

CUSC Alternative Form

CMP381 WACM1:

Defer exceptionally high Winter 2021/22 BSUoS costs to 2022/2023

Overview: This alternative is identical to the original solution, except for the implementation date. We propose implementation is one business day after an Ofgem decision.

Proposer: George Moran, Centrica

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What is the proposed alternative solution?

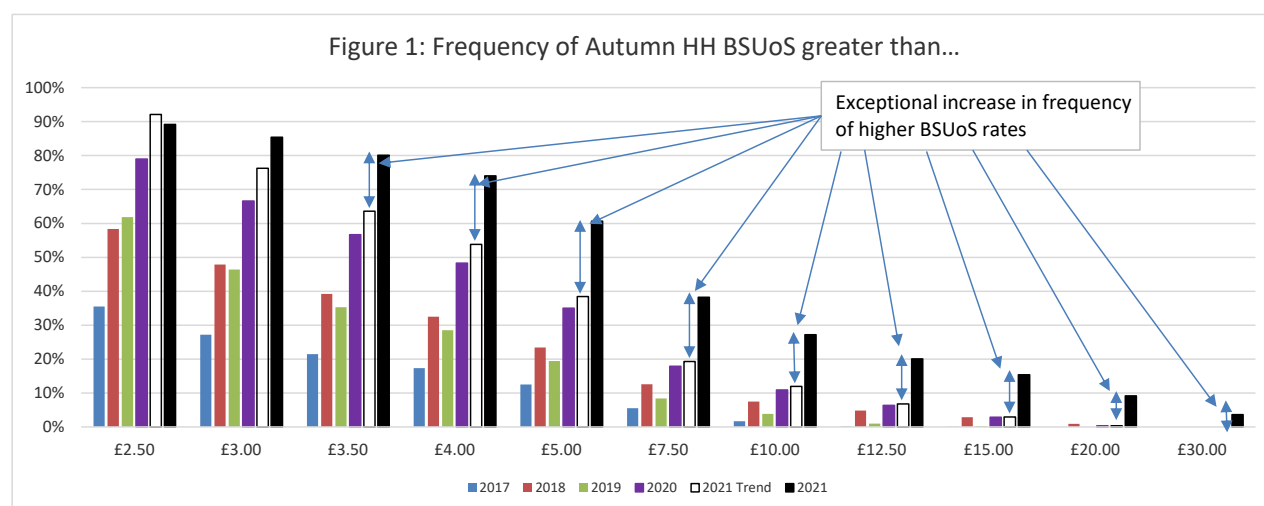
Our alternative is identical to the Original Proposal except for the implementation date. Therefore, the key elements are:

- Set a £10/MWh cap on BSUoS from 1st business day after Ofgem decision until 31 March 2022.
- Defer the additional BSUoS costs above the cap to the 2022/23 charging year using a similar mechanism approved under CMP345 and CMP350 (as per Original).
- Recover the additional BSUoS costs above the cap from 1 April 2022 (based on forecast if actuals are not available) (as per Original).
- Recover an identical amount per day that is allocated to Settlement Periods on a chargeable volume weighted basis. This is in line with the approach used for CMP373 (as per Original).
- Limit the BSUoS costs that could be deferred to £300m (as per Original).

We are retaining the £10/MWh cap proposed in the Original as our analysis, based on publicly available data, requires this level of cap for HH BSUoS prices to produce an average BSUoS price which a prudent market operator could have reasonably foreseen.

The issue, as we understand from the Proposal, is that the **totality** of BSUoS costs observed to date in Winter 2021 have been much higher than consumers and industry parties could have reasonably forecast. The totality of BSUoS costs is represented by the average BSUoS rate and so the issue is that the **average BSUoS price** is exceptional.

The average BSUoS price is exceptional due to the increase in the frequency of 'high' BSUoS prices across the distribution curve, not just at the extreme end of the distribution curve. This is demonstrated by Figure 3 in the consultation document and by our own Figure 1 below:



Using data from the autumns (Sep-Nov) of 2017-2020 we have plotted the trend in how frequently BSUoS could be expected to outturn higher than a range of different price levels (the hollow black column in the chart) and compared this to what has been observed in 2021 (black column). We consider that the trended frequency distribution represents an objective view of the reasonable expectation of market participants since they take account of the observed increases in both the absolute level of BSUoS and BSUoS volatility over the last few years. The difference between the observed 2021 levels and the trended 2021 levels can therefore be considered to be a reasonable representation of the exceptional BSUoS costs observed in Autumn 2021.

Therefore, we believe that debate surrounding what constitutes an exceptional Half Hourly BSUoS rate, or data point, fails to properly address the issue raised by the Proposal. The question is not '**what constitutes an exceptional HH BSUoS price?**' but rather '**what HH cap is required to reduce the exceptional average BSUoS price to one which could have been reasonably foreseen?**'.

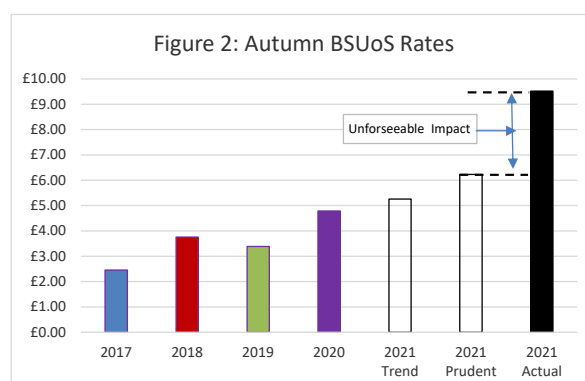
We have produced analysis which:

1. Objectively derives **£6.23/MWh** as an average BSUoS rate which a prudent market participant could have reasonably foreseen for Autumn 2021.
2. Derives the HH cap (**£9.87/MWh**) which would have delivered this prudent average BSUoS rate.

Objectively derived prudent BSUoS rate - £6.23/MWh:

Using a trend of observed BSUoS rates over previous autumns to project what a market participant could have anticipated for autumn 2021 provides an estimated BSUoS rate of £5.26/MWh. This 'central' view is not too dissimilar, but is higher, than the forecast provided by National Grid ESO in August (just prior to the autumn) of £4.95/MWh. We use this as a sense check for the objectively constructed trend estimate of £5.26/MWh. It is not surprising that this is higher than the ESO forecast since it includes unadjusted exceptional BSUoS costs from the Covid lockdown period in Autumn 2020 to derive the trend value and so could already be considered to include an element of prudence.

We then build in an error margin to reflect the likely actions a prudent market participant would take when seeking to price BSUoS for autumn 2021 ahead of time. For this, we have used the BSUoS variability analysis conducted by the ESO and published as Table 4 in the CMP361 Code Administrator consultation. That analysis estimates a quarterly P80 level of BSUoS cost variability of £122m, which equates to £0.97/MWh for Autumn 2021. Adding this P80 variability risk to the central view above gives a prudent BSUoS estimate of £6.23/MWh. Figure 2 below shows how this prudent estimate compares with Autumn 2021 outturn BSUoS rates. We consider the difference between the objectively derived prudent estimate of £6.23/MWh and the outturn rate of £9.52/MWh is a good representation of the BSUoS costs that could not have been reasonably foreseen by a market participant acting prudently.



Cap to deliver prudent BSUoS rate - £9.87/MWh:

To find the cap level required to produce the prudent BSUoS rate for Autumn 2021 (i.e. £6.23/MWh as described above), we have taken published half hourly SF BSUoS prices for Sep-21 to Nov-21 and utilised Excel's goal seek functionality. The resulting HH BSUoS cap required is £9.87/MWh. We therefore consider the £10/MWh cap proposed in the Original is appropriate.

We have included a spreadsheet with our response (CMP381 – supporting data. xlsx) which provides the supporting data and calculations behind this analysis.

What is the difference between this and the Original Proposal?

Our alternative is identical to the Original Proposal except for the implementation date

What is the impact of this change?

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;	<p>Positive impact</p> <p>The proposal will provide some mitigation against the exceptional losses likely to be being incurred by Parties because of the current levels of BSUoS costs.</p> <p>Deferring costs to a future period will allow Parties to reflect these exceptional costs into future tariff offerings. Such protection, for exceptional events, that are high impact and low probability, will reduce the level of risk that will need to be factored into future tariffs and facilitate effective competition in the generation and supply of electricity. In our view this will, as a result, lower the long-term costs to consumers.</p> <p>The change will also mitigate against the risk of further insolvencies that would lead to greater costs for consumers in both the short term (SoLR costs) and long term (reduced competition).</p>
(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 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);	None

(c) That, so far as is consistent with subparagraphs (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;	None
(d) Compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency *; and	None
(e) Promoting efficiency in the implementation and administration of the system charging methodology.	None
*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).	

When will this change take place?

Implementation date:

First business day following an Ofgem decision.

Implementation approach:

As per Original, except for the implementation date.

Acronyms, key terms and reference material

Reference material:

1. We have included a spreadsheet with our response (CMP381 – supporting data. xlsx) which provides the supporting data and calculations behind the analysis above.