

CMP308

Removal of BSUoS charges from Generation

26th October 2018



Summary

- We are concerned about the **current market arrangements not ensuring fair competition** between GB and other interconnected countries so have been considering options for reform.
- We are considering **raising a CUSC mod to only levy BSUoS on demand**, i.e. reconsider CMP201 in the light of new evidence and changed circumstances, as other interconnected countries in general levy similar costs solely on demand.
- This is **critical in the context of GB interconnection growth** which is set to significantly increase (4GW today, 8GW by 2020 - and, with Ofgem's approved pipeline, up to 18GW by early 2020s).
- **Ofgem broadly supported CMP201** but considered the short-term consumer negative impact outweighed the longer term benefits:

"We consider that in principle, removing BSUoS from generators would have a small positive impact on competition. However, we are concerned that at this time the potential benefits this would bring would not be material enough to offset the potential costs to consumers from implementing the modification" - Ofgem decision Oct14

- **NGET's calculations**, on which Ofgem's decision was based, were that CMP201 would be detrimental to consumers - but **did not take into account the impact of CMP202** (Revised treatment of BSUoS charges for lead parties of Interconnector BM Units), so:
 - CMP201 modelling (for status quo) assumed BSUoS was split 50:50 between demand and generation.
 - As a result of CMP202 the G:D split for BSUoS charging in 2017 was around 49:51 and expected to be 47:53 by 2020.
 - This reduces the cost increase for suppliers to a value that is roughly equal to the reduction in GB wholesale prices.
- Our **modelling indicates that this change will leave GB consumers neutral** in the short term **with the potential for longer term consumer benefits from competition**.



Defect in current arrangements

- In our European trading partners and other interconnected countries the **equivalent charges for balancing activities are more commonly paid entirely by suppliers**.
 - As a result, the wholesale prices offered by generators in interconnected countries will not reflect these costs in the same way as those offered by a GB generator. (Our estimate is that GB generation is disadvantaged by the extra cost **~£600m in 2017**)
- Our proposal seeks to remove BSUoS charges from GB Generators, thereafter recovering all BSUoS from GB Suppliers. In doing so, it seeks to better facilitate **efficient competition between GB generation and generation in other interconnected markets**.
 - Better aligning the GB market arrangements and the charges faced by GB generation with those prevalent in other interconnected countries, where generation is typically not subject to such charges, allows GB and continental generation to **compete on a more equitable basis and removes the potential for BSUoS to distort cross border trade**.
 - **Supports the UK Industrial Strategy** for building a nation fit for the future with investment in skills, industries and infrastructure.
- The EU “Third Package” aims to deliver all consumers greater choice with more cross-border trade so as to achieve efficiency gains, competitive prices and security of supply.
 - It recognises that different market structures will exist, however it also acknowledges the need for fair competition across the European Community so as to provide producers with the **appropriate incentives for investing in new generation**.
Changing the GB arrangements as proposed thus facilitates the aims outlined in EU Directive 2009/72/EC concerning rules for the internal market in electricity.



Consumer benefits of change

- The proposed CUSC mod **better facilitates code objectives** (a) effective competition, (c) developments in transmission business and (d) EU compliance. It is neutral on (b) cost reflectivity.
- Consumer cost impact
 - demand BSUoS will be less than double of current BSUoS £/MWh rates as interconnector flows to GB do not pay BSUoS (i.e. split of BSUoS between demand and generation is not currently 50:50), i.e. **consumers neutral short term**.
 - sufficient **lead time of 2 years** after a decision is made to ensure
 - wholesale market adjusts to the removal of BSUoS from generation.
 - time for consumers and suppliers to adjust for change.
 - **benefit of avoiding** the need to factor **BSUoS risk** into generation/wholesale market costs, instead being covered within more predictable demand volumes.
- In the **long run** removal of a distortion in the wholesale market will ensure more effective competition which is in **consumers' interests**: i.e. will ensure investment in new generation is more efficient.



How does this BSUoS change fit with other reforms?

1. Ofgem's RAFLC:

- Proposes National Grid review of BSUoS costs to confirm whether they are 'cost recovery' or contain pricing signals
- Grid to lead review outside of SCR
- Timescales tbc

2. Ofgem's TCR:

- Considers addressing current BSUoS embedded benefit
- Impacts distribution connected generators
- Ofgem policy decision late 2018; industry mod to follow Apr 2020+

3. EDF Energy's BSUoS mod:

- Proposes to recover BSUoS costs from demand; reducing production costs to zero
- Industry code process
- 6 months process with 2 year implementation period, i.e. April 2021

Affects size of BSUoS by potentially changing scope (e.g. could determine some elements are price signals)

Affects how BSUoS is charged (e.g. could change to gross volumetric impacting embedded benefits)

Affect who pays BSUoS (i.e. change demand recovery to 100%)

CMP250 fixes BSUoS charges for long period to provide certainty to users. This change is independent of the 3 above but appears more sensible if demand pays 100% of BSUoS.

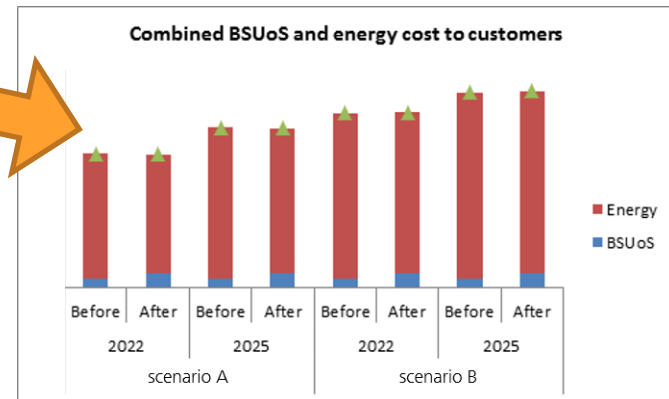
CMP281 proposes to exempt import or export BSUoS costs from storage assets; designed to align storage assets with generation

- **These are 3 separate policy considerations which can be progressed in parallel.**
- **The conclusion of 1) may impact the BSUoS "pot" but is unlikely to change the scale of materiality and urgency.**
- **National Grid should undertake a targeted 6 month review of BSUoS elements (Oct-March) to support overall timescale for BSUoS reforms**

CMP201 Modelling revisited

- An assumption of CMP201 was that BSUoS charges were split 50:50 between production and demand.
- Following CMP202 the production volume from interconnection is no longer liable for BSUoS charges and thus this assumption no longer held
- This assumption affects the modelled consumer impacts in the short-term identified by National Grid's modelling
- Revising this assumption means that the consumer impacts in the short-term are close to neutral
- The longer term benefits from more effective competition will remain.

The case for change has grown since CMP201:			
	Interconnection (GW)	Interconnection volume (TWh)	BSUoS (£/MWh)
CMP201 (2012)	3GW (2GW to mainland EU)	10	£1.51/MWh
Now (2017)	4GW (3GW to mainland EU)	16	£2.48/MWh
Future	c.8GW 2020 c.18GW early 2020s	30-70TWh (2021-2025) ¹	Growing



¹ - BEIS, Updated Energy & Emissions Projections 2017 (January 2018) – Figure 5.1
<https://www.gov.uk/government/publications/updated-energy-and-emissions-projections-2017>



Next Steps:

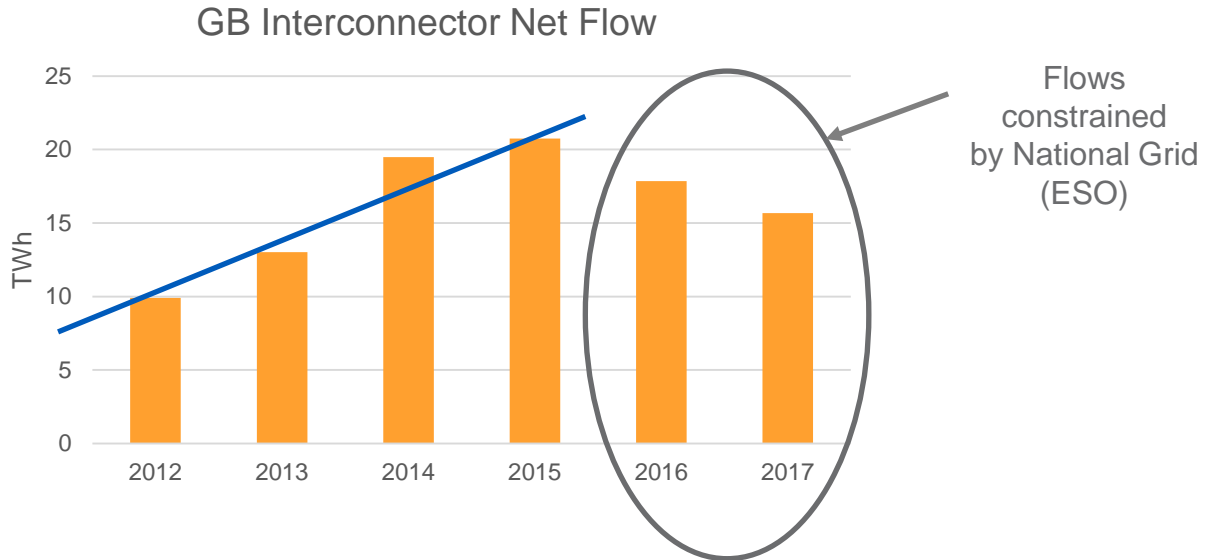
- 26th October 2018 – CUSC Panel
- Q4 2018/Q1 2019 - Workgroup
- H1 2019 – Ofgem decision
- Implementation – 2 years after Ofgem decision to give notice to market



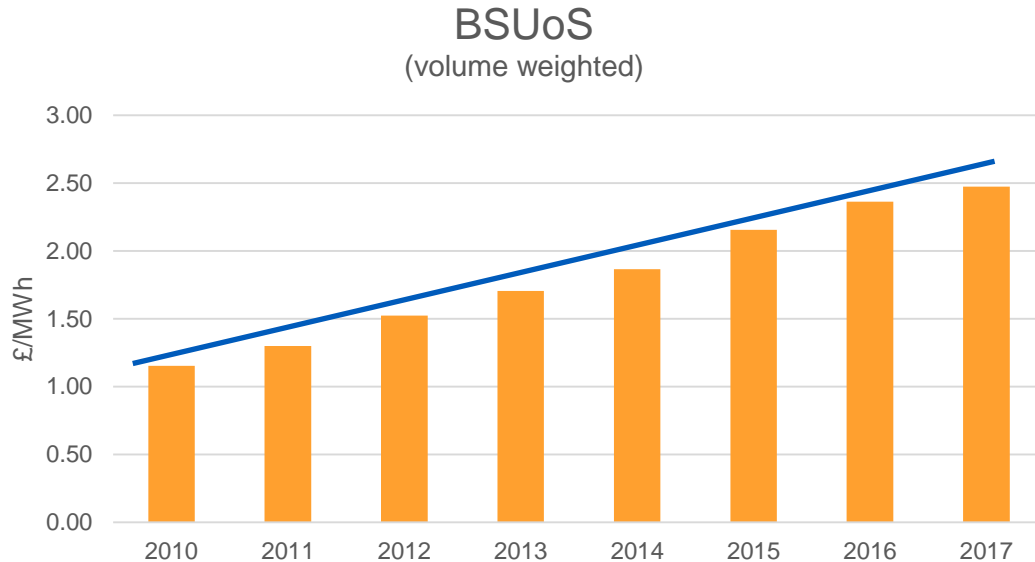
Appendix



Change in interconnector flows since 2012



Historical BSUoS



Impact of BSUoS charged solely on GB demand

- Based on actual 2017 BSUoS data and modelling of interconnector flow changes the table below shows the estimated impact if BSUoS had been charged solely on GB demand.

	2017 Actual data	2017 with change implemented
Increase of GB generation due to proposed change (TWh)	0	2.1
GB chargeable BSUoS volume (TWh)	502.5	504.6
net imports (TWh)	15.7	13.6
Total GB demand (TWh)	259.1	259.1
BSUoS 2017 average (£/MWh)	2.48	2.46
Total BSUoS cost (£m)	1,243.9	1,243.9
BSUoS if charged 100% on demand (£/MWh)	4.80	4.80
Double current BSUoS rate (£/MWh)	4.95	4.95
Delta of BSUoS rate (£/MWh)	0.15	0.15
Minimum Wholesale Market fall to maintain status quo (£/MWh)	2.33	2.33
Consumer impact (£/MWh)		0.00
Consumer impact (£m)		0.0



Note: the minimum Wholesale Market decrease to maintain status quo is 15p/MWh less than the generation BSUoS rate.

Embedded Generation

- The impact on embedded generation of moving BSUoS recovery solely onto GB demand is expected to be neutral, as shown in the table below.

	£/MWh
BSUoS embedded benefit increase	2.33
Wholesale Market decrease*	2.33
Net Embedded Generator impact	0.00

*Wholesale Market decrease to maintain status quo

