

Modification proposal:	Connection and Use of System Code (CUSC) CMP334: Transmission Demand Residual - consequential definition changes (TCR)		
Decision:	The Authority ¹ directs that WACM1 of this modification be made ²		
Target audience:	National Grid Electricity System Owner (NGESO), Parties to the CUSC, the CUSC Panel and other interested parties		
Date of publication:	30 November 2020	Implementation date:	14 December 2020

Background

In November 2019, we published our Decision (and associated Direction) on the Targeted Charging Review (TCR) Significant Code Review.³ Once the Decision is implemented, the costs of operating, maintaining and upgrading the electricity grid will be spread more fairly and, through reducing harmful distortions, will save consumers approximately £300m per year, with anticipated £4bn-£5bn consumer savings in total over the period to 2040.

The TCR included a review of how residual network charges are set and recovered. The aim of the TCR is to ensure that these charges are recovered from network users in a way that meets the TCR Principles:

- reducing harmful distortions;
- fairness; and
- proportionality and practical considerations.

We decided that residual charges should apply to final demand consumers and that residual charges will be fixed charges, from implementation in April 2022. For domestic consumers we decided that there will be a single transmission residual charge, and a single distribution residual charge within each of the 14 distribution licensed areas. For distribution-connected non-domestic consumers, we decided that there will be a charging structure that combines a fixed transmission residual charge and a banded fixed distribution residual charge. For transmission-connected non-domestic consumers we directed that consideration should be given to whether a single transmission band or alternative banding options would be more appropriate.

Alongside our Decision, we issued a Direction to National Grid Electricity System Operator (NGESO) (the 'TCR Direction'), to bring forward proposals to modify the Connection and Use of System Code (CUSC) in relation to residual charges, to give effect to the terms of the TCR Direction.

For the transmission network, the Transmission Owners (TO) recover their allowed revenue from their customers through transmission network use of system (TNUoS)

¹ References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day to day work. This decision is made by or on behalf of GEMA.

² This document is notice of the reasons for this decision as required by section 49A of the Electricity Act 1989.

³ https://www.ofgem.gov.uk/system/files/docs/2019/12/full_decision_doc_updated.pdf

tariffs. Under current arrangements, the forward-looking component of TNUoS charges is calculated first. The residual component is then calculated, so that the total charges recovered are equal to the allowed revenue for network companies set under the price controls.

The modification proposal

NGESO raised five CUSC modification proposals to implement TDR reforms in line with the TCR Decision. CMP343 proposes the methodology for TDR charges to be applied to 'Final Demand' on a 'Site' basis.⁴

NGESO (the 'Proposer') raised modification CMP334 on 16 January 2020, to incorporate definitions relevant for the proposals set out in CMP343, as a consequential modification. CMP334 seeks to define the terms to determine 'Final Demand' on a 'Site' basis in a manner which is consistent with the TCR Direction and the Distribution Connection and Use of System Agreement (DCUSA). It was progressed as part of a Joint Workgroup alongside the equivalent proposed modification to distribution residual charges.⁵

CMP334 identifies which customers are liable for a TDR charge. In line with the TCR Direction, the Original Proposal would introduce new defined terms for 'Final Demand' and 'Single Site'. It would also:

- modify existing definitions that were added to Section 11 of the CUSC, further to the approval of CMP319;⁶
- modify the definitions for the following terms: 'Electricity Generation', 'Electricity Generation Facility, Generator', 'Generation Licensee', 'Electricity Storage Facility' and 'Declaration'; and
- introduce defined terms for 'Final Demand Site', 'Non-Final Demand Site' and 'DCUSA'.

The Proposer considered that the Original Proposal would be positive in terms of Applicable CUSC Objective (ACO) (a) as NGESO has been directed to raise and implement this modification by the Authority to enact the TCR Decision. The Proposer's view is that the Original Proposal would also improve the efficiency of the CUSC arrangements by defining terms which will be used as part of the residual charging methodology and ensure alignment with the DCUSA, and therefore would better facilitate ACO (d).

Following the Workgroup Consultation, a number of respondents raised concerns about the definition of 'Final Demand' in the Original Proposal. Their concern was that the proposal would treat some market participants, which are not final users of electricity as 'Final Demand', making them liable for the TDR. Specifically, they argued that users that solely provide reactive power services for voltage support should not be captured within the 'Final Demand' definition and should be excluded from paying the TDR.

The Proposer raised an alternative proposal to the Workgroup to address this. The Workgroup agreed to support the Workgroup Alternative CUSC Modification ('WACM1'). WACM1 proposes that a specific type of service provider (those providing 'Eligible Services') would not be liable to pay the TDR. This would be achieved by amending the

⁴ CMP343 'Transmission Demand Residual bandings and allocation for 1 April 2022 implementation': <https://www.nationalgrideso.com/industry-information/codes/connection-and-use-system-code-cusc-old/modifications/cmp343-and-cmp340>

⁵ We published our decision on DCP359 on 30 September 2020: <https://www.ofgem.gov.uk/publications-and-updates/dcp359-ofgem-targeted-charging-review-tcr-implementation-customers-who-should-pay>

⁶ <https://www.ofgem.gov.uk/publications-and-updates/cmp319-consequential-changes-section-11-cusc-result-cmp280-andor-281>

definition of 'Final Demand Site' and 'Non-Final Demand Site' such that those 'Single Sites' that import 'Active Power' from the transmission network solely for voltage support would be excluded from paying the TDR. This would mean that users that solely import active power for voltage support ('reactive power assets' for the purpose of this document) would be excluded from paying the TDR.

The Proposer believes WACM1 would be better facilitate ACO (b) than the Original Proposal because it would address the distortive effects which reactive power assets would face under the Original. The Proposer considers the Original to be distortive as such users would be required to pay the TDR, unlike other users (e.g. generators) that also provide reactive power services.

The Workgroup assessed the Original Proposal and WACM1 against the ACOs. The Workgroup voted by majority in favour of WACM1.

CUSC Panel⁷ recommendation

At the CUSC Panel meeting on 31 July 2020, a majority of the CUSC Panel considered that CMP334 would better facilitate the CUSC objectives and the Panel therefore recommended its approval. The CUSC Panel unanimously recommended the Original, and by majority, WACM1 would better facilitate the CUSC Objectives than the Baseline. Four Panel Members voted for the Original as the best option, and five Panel Members voted WACM1 as the best option. The table below summarises the Panel votes against the ACOs.

Proposals	Applicable CUSC Objectives							
	A		B		C		D	
	+ve	-ve	+ve	-ve	+ve	-ve	+ve	-ve
Original Proposal	9	0	0	0	0	0	7	0
WACM1	5	3	0	2	0	0	4	2

Summary of Panel Member votes. Neutral assessments not shown.

Our decision

We have considered the issues raised by the FMR⁸ dated 13 August 2020 including the responses to the Workgroup Consultation and the Code Administrator Consultation. We have concluded that:

- WACM1 would better facilitate the achievement of the ACOs;⁹ and
- directing that WACM1 be made is consistent with our Principal Objective and statutory duties.¹⁰

Reasons for our decision

⁷ The CUSC Panel is established and constituted from time to time pursuant to and in accordance with section 8 of the CUSC.

⁸ CUSC modification proposals, modification reports and representations can be viewed on NGENSO's website at: <https://www.nationalgrideso.com/industry-information/codes/connection-and-use-system-code-cusc/modifications>

⁹ As set out in Standard Condition C10(1) of the Electricity Transmission Licence, see: <https://epr.ofgem.gov.uk/Content/Documents/Electricity%20transmission%20full%20set%20of%20consolidated%20standard%20licence%20conditions%20-%20Current%20Version.pdf>

¹⁰ The Authority's statutory duties are wider than matters which the Panel must take into consideration and are detailed mainly in the Electricity Act 1989 as amended.

We consider that both the Original and WACM1 would better facilitate ACOs (a), (b) and (d). We believe that approving WACM1 brings further benefits than the Original as it implements the relevant parts of our Decision whilst facilitating additional benefits with respect to ACO (b).

(a) the efficient discharge by the licensee of the obligations imposed upon it under the Act and by this licence

The Proposer believes that both the Original and WACM1 would better facilitate ACO (a), as NGESO has been directed by the Authority to raise modifications to implement its Decision.

The Panel unanimously voted that the Original proposal would better facilitate ACO (a), as the proposal would allow the implementation of the TCR Decision and satisfy NGESO's licence requirements.

Regarding WACM1, five Panel Members voted that it would better facilitate this objective, for the same reasons as the Original. Three Panel Members voted that this proposal would be negative on ACO (a). They expressed concerns that exempting some parties from the TDR would result in some market participants avoiding what they consider to be a cost-reflective charge. They further argued that it is arbitrary to exclude market participants operating these assets from the TDR charge as they are not covered by the Decision. One Panel Member assessed the WACM1 proposal as neutral to this objective.

Our position

We consider that both the Original and WACM1 better facilitate ACO (a). We are satisfied that both proposals address the TCR Direction to define 'Final Demand' and 'Site'. Both proposals introduce the definitions necessary for the implementation of the TCR Direction, and they will overall enable NGESO to ensure consistency and clarity in the use of the new terms across the CUSC.

We do not agree with the view that WACM1 arbitrarily excludes specific market participants from the requirement to pay TDR charges. While the treatment of reactive power assets was not a specific requirement of the TCR Direction, we welcome the Workgroup discussions and consider the proposal to be consistent with the TCR Decision. Therefore, we believe that this approach is aligned with our policy intention to reform residual charging arrangements and remove these charges from non-final demand consumers. We address the Panel views on cost-reflectivity under ACO (b), below.

Private wires / complex sites

In the TCR Direction, we directed (paragraph 33.c) that '*appropriate arrangements to develop any consequential changes that may be required in relation to residual charges for [...] consumers connected to private wires and complex sites.*' At the Workgroup Consultation stage, two respondents raised concerns that the definitions in the proposals for CMP334 and DCP359 do not work for complex sites.

We agree that the Workgroup has failed to bring forward a proposal that covers private wires and complex sites. The Workgroup indicated in the CMP334 FMR that changes to private wires and complex sites would be dealt with through DCP328, not this modification.¹¹ DCP328 is only applicable to distribution-connected customers, and

¹¹ DCP 328 'Use of System Charging for Private Networks with Competition in Supply'
<https://www.dcusa.co.uk/change/use-of-system-charging-for-private-networks-with-competition-in-supply/>

therefore would not cover transmission-connected customers. As a result, our view is that this obligation of the TCR Direction has not been discharged and will continue to apply notwithstanding our decision on this proposal. This is addressed further below in the "Other Issues" section of this letter.

(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

The Proposer and Panel unanimously considered that the Original proposal is neutral for ACO (b).

The Proposer believes WACM1 would better facilitate ACO (b) as it would avoid a distortion among reactive power service providers that the Proposer perceives the Original Proposal to create. The Proposer believes that the aim of the TCR to '*reduce harmful distortions which impact competition and the efficiency of the electricity market*' is not fully met by the Original Proposal, as it does not cover all types of market participants which it does not think should be considered to be 'final' demand'.

The CUSC Panel by majority voted that WACM1 is neutral against ACO (b). Two members voted that this proposal does not better facilitate this objective. They argued that WACM1 gives preferential treatment to certain parties by excluding them from paying what they consider to be cost-reflective charges, distorting competition.

Our position

We believe that removing the residual charges from all generation (including electricity storage) facilitates competition and as such, both the Original and WACM1 are positive against ACO (b). We consider that competition is facilitated to a greater extent under WACM1 as it will remove the distortion that would otherwise exist between other competitors and reactive power assets if the latter were required to pay TDR whilst the former are not.

We also note that (as stated in the TCR Decision), we believe that, unlike forward-looking charges, residual charges should not send a cost-reflective signal, as they are cost recovery charges. We therefore disagree with the assertion that WACM1 excludes some parties from paying certain cost-reflective charges.

In our assessment of WACM1 against this objective, we considered the existing markets in which reactive power assets could compete to understand the impact of the WACM1 solution on competition. We disagree with the view that this proposal would result in discriminatory or preferential treatment.

In providing these services, reactive power assets are competing with (amongst others) generators and TOs, which are not subject to the TDR. As such, not requiring reactive power assets to pay the TDR would level the playing field between them in this respect.¹² WACM1 will help level the playing field for participants in the reactive power services market. We therefore disagree with the contention that WACM1 would be distortive.

¹² Reactive power assets may also compete with demand-side response (DSR) providers, which will be subject to the TDR as final demand consumers. As a fixed charge, we would not expect the TDR to distort the market for DSR assets providing voltage support services. Though, we acknowledge that use of DSR could conceivably affect a user's charging band allocation (if applicable) and hence its residual charge. Whether or not to apply a banding approach for TDR for transmission final demand consumers is under consideration as part of CMP343.

We note that the exclusion for reactive power assets from paying the TDR would not extend to the equivalent Distribution Use of System (DUoS) residual charge. In our decision on DCP359, we noted that it would be open to DCUSA Parties to bring forward a further modification proposal to align the two codes in this respect (if we were to approve the WACM).

We also note that, during the Workgroup assessment, it was discussed that it may be proportionate for other assets competing in different areas of the market to be treated in the same way as reactive power assets under the WACM1 proposal. It would be open to industry parties to bring forward a further modification proposal to the CUSC for any similar assets to be consistently treated in the CUSC. This potential for further modifications does not change our assessment that WACM1 better facilitates ACO (b).

In conclusion, we consider that WACM1 will better facilitate ACO (b) to a greater extent than the Original by aligning the treatment of generators, TOs and reactive power assets in respect of the TDR.

(d) promoting efficiency in the implementation and administration of the CUSC arrangements

The Proposer believes that both the Original and WACM1 better facilitate ACO (d) as both improve the efficiency of the CUSC arrangements by defining terms which will be used as part of the residual charging methodology ensuring alignment with the DCUSA.

The majority of the Panel Members agreed with the Proposer that the Original would better facilitate ACO (d). Two members assessed the modification as neutral against this objective.

In the assessment of WACM1, four members of the Panel believed that it better facilitates ACO (d) for the same reasons as the Proposer. Some also argued that WACM1 has more benefit for this objective compared to the Original as it avoids a potential market distortion and inefficiency that would be created by the Original. Two Panel Members argued that WACM1 is negative against ACO (d) for the same reasons as they voted in the previous ACOs. They argued that this proposal creates discrimination by allowing some market participants to avoid what they perceive to be a cost-reflective charge.

Our position

We consider that both proposals better facilitate ACO (d), as both define the terms that are necessary for the implementation of the TCR Direction and clarify who should be liable for TDR charges. As noted in the previous ACO assessments, we disagree with the negative arguments against WACM1. We have addressed these arguments under ACO (b).

We note that WACM1 would introduce differences between the treatment of reactive power assets between the CUSC and DCUSA. We do not consider that this would affect ACO (d), but we have noted above that it is for DCUSA Parties to bring forward a further modification proposal to align the two codes in this respect.

Other Issues

Obligation to address private wire and complex sites

As noted in our assessment on ACO (a) we believe that the obligation of the TCR Direction to address private wire and complex sites has not been discharged.

We expect the new modification to be developed in a way that allows implementation by April 2022. This will provide the Workgroup the opportunity to establish a comprehensive approach to treating private wires and complex sites, as it will allow for different potential scenarios and potential consequences to be explored in detail. We note that there may be a need for further changes to other industry codes as a result of this modification. For clarity, we expect that any proposal brought forward will ensure that:

- sites that would not be subject to the TDR under CMP334 WACM1 would be not be subject to the TDR if they exist in a private wire/complex site; and
- any site in a private wire/complex site that has associated final demand would be liable for the TDR in a proportionate way.

Impact Assessment

Section 5A of the Utilities Act 2000 imposes a duty on the Authority (its 'Section 5A duty') to undertake an impact assessment in certain circumstances. In particular, that applies where it appears to the Authority that a proposal is important. A proposal is important for these purposes if its implementation would be likely to, among other things, "have a significant impact on persons engaged in commercial activities connected with the ... generation, transmission, distribution or supply of electricity." Where this applies, the Authority is obliged to carry out an impact assessment.

We conducted an impact assessment as part of our TCR Significant Code Review which was taken into consideration in our Decision. The designation of the residual charge to final demand consumers, as achieved by WACM1 of CMP334, is consistent with our TCR Decision. The implementation of this modification will give effect to specific aspects of the Decision, and as such, we consider that the impact assessment conducted for the TCR Decision satisfied our obligations under the Utilities Act, with respect to this modification.

Implementation Date

Two respondents to the Code Administrator Consultation supported the need for a further year's delay of the implementation of the TCR due to the impacts of the pandemic on suppliers, proposing alignment with the implementation of the Access and Forward-Looking Charges reforms scheduled for 2023.¹³

We consider that, although Covid-19 may have impacted industry over recent months, we have not been presented with robust evidence to support delaying this specific modification.

Legal Text

We have reviewed the legal text and, while we do not believe there to be substantive issues, there may be merit in considering if a housekeeping modification should be raised. It appears that there is at least one inconsistency in the legal text that could cause confusion. For example, in the definition of 'Final Demand Site' we believe that "All Users" should be replaced with "For Users" for consistency with the subsequent points.

Decision notice

¹³ <https://www.ofgem.gov.uk/electricity/transmission-networks/charging/reform-network-access-and-forward-looking-charges>

In accordance with Standard Condition C10 of the Transmission Licence, the Authority, hereby directs that WACM1 of modification proposal *CMP334: Transmission Demand Residual - consequential definition changes (TCR)* be made.

Andrew Self

Deputy Director, Electricity Access and Charging – Energy Systems Management & Security

Signed on behalf of the Authority and authorised for that purpose