commitment to carry out quantitative work to assess the overall impacts of these reforms. Quantitative analysis of different solutions using alternative combinations of fixed charges and notice periods is set out in the report by

Frontier Economics and LCP, which can be found in Annex 4. It will form part of Ofgem's overall Impact Assessment of the proposed reform.

Frontier Economics presented an overview of their analytical methodology to the Workgroup. This included an explanation of the methodology adopted, a description of the options they have assessed, the key limitations of their analysis and their preliminary results and findings.

A number of questions were asked by Workgroup members regarding the limitations of the draft analysis undertaken by Frontier Economics. The Proposer shared a note with the Workgroup (included in Annex 5) which sets out their concerns with three main assumptions used in the draft analysis. These were:

- Assumptions around BSUoS cost variability (Frontier's values for ESO exposure),
- The ESO is capable to raise a working capital facility (WCF) which can cover a BSUoS cost variability scenario that would lead to restating tariffs; and
- Forecasting accuracy is constant at all time horizons.

In their final report (Annex 4), Frontier Economics made the following conclusions:

"Overall it seems likely that there is a good case for the implementation of some form of fixed BSUoS charge announced with a notice period.

- The system modelling does not suggest that there are significant system or consumer costs of doing so;
- It would substantially mitigate distributional concerns that may arise from the implementation of CMP308 in isolation; and
- There are clear and material benefits from a transfer of forecasting risk.

However, the quantitative evidence alone does not suggest that there is a strong frontrunner among the options analysed in this report. Indeed, it suggests that the differences in benefits among the options may be relatively small."

Historic Fixed BSUoS case study

The ESO presented a case study to the Workgroup, this was to demonstrate the impact of forecast error and K for future periods. It was assumed that fixed BSUoS was in place for the years 19/20 and 20/21. The table below compares the total K value (under recovery in this instance) for the financial year for the three different notice and fixed time combinations as detailed above.

Table 2

Financial Year	Total K - 3N12F	Total K - 9N6F	Total K - 12N3F
19/20	£222,302,654.12	£255,930,884.79	£280,444,986.63
20/21	£395,820,125.67	£421,163,176.39	£414,346,073.10

Table two compares the mean K value (under recovery in this instance) per month for the three different notice and fixed time combinations.

Table 3

	3N12F		9N6F		12N3F	
Financial Year	Mean K per month (£/MWh)	Mean K/mean outturn	Mean K per month (£/MWh)	Mean K/mean outturn	Mean K per month (£/MWh)	Mean K/mean outturn
19/20	-0.87	25%	-0.99	29%	-1.08	31%
20/21	-1.71	35%	-1.80	37%	-1.76	36%

Workgroup Consultation Question: The Original solution has 3 months' notice and 12 months fixed, what would your preferred combination of notice period and fixed period be? Please provide your justification.

Financeability options

To enable a fixed tariff, where the ESO sets the tariff in advance and holds the associated risk, the CUSC must also be updated to ensure that the ESO financial position remains viable. This is by setting out in CUSC:

- how any additional working capital can be provided; and
- a process for exceptional circumstances

BSUoS Fund

The Original proposal is to place a cap on the ESO's total support via its working capital facility (WCF) and form an industry funded BSUoS Fund to ensure an agreed probability of tariffs being reset is covered. This would be collected as part of the BSUoS tariff. The Proposer explained that the BSUoS Fund is a pot of money funded by industry which will be ringfenced for BSUoS funding purposes and can be returned. Essentially the BSUoS tariff will be purposely designed to over recover for the first two years and this revenue will remain in a pot instead of being returned back to Industry via the reconciliation process currently and a specific K factor introduced by this modification.

The BSUoS fund would provide more certainty to industry about the likelihood of tariffs being re-set within the fixed period, and therefore reduce / remove associated risk premia. The likelihood of tariffs being re-set are covered in a following section below.

A Workgroup member suggested that this method adds more risk as Suppliers are likely to need to build the cost of the BSUoS Fund into their prices or fund it themselves if they have Fixed price contracts already underway before this modification is approved, which could be less effective than amending the prices if there wasn't a BSUoS Fund. It was suggested by a Workgroup member that an option without a BSUoS Fund should be considered. The ESO representative questioned if there was no cap on the ESO's total and under recovery then the ESO would be at risk of a license breach if all the working capital had been spent to fix the cost of BSUoS, the ESO would also need to ensure they had enough funding. This will increase the likelihood of a mid-year tariff change to ensure the ESO had enough funding. A Workgroup member noted that other companies would have parent companies to provide the funding and questioned if National Grid in its entirety be able to support the ESO. The Workgroup noted a recent publication on the Future of the System Operator[2].

[2] https://www.gov.uk/government/consultations/proposals-for-a-future-system-operator-role

Workgroup Consultation Question: Do you support the use of an industry-funded BSUoS Fund to reduce the probability of re-setting tariffs?

Exceptional circumstances

Should the outturn of BSUoS result in there not being a sufficient working capital facility to cover Balancing Service spend (i.e. both ESO WCF and the BSUoS Fund are forecast to be used up), then tariffs would need to be re-set within the fixed period. This would be in an exceptional circumstance. The Original proposal is that this is set as a 1 in 100-year (P99) likelihood of happening (with alternates expected on this level of probability). The ESO would have the automatic right to re-set tariffs should this be forecast to happen.

Should tariffs need to be re-set within the fixed period, the tariff would be made up of forecast costs and demand for the remainder of the fixed period. The Workgroup discussed how it would not be appropriate in this tariff to re-build the total BSUoS fund and recover all of the ESO's WCF as this would be a significant spike in costs within the period. It was however noted that there would need to be an element of buffer in place added to the costs, to ensure that the tariffs didn't need to be re-set again shortly after. This could be achieved by setting tariffs using a far higher P rate. The total under-recovery would then be accounted for in the next notice period.

Alternative approaches discussed

The workgroup discussed alternate approaches to those set out above, this included using a Low Carbon Contracts Company (LCCC) approach to collecting a fund, where collection was separate to the tariff. This option was not taken forward due to additional complexity for parties, and concerns over ability for Suppliers to recover this money as this would not be included in any price cap.

An option was also noted where in an exceptional circumstance, payments to balancing service providers could be temporarily paused. This was not taken forward, due to the potential impacts on system security and complexity in contractual arrangements.

More information on these can be found in annex 3.

The Original proposal initially set out that the ESO would set two prices to reflect changes in £/MWh levels (Summer vs. Winter) allowing within year cashflow positions to be managed. However after consideration, the Proposer amended their Original solution to be that only one price is set for the charging year because they considered that two tariffs within a year may add additional complexity and uncertainty for industry, whilst not providing any significant benefits from a cash flow perspective.

Likelihood of tariffs being reset

The Original proposal is set as a 1 in 100-year (P99) likelihood of needing to re-set tariffs within the fixed period. Other P levels were considered by the Workgroup. It was discussed that the most appropriate P level to set this at depends on the industry's appetite for risk.

The ESO provided the Workgroup with a broader range of variability analysis. This shows what different P levels generally equate to from both a financial perspective, and then the likelihood of tariffs being reset in years. The table below shows estimated variability of BSUoS costs in FY2023/24 for a new BSUoS forecast model.

It was advised that the ESO can currently provide £300m working capital fund now therefore anything above £300m would be the BSUoS fund requirement, however this may change in the future depending on the circumstances of the ESO. The Workgroup noted a recent publication on the Future of the System Operator[3].

The annual variability provided in Table 4 is estimated by combining quarterly forecasts, while considering the difference in variability between those quarters. This means the annual variability is not simply the quarterly variability multiplied by four. For the purposes of this analysis the forecasts for each quarter are considered to have been done at the same time, rather than with a 3-month lag between each one. As 3 months doesn't give much extra information for a forecast, this simplification should have a minimal effect on the variability in the forecast.

This means that the quarterly and annual figures can be used in a comparable manner when assessing the risk of tariff resetting.

Table 4

Percentile	Quarterly (£m)	Annual (£m)	Odds in years
p50	43	163	1 in 2
p55	55	186	
p60	66	210	
p65	78	234	~ 1 in 3
p70	91	259	
p71	94	265	
p72	97	270	
p73	99	276	
p74	102	282	
p75	105	287	1 in 4
p76	108	293	
p77	111	300	
p78	115	307	
p79	118	313	
p80	122	321	1 in 5

[3] https://www.gov.uk/government/consultations/proposals-for-a-future-system-operator-role

p85	137	352	
p90	165	408	1 in 10
p95	203	483	1 in 20
p99	264	574	1 in 100

If the maximum ESO fund equals £300m, without any other funding mechanism the table above indicates that there would be around a 1 in 4 chance of a mid-year tariff change.

The Proposer explained that their assumption is that the higher the P level, the smaller any Supplier risk premia would be due to the decreased risk of a mid-year tariff change, and therefore there are greater consumer benefits in the longer term. It is understood that greater certainty of tariffs is important to both Suppliers and demand users. The Proposer shared their concern that levels less than P90 (less than 1 in 10 years for tariffs being reset) would not provide the intended certainty of fixed BSUoS.

The Proposer also noted, that if the BSUoS fund was "full" in year 2, then future tariffs would be reduced and set at the forecast of BSUoS costs, hence the long-term benefits, particularly in the P99 approach. Should the BSUoS fund be used, or the requirement change, then this would be accounted for in future tariffs.

A Workgroup member questioned whether tariffs needed to be set at P99 for risk premiums to be removed, as different parties have different risk appetites. They suggested that industry would not want to cover such a low likelihood of tariffs being re-set if it could result in an inefficient use of industry capital, therefore suggesting a low P level would be more appropriate.

Workgroup Consultation Question: What would the appropriate balance be between the level of the BSUoS Fund requirement, and the probability of tariffs being reset within the fixed period due to under recovery? (In the Original solution is this set at P99 – see table on pages 15-16)

BSUoS Fund collection

Following discussion over concerns of the initial spike in tariffs to collect the BSUoS fund, the Proposer amended their solution so that the ESO would build the initial BSUoS Fund over two years.

To reduce the impact of BSUoS Fund collection in the first fixed period, half of the BSUoS Fund requirement will be added to the first fixed tariff. The remaining BSUoS Fund requirement will be collected via the second fixed tariff. The remaining BSUoS Fund requirement in the second tariff may be different than 50% for a number of reasons:

- The overall BSUoS Fund requirement may change if the variability changes from year 1 to year 2 (it could be higher or lower)
- If the overall requirement remains the same, it may still not be 50% in the second period. The requirement may be higher if the fund has been used in the first fixed period. It may be less if the ESO over recovered BSUoS in the first fixed period

This means that in practice, P99 will not be covered in the first fixed period as only part of the fund has been collected, and therefore the likelihood of tariffs being reset in the first period will be higher.

Workgroup Consultation Question: Do you agree with the proposed approach to recover half of the BSUoS Fund in the first financial year and the rest in the second financial year?

Final demand data for forecasting purposes

The Proposer advised that to be able to set the first fixed tariffs accurately, the ESO may need to know what final demand looks like depending on CMP308 being approved. The ESO representative stated that the declarations process has not yet started for parties to say they aren't final demand and discussions are being held to see how the declarations process can work in practice. If the CVA process starts in early 2022 and completed by September 2022, and SVA data is received in October 2022 from DNO's, the ESO could provide more accurate forecasting in December 2022, in comparison to earlier in 2022. There were concerns raised by some work group members about what this means for different fix and notice periods. The Proposer noted that this should not change fix and notice proposals, as if the ESO is required to set tariffs earlier in 2022 this can be done on a forecast.

Data Transparency

The Proposer confirmed that the ESO will be doing monthly two year rolling BSUoS forecasts and forecasts of costs. In response to a question from a Workgroup member the Proposer stated that the publishing monthly draft BSUoS tariffs would not be feasible due to the significant amount of inputs required. If using a 3-month notice period, 12-month fixed period approach, the ESO will provide draft BSUoS tariff forecasts to industry each quarter.

A Workgroup member questioned how the charging dispute process would work. It was also questioned, what would happen if a dispute was successful and there were not sufficient funds to cover it.

The Charging Dispute process would work as laid out in Section 7 of the CUSC, under paragraph 7.3 'Charging Disputes'. The determination made by Ofgem could take into account the availability of funds when stating timescales, the repayment would have to be made in.

The Proposer noted that they believe this is where information provision was key. By providing quarterly forecasts of the BSUoS tariff with an explanation behind how the forecast is produced, industry will have notice to challenge and review BSUoS tariffs in advance of them being set. This parallels the way TNUoS tariffs are handled today.

Licence vs CUSC approach

Ofgem delivered a presentation on their developing thinking on the Licence vs CUSC approach. The full slides can be found in annex 6. The Ofgem representative explained that the license sets out what can be recovered and the CUSC sets out how this is recovered. If a fixed term was introduced, then a K factor would need to be introduced into the license and would need to be consistent with the notice period and duration. The rate of interest and speed of recovery would also need to be set out. The Workgroup noted that any such change to the Licence would need to be factored into the timescales for the modifications.

Implementation date

An implementation date of earlier than 2023 was considered, as it was identified in the Authority's response to the BSUoS Task Force's report that this may benefit consumers. However, it was explained by the proposer that a new billing system will be required to implement the modification, and the ESO will require sufficient notice in order to meet the requirements of the solution. Therefore, no potential alternatives have so far been discussed with an earlier date.

Consumer Price Cap

A Workgroup member provided the Workgroup with their view on the Consumer Price cap, stating that, Suppliers currently operate under a price cap regime for domestic customers. The Default Tariff Cap sets a maximum amount that can be charged for a typical domestic customer on a default tariff i.e. a standard variable tariff or a default fixed term or prepayment tariff. The Supply Licence (Condition 28AD) and supporting annexes set out the methodology for calculating the level of the Default Tariff Cap. The price cap is currently expected to expire on 31 December 2023.

The Workgroup member explained that at the beginning of every February and August, Ofgem publish the level of the cap for the forthcoming charge restriction period, which run from April to September (Summer) and October to March (Winter). The cap provides allowances for wholesale costs and network costs (including BSUoS), as well as for other costs, and is set at a level which reflects Ofgem's view of efficient costs. The BSUoS element of the price cap methodology is currently set on a lagged pass-through basis. Specifically, the BSUoS allowance is derived using a volume weighted average of BSUoS charges in £/MWh in each settlement period across the preceding year ahead of publication of the price cap level. The summer (Apr-Sep) price cap uses BSUoS data from the previous calendar year and the winter price cap (Oct-Mar) uses BSUoS data from 1 July in the previous year to 30 June. This weighted average charge is then uplifted by forecast losses before being multiplied by annual domestic consumption to provide the BSUoS allowance in the price cap.

Setting the BSUoS allowance on a lagged pass through basis can create significant differences between the BSUoS allowance in the cap and BSUoS costs being faced in real time. However, under the current ex-post approach to charging it is necessary since it is not possible to forecast an efficient level of BSUoS costs ahead of time. All other elements of the network charge allowance, e.g. for TNUoS and DUoS, use published ex-ante rates.

A move to a fixed ex-ante charge envisaged under CMP361/2 for BSUoS would create the opportunity to reflect the true BSUoS costs in the price cap allowance by setting the allowance equal to the published ex-ante tariff. This would seem appropriate when considered alongside the proposed move to a demand only charge under CMP308 since under the current lagged methodology the impact of a new and much higher demand only BSUoS charge would not be fully included in the domestic price cap for 18 months post implementation. This would create a risk for suppliers that they would be unable to adequately fund increased BSUoS costs.

If the price cap was changed to incorporate the ex-ante fixed BSUoS charge, then a further consideration would be the approach to any cost true up required for cap periods prior to the move to an ex-ante approach. There may be a need for a transitional approach to include this prior period cost true up.

These price cap issues were also considered by the Second BSUoS Task Force, who recommended that Ofgem include the new fixed BSUoS price in the price cap from the point of implementation, including any necessary adjustment to true up allowances for cap periods before the move to an ex-ante approach.

CMP250 Learnings

It was within the Workgroup's Terms of Reference to consider any points of learning from the CMP250 Workgroup and Ofgem's CMP250 decision. Some Workgroup members who had been involved with CMP250 agreed that the Workgroup has happened a long time ago and there had since been a lot of change, so there was limited discussion around any key learnings.

Draft legal text

The Business Rules for this change can be found in Annex 7.

What is the impact of this change?

Proposer's assessment against Code Objectives

CMP361 – Charging Objectives

Proposer's assessment against CUSC Charging 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** This modification will contribute to CMP308's aim of removing competitive distortions between transmission, distribution and interconnected generation. It will also improve competition between suppliers by removing volatility in their pricing leading to efficiencies in consumer offerings.
(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	**Neutral**

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);	
(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;	**Positive** This CMP applies the TCR principles of reducing harmful distortions, fairness and proportionality. The ESO Forward Plan commits to reviewing fixed BSUoS to address industry concerns about BSUoS unpredictability and resulting risk premia. The Proposer believes that fixing BSUoS could allow more efficient pricing to consumers than those currently available through the removal of risk premia.
(d) Compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency *; and	**Neutral**
(e) Promoting efficiency in the implementation and administration of the system charging methodology.	**Positive** Reforming BSUoS charging to create an ex ante fixed price methodology simplifies BSUoS payers' charging methodology and unlocks process efficiencies for BSUoS payers.
*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).	

CMP362 – Non-Charging Objectives

Proposer's assessment against CUSC Non-Charging 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;	**Neutral**
(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;	**Neutral**
(c) Compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency *; and	**Neutral**
(d) Promoting efficiency in the implementation and administration of the CUSC arrangements.	**Positive**

	This modification improves efficiency by ensuring all required definitions for BSUoS reform are accurate and in CUSC Section 11.
*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).	

Standard Workgroup consultation question: Do you believe that CMP361 Original proposal better facilitates the Applicable Objectives?

Standard Workgroup consultation question: Do you believe that CMP362 Original proposal better facilitates the Applicable Objectives?

When will this change take place?

Implementation date

1 April 2023 - alongside the wider BSUoS Reform implementations. A single implementation date would simplify the implementation process for industry.

The interaction between this modification and CMP308 (Removal of BSUoS Charges from Generators) creates a further driver for joint implementation. The additional BSUoS liability shifted to final demand may be offset to some extent through creating a fixed BSUoS tariff and reducing uncertainty around pricing.

Date decision required by

An Ofgem decision is required by February 2022 to allow effective implementation in ESO systems. This would provide certainty to involved parties which could remove cost from their risk premia. The Workgroup and consultation process will determine if a longer period or later implementation is necessary.

Implementation approach

Relevant IT and process changes will be required prior to the implementation date.

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

Interactions

☐Grid Code	☐BSC	☐STC	☐SQSS
☐European Network Codes	☐EBR Article 18 T&Cs[4]	☐Other modifications	☐Other

[4] If the modification has an impact on Article 18 T&Cs, it will need to follow the process set out in Article 18 of the Electricity Balancing Regulation (EBR – EU Regulation 2017/2195) – the main aspect of this is that the modification will need to be consulted on for 1 month in the Code Administrator Consultation phase. N.B. This will also satisfy the requirements of the NCER process.

This modification is linked to CMP308 as mentioned above. To ensure the interactions are considered it is recommended that the legal text is considered creating a holistic legal text solution. This modification interacts with CMP362 which will update any required new and amended definitions into CUSC Section 11.

Additionally, a further modification is expected to be raised to review BSUoS billing frequency and credit cover requirements that will interact with how a fixed BSUoS charge would be billed.

The Workgroup discussed that there may be an impact on Residual Cashflow Reallocation Cashflow (RCRC) and that a BSC issues group would be required to look into this.

How to respond

CMP361 Standard Workgroup consultation questions

1. Do you believe that CMP361 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?

CMP362 Standard Workgroup consultation questions

5. Do you believe that CMP362 Original proposal better facilitates the Applicable Objectives?
6. Do you support the proposed implementation approach?
7. Do you have any other comments?
8. Do you wish to raise a Workgroup Consultation Alternative request for the Workgroup to consider?

Specific Workgroup consultation questions

9. The Original solution has 3 months' notice and 12 months fixed, what would your preferred combination of notice period and fixed period be? Please provide your justification.
10. Do you support the use of an industry-funded BSUoS Fund to reduce the probability of re-setting tariffs?
11. What would the appropriate balance be between the level of the BSUoS Fund requirement, and the probability of tariffs being reset within the fixed period due to under recovery (in the Original solution is this set at P99 – see table on pages 15-16)?
12. Do you agree with the proposed approach to recover half of the BSUoS Fund in the first financial year and the rest in the second financial year?
13. Do you agree with the proposed data transparency approach set out in the Workgroup consultation?

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 CMP361 & CMP362 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, mark the relevant box on your consultation proforma. Confidential responses will be disclosed to the Authority in full but, unless agreed otherwise, will not be shared with the Panel, Workgroup or the industry and may therefore not influence the debate to the same extent as a non-confidential response.

Acronyms, key terms and reference material

Acronym / key term	Meaning
BSC	Balancing and Settlement Code
BSUoS	Balancing Services Use of System
BSUoS Fund	The Original proposal is to place a cap on the ESO's total support via its working capital facility (WCF) and form an industry funded BSUoS Fund to ensure an agreed probability of tariffs being reset is covered. This would be collected as part of the BSUoS tariff.
CMP	CUSC Modification Proposal
CUSC	Connection and Use of System Code
LCCC	Low Carbon Contracts Company
SCR	Significant Code Review
CVA	Central Volume Allocation
DNO	Distribution Network Operator
DUoS	Distribution Network Use of System
EBR	Electricity Balancing Regulation
ESO	Electricity System Operator
Ex ante	"before the event" (Latin)
LCCC	Low Carbon Contracts Company
RCRC	Residual Cashflow Reallocation Cashflow
RIIO2	Price Control Period
SCR	Significant Code Review
SQSS	Security and Quality of Supply Standards
STC	System Operator Transmission Owner Code
SVA	Supplier Volume Allocation
T&Cs	Terms and Conditions
TCR	Targeted Charging Review
TNUoS	Transmission Network Use of System
WCF	Working Capital Facility

Annexes

Annex	Information
Annex 1	Proposal forms
Annex 2	Terms of reference

Annex 3	Consideration of other finance options
Annex 4	Frontier Economics Report
Annex 5	ESO response to Frontier Economics Analysis
Annex 6	Licence vs CUSC slides
Annex 7	Business Rules
Annex 8	CMP361 – Alternative 1 (12-month notice, 3-month fixed)