

# Amendments to NTC Commercial Compensation Methodology Consultation Cover Note

## Executive Summary

ESO is seeking views from across industry on the amended Commercial Compensation Methodology for Interconnector Capacity Management. The Commercial Compensation Methodology was developed in collaboration with, and was intended to be implemented for, all GB interconnectors in June 2021. The Commercial Compensation Methodology is independent of the capacity calculation process and seeks to ensure the correct commercial arrangements for interconnectors when ESO restricts capacity to ensure secure system operation (system security).

## Context

The consultation focuses on the Commercial Compensation Methodology only. However, as part of the discussions with GB interconnectors over the past year, there have been clarifications on how interconnector capacity is managed, and the regulatory documents that underpin it. The following section outlines the regulatory changes and obligations that are now in place.

The tool for managing interconnector capacity is called Net Transfer Capacity (NTC), which covers Day-Ahead and Intraday timescales for the possible restriction and/or curtailment of nominated, allocated and unallocated capacity. NTC restrictions are used to ensure and maintain secure system operation; it is therefore classed as a non-frequency balancing ancillary service as it is a service used predominantly for managing system security. Licence condition C28<sup>1</sup> dictates that non-frequency balancing ancillary services must be market-based unless covered by a derogation. The NTC process is not market-based as there is no tender process to manage interconnectors' capacities, rather it is an input to subsequent interconnector market processes.

The ESO submitted its original derogation request from the requirements of Standard Licence Condition ("SLC") C28 on the 18<sup>th</sup> June 2021. OFGEM published their decision to grant the ESO a temporary derogation on the 23<sup>rd</sup> August 2021 until the 1<sup>st</sup> May 2023 or the date from which a methodology for capacity calculation, as part of the Trade and Cooperation Agreement (TCA), is established.

On 17<sup>th</sup> February 2023, the ESO submitted a request to OFGEM to extend the extant derogation against standard licence condition C28 to procure balancing services following market-based procedures for the non-frequency balancing ancillary service, NTC. On the 26<sup>th</sup> April 2023 OFGEM granted the ESO an extension to the C28 derogation<sup>2</sup> originally issued on the 23<sup>rd</sup> August 2021. This derogation is in place for a limited time, expiring on the 30<sup>th</sup> September 2023. OFGEM stated in this decision letter that they expect the ESO to provide 'evidence, including views of consulted stakeholders, that the NTC commercial compensation methodology (which may have been modified by that time) is clear and fit for purpose, leaving no significant detriment to any party'. They also stated 'The ESO should urgently revisit the NTC commercial compensation methodology, consult with appropriate parties, and address any shortcomings identified, to be re-agreed with the Authority as necessary'. For this reason, the ESO will re-consult on the Commercial Compensation Methodology in advance of the expiry of the C28 derogation.

## Pre and Post EU-exit regulatory arrangements for NTC

Previously the NTC restriction process was captured under CACM<sup>3</sup>. The capacity calculation methodology under CACM determined the amount of interconnector capacity that could be made available to the market. In

<sup>1</sup> [Decision on the proposed modifications to the RIIO-2 Transmission, Gas Distribution and Electricity System Operator licences | Ofgem](#)

<sup>2</sup> [Decision to Grant National Grid Electricity System Operator extension to Derogation from Standard Licence Condition C28 for Net Transfer Capacity | Ofgem](#)

<sup>3</sup> [Commission Regulation \(EU\) 2015/1222 – Capacity Allocation and Congestion Management](#)

addition, CACM set out a limited number of exceptional circumstances when allocated interconnector capacity can be curtailed, such as CACM Article 23. CACM has been revoked in the Statutory Instruments and is no longer in GB law. The capacity calculation process is now covered by the Trade and Cooperation Agreement (TCA)<sup>4</sup>, from which a Technical Procedure (TP) is being developed. In addition, the TCA sets out the limited number of circumstances in which allocated capacity can be curtailed, such as TCA Article 311(1)(c).

Capacity Calculation and Congestion Management methodologies are being developed under the TCA, and the commercial compensation methodology will be adapted to any resulting processes e.g., as new market coupling arrangements are brought online. This may mean, should compensation rules change through the access rules, the Commercial Compensation Methodology may also need to be updated. However, the principles of the methodology will remain the same e.g., interconnectors will be kept cost neutral. The Commercial Compensation Methodology should therefore be viewed as separate to any Capacity Calculation and Congestion Management methodologies that are developed. Whilst these methodologies are developed, ESO will continue to use the existing capacity calculation processes.

It is ESO's intention to manage interconnector capacity in line with the TCA obligations of maximising capacity subject to the ensuring secure system operation (system security).

## Implementation of the current Commercial Compensation Methodology

NTC arrangements are applied based on the specific market mechanism used by each interconnector;

- 1) Explicit DA and ID, e.g., Channel Interconnectors (Table 1 within the Commercial Compensation Methodology), and;
- 2) Implicit DA and/or ID e.g., Irish Interconnectors (Table 2 within the Commercial Compensation Methodology) and NSL (Table 3 within the Commercial Compensation Methodology).

The current Commercial Compensation Methodology arrangements are implemented via the individual interconnector Operating Protocols (OPs) and settlement agreements. These arrangements are in use having been approved via the C16 process, under the current derogation under License Condition C28 and following incorporation into the interconnector OPs and settlement agreements.

## Overview of changes proposed to the Commercial Compensation Methodology

This consultation focuses on amendments to the current Commercial Compensation Methodology. The changes that the ESO have proposed fall under the following categories:

- General clarity of wording – no material changes to the content but better readability.
- Adding clarity to the principles of use of NTC.
- Pragmatic removal of correction factor to implicit spread calculation, this is not immaterial but gives better use of resources.
- Alignment of working settlement formula for OMW auctions (e.g., averaged on monthly, directional data).
- Reference that the methodology applies in full, so ESO can ensure consistent approach to the use of NTCs across all signatories.

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<sup>4</sup> [Trade and Co-operation Agreement](#)