ESO

# 2024/25 BSUoS Fixed Tariffs Webinar

## Q&A Summary – 07/07/23

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| **Purpose** | To summarise the questions asked as part of the 2024/25 BSUoS Fixed Tariffs webinar and the answers provided by the presenters. |
| **Date:** | 07/07/2023 |

You can download the slide deck from this webinar **HERE**

You can view a recording of this webinar **HERE**

## Introduction

A webinar was held on 7th of July 2023 to outline the ESO's view of the 2024/25 BSUoS Final Fixed Tariff 3 and Draft Fixed Tariff 4.

The following questions were asked, and answers provided during the webinar Q&A session:

| # | Questions | Answers |
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| 1 | You have estimated c £429m over recovery from Tariff period 1 (Apr-23 to Sep-23) when setting the tariff period 3 (Apr-24 to Sep-24). How confident are you with this estimated over recovery? What would happen if the actual over recovery was considerably less than estimated £429m? Thanks | BSUoS costs, and especially balancing costs are very volatile so there is still significant uncertainty. The over-recovery of Tariff 1 passed into Tariff 3 is based on the latest available outturn data and the monthly BSUoS forecast published in Jun-23. For the first three months of Tariff 1 we have some outturn data, although this is from a range of settlement runs and data sources. For July to September the forecast was used. For the balancing cost element in these months:<br><br>- the P10 is ~140m below the central forecast (which would give over-recovery of ~570m).<br><br>- the P90 is ~140m above the central forecast (which would give over-recovery of ~290m).<br><br>This does not consider uncertainty in the other forecast elements or in the outturn data, but hopefully gives an idea of our confidence based on balancing cost volatility.<br><br>However, despite this uncertainty Tariff 3 is now a fixed tariff and so wouldn't be affected by changes in the Tariff 1 over-recovery, any adjustments would be passed on to future tariffs that have not yet been set. |
| 2 | How did you get to £25m as needed for this winter? What will | Best guess estimate in all honesty looking at what we paid out for DFS last year and what we could potentially use for winter 2024/25. |

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| | it be spent on? Why do you return the £150m over two periods? | We split it over tariffs 1 and 2 so have reflected the adjustment in tariffs 3 and 4. |
| 3 | Typo in the first bullet on over-recovery slide? | Yes, apologies.<br><br>First bullet point of Slide 10 should read :<br>"Forecast over-recovery positions from Fixed Tariff 1 and Fixed Tariff 2 are reflected in the corresponding tariffs for Fixed Tariff 3 and Fixed Tariff 4".<br><br>This has been corrected in the published presentation. |
| 4 | Balancing costs for period 3 are about £127m lower that the costs used to set the period 1 rate, which you expect to over-recover by ~£430m. Can you explain the drivers of your forecast of balancing costs for period 3 given the expected over-recovery in period 1? | The main two drivers of balancing costs are wholesale electricity prices and renewable generation as a proportion of demand (referred to as renewable %). For Tariff 1 (T1), the latest view of prices and renewable % is significantly below that used to set the tariff. For Tariff 3 (T3) the price element is based on the futures markets, which have significantly dropped since T1 was forecast, but are not as low for the T3 period as the latest best view of the T1 period. Therefore, based on just this driver we would expect the costs for T3 to be below the forecast for T1 but not as low as the projected outturn for T1.<br><br>The renewable % is calculated based on a long history of weather (not just the previous year), combined with our view of installed capacity which is projected to increase into the future. Therefore the % in T3 is slightly higher than T1, even though the latest best view of renewable % in T1 is much lower than forecast. Based on this driver we would expect the costs to be similar or slightly higher for T3 than T1.<br><br>Of course, we do use historic data in many ways in the model, in particular to set the relationships between balancing costs and its drivers, but these relationships did not necessarily change significantly due to the over-recovery. Across these two drivers it is therefore logical to see a small decrease in the forecast costs between T3 and T1, but not to the levels T1 is expected to outturn at. |
| 5 | Can the actual rate also be included in the Daily Costs report please? | Would be interested to hear why this would be beneficial as the cost report is somewhat detached from actual recovery where the fixed tariff is relevant. Concerned that if we added a notional tariff to the daily cost report then we may confuse some people as the tariff is now fixed. |
| 6 | Could you explain what the different lines on the charts on the Revenue vs Cost Report mean? What's the difference between Tariff Setting Revenue and Tariff Setting Costs? | "Tariff Setting Revenue" shows the Fixed Tariff x volume forecast, as of tariff setting (Jan '23). i.e. the amount of revenue forecast when the tariffs were set.<br><br>"Tariff Setting Costs" are the forecast monthly costs as of tariff setting (Jan '23)<br><br>The difference between "Tariff Setting Revenue" and "Tariff Setting Cost" shows our forecast cash position as of tariff setting. There will be some over/under-recovery throughout the period due to a fixed price being used against a variable cost.<br><br>"Latest Revenue" shows the Fixed Tariff x latest volume forecast |

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| | | Comparing "Tariff Setting Revenue" and "Latest Revenue" will show the impact of the latest volume forecast on revenue.<br><br>"Latest Costs" shows the latest of outturn data (Control room, II or SF) or our monthly forecast data.<br><br>The difference between our "Latest Revenue" and "Latest Costs" shows our current forecast over/under-recovery position.<br><br>"Maximum Available Headroom" shows the current £300m working capital fund available to meet any short-term under-recovery. |
| 7 | Are there any very early pointers to what all of this might imply for tariff levels in 2025/26 pls – for example, taking account of last year's over-recovery? Of course, appreciate if your view is that it's just too soon to say given the number of variables and the forecasting challenges - and useful even to know if that's your viewpoint. Many thanks | The monthly operational forecast we will be publishing this month goes out to Jun-25, and so will contain the first half of tariff 5. The same model and process is used for the monthly operational forecasts as for tariff setting for the balancing cost element. Our latest forecast for Apr-Jun 2025 is lower than for Apr-Jun 2024 because the wholesale prices are currently lower but there is huge uncertainty out this far. The wholesale price is set by traders in the market - there will not be much trading activity at longer time horizons and so there is limited market intelligence.<br><br>(See the answer to question 4 on why an over-recovery for a previous tariff may not translate to an equivalent drop in future tariffs) |
| 8 | Thanks all, What date forward curve has been used to model the balancing costs for fixed tariff 3? | Balancing costs are based on an average of forward price curve derived between 1st and 7th June 2023. A monthly forecast is interpolated using the raw price data. |
| 9 | Ofgem is currently consulting on recovering most of the one-off costs for FSO implementation via the ESO's price control arrangements (ie BSUoS). The costs are significant - in excess of £300. Is there any reason why a provision has not been made from these costs in your rate? | It's at consultation stage, we did have an internal discussion about whether to include this but ultimately decided it would be presumptuous to do so but we have called it out as an uncertainty so that people can see the impact on the numbers if they want to include it in their own forecasts. By the time we publish tariff 4 (Oct 2024 – Mar 2025) as final, in December 2023, then these numbers should be firm and included in the tariff. |
| 10 | Does there need to be a code change to address the issue of the return of over-recovery "loose" methodology? | Open governance allows for anyone to raise a mod so that's always an option that is open, personally I believe the current methodology allows us to strike a good balance based on the information we have available at the point when tariffs are set. A stricter methodology may provide more certainty but also restrict us in certain circumstances. |

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| 11 | I appreciate the winter costs were to be recovered over 2 periods but, now that it is known the costs are not needed, what prevents you from returning £150m in period 3? | Nothing specifically prevents it; we have taken this approach to help balance risk and to reflect the costs that were originally included in tariffs 1 and 2 |
| 12 | Including the rate in the Daily Costs report would be helpful as it's an early indicator of the actual rate for that day is (instead of waiting for the II/SF data). We use that info for various reasons internally | Thank you for the feedback, we will investigate this but as previously mentioned there is a concern that publishing a notional tariff for each day confuses some people as the tariff is now fixed and daily costs are somewhat detached from this in the short term. |
| 13 | It might be worth revisiting the decision re FSO transition costs. Excluding the costs may motivate parties to include a risk premium for what is a known cost item, which may defeat the point of having a fixed tariff in the first place | Thank you for the feedback, we will take this view into consideration for future tariffs. |