



Please use this Pro-Forma when responding to the Interim Report and Consultation of the second Balancing Services Charges Task Force.

The Taskforce will take all responses into its consideration when producing the final report. When providing a response please supply a rationale, particularly in respect of any specific questions detailed below.

Please send your responses to chargingfutures@nationalgrideso.com by 5pm on **26 August 2020**. Please note that any responses received after the deadline or sent to a different email address may not be taken into account by the Taskforce.

If you have any queries on the content of this consultation, please contact us at chargingfutures@nationalgrid.com.

Question	Response
<p>1. Do you agree with the Task Force's recommendations on who should pay Balancing Services Charges (Deliverable 1)? Please state your reasoning and evidence behind your answer.</p>	<p>Yes, SSE agrees that it is appropriate to collect BSUoS wholly from final demand, as long as suppliers have sufficient notice of the change – we suggest at least 2 years. The reasons for collecting BSUoS wholly from final demand are the same as those identified by Ofgem in the TCR decision and we have called out some specific points below.</p> <p>Collecting BSUoS wholly from final demand would reduce the market distortion and competitive disadvantage that GB transmission connected generators currently face compared with distribution connected generators and interconnected generators. Removal of this distortion will tend to result in a more economically efficient system at lower cost to customers over the long-term.</p>

	<p>It will also remove distortions to the electricity wholesale market, balancing market and ancillary services markets, including a feedback loop whereby an inaccurate forecast of generator BSUoS charges feeds into generator bid prices, which in turn feeds back into the BSUoS charge. Moving the charge to wholly final demand would remove these distortions, along with associated risk premiums and unintended consequences which arise from charging BSUoS to larger generators.</p> <p>We agree that the alternative approach to rectifying the distortion, to charge BSUoS to all forms of generation, is not a viable solution, because it would not be practical, or proportionate to develop a methodology to charge BSUoS to all generators behind customer meters.</p>
<p>2. The Task Force have discussed how the recommendation on Deliverable 1) for Final Demand only to pay Balancing Services Charges could impact on large energy users and the potential for 'grid defection'. Do you think 'grid defection' is a possibility and to what extent would the Task Force's recommendations impact on your answer?</p>	<p>The answer to this question depends on the choice of charging base and whether it is applied as a £/site fixed charge, or a £/MWh volume charge.</p> <p>If £/site fixed charge – best solution</p> <p>If the charge is applied on a “per site” basis the same as the TCR solution for TNUoS and DUoS, then this will generally <u>reduce</u> the risk of grid defection. A fixed charge would reduce the incentive for customers to invest in and operate behind the meter generation as it would become more difficult and less financially attractive to attempt to avoid network charges through either partial, or full defection from the grid. This reduction of harmful distortions is a key benefit of moving to the £/site fixed charge solution.</p> <p>However, we understand that some parties may be concerned about a theoretical risk that a minority of large customers could face an increased incentive for full grid defection, although</p>

	<p>we are not convinced this risk is material in practice. This theoretical risk would only apply to a specific group of large customers who already have a substantial capacity of behind the meter generation and could face an increased incentive to move from their current position of partial grid defection to a position of full grid defection. This full grid defection may be achieved through either investing in additional behind the meter generation, or relocating their business activities away from the GB market. This change in incentive occurs because, currently, if a customer has already partially defected from the grid, then the incremental value to them of incremental levy avoidance from taking these additional steps would be relatively low. However, if BSUoS revenue recovery charges changed, so they could only be avoided by full grid defection, then this may increase the value to that specific type of customer of the final incremental investment required to make the leap to full grid defection.</p> <p>We would suggest any perceived increase in risk of some large customers transitioning from partial grid defection to full grid defection should not undermine the proposed solution, but should instead be treated as an implementation issue. If Ofgem is concerned that this risk may exist, then it would be most appropriately addressed by considering the economic principle of Ramsey Pricing applied to revenue collection, whereby behavioural distortions could be reduced by reducing charges on those users which have a relatively high price elasticity and correspondingly increasing charges on those users which have a relatively low price elasticity.</p> <p>Any solution for BSUoS should be considered in the context of Ofgem's decision regarding the TCR changes to the TNUoS and DUoS demand residuals and could include consideration of:</p>
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- 1) Appropriate banded charge for larger users relative to other types of customer for TNUoS, DUoS and BSUoS.
- 2) Specific band, or discounts to the regular band for users specifically classed as being Energy Intensive Industries (EII). This would be consistent with the approach BEIS uses for the collection of low carbon policy costs. We would recommend that Ofgem discuss this issue with BEIS.

If £/MWh volume charge – a poor solution

For the reasons provided in our answer to question 1, we fully support the proposal to move revenue collection levies, including BSUoS, to be wholly from final demand. However, if BSUoS were moved to be wholly from final demand and specifically left as a £/MWh volume charge, then this would tend to increase the incentive for grid defection for all types of customer, as compared with using a fixed £/site charge.

We agree with Ofgem's conclusions in the TCR decision that a volumetric £/MWh charge is one of the worst possible methods for revenue recovery. This is because it is the easiest to avoid and therefore provides the largest distorted incentive for grid defection through an excessive incentive to invest in and operate behind the meter generation.

If demand BSUoS were applied on a £/MWh volume basis, it would mean that behind the meter generators could still earn a demand BSUoS levy avoidance credit, putting them at odds with generators connected at all other locations. This is because Distribution connected generators have their BSUoS embedded benefit removed by CMP333, while transmission connected generators

	<p>never had a BSUoS embedded benefit to begin with.</p>
<p>3. Do you agree with the Task Force's recommendations that an ex ante fixed charge would deliver overall industry benefits? Please state your reasoning and evidence behind your answer.</p>	<p>Yes we agree with this Task Force recommendation for the reasons described in the draft Task Force report and in particular, summarised below.</p> <p>Fixed for a period of time As per the conclusions of the first BSUoS Task Force, BSUoS does not provide any useful price signal, so it should be treated as revenue collection according to Ofgem's TCR principles. With this in mind, the current approach of having BSUoS vary per half hour settlement period does not provide any system benefit, but instead creates unnecessary distortions and risk resulting in higher system cost. It would therefore be beneficial for the system and better value for customers in the long-term for BSUoS to be a fixed charge set for a period of time.</p> <p>Fixed in advance Setting BSUoS in advance will reduce the costs associated with risk for suppliers, resulting in lower costs for customers over the long-term. For suppliers, BSUoS forecasting errors represent a volatile and unpredictable P&L impact, and is a substantial unnecessary source of risk for suppliers. Being fixed in advance would reduce supplier cost of capital and cost of risk margins, so ought to result in lower costs to customers. There would be no offsetting system benefit from exposing suppliers to BSUoS risk because suppliers cannot take any action to manage any of the underlying fundamental causes of BSUoS variability.</p> <p>Fixed by the ESO The ESO is in the best position to accurately forecast BSUoS and to take actions which may mitigate the underlying drivers of BSUoS volatility. As long as ESO has the regulatory authority to collect BSUoS costs from suppliers, then for the ESO, BSUoS is only a cash flow item, not a P&L item, so the value of BSUoS risk to</p>

	<p>the ESO should be much smaller than for suppliers. This suggests ESO should be much better placed to manage BSUoS uncertainty and volatility at a lower cost of capital and lower cost of risk margin, compared with suppliers.</p> <p>Moving BSUoS forecasting risk from suppliers to the ESO should result in a reduction in total system cost and a net reduction in cost to customers. However, consideration should be given to what adjustments to ESO incentives may be appropriate to recognise any related change in ESO exposure to cash flow risk such as ESO securing additional debt finance.</p> <p>Lower collection risk if charged £/site Using a fixed charge £/site would reduce the value associated with the risk of BSUoS forecast error because the denominator (number of sites) is known in advance and would have little variation between years. This would tend to reduce the magnitude of ESO over, or under collection along with corresponding adjustments to future years. By contrast, if using £/MWh, the denominator of demand volume is much more variable and uncertain between periods and would tend to result in relatively greater forecast error, incorrect collection and relatively larger adjustments to future years.</p>
<p>4. How long do you think the fixed period should be and what in your opinion is the optimal notice period in advance of the fixed charge coming into effect? Please state your reasoning and evidence behind your answer.</p>	<p>We recognise that there is a trade-off between fixing the price for a longer duration with a longer notice, compared with the risk of larger forecast error and longer lag times before adjustments can be applied. It is therefore important to identify an appropriate balance of these issues.</p> <p>For a fixed charge £/site – best solution To achieve the majority of the supplier benefit from a reduction in the cost of managing BSUoS risk and deliver the best value for customers, then BSUoS should be fixed for a duration of at least 6 months with a minimum of 8 months' notice,</p>

	<p>although 14 months' notice could deliver some additional benefit.</p> <p>The rationale for 8 months' notice is that if a customer is negotiating to fix their supply tariff a couple of months before the start of a financial year, then this would give suppliers visibility of the fixed BSUoS rate for the whole 12 month contract period, with one period starting in two months and the second period starting in 8 months.</p> <p>Fixing the duration for 6 months would mean the process would work equally well for customer who may want their fixed price period to begin from either April, or October. Also 6 months would shorten the lag time for ESO to apply forecast error adjustments compared with a 12 month fixed duration.</p> <p>A fixed duration of 12 months would also be beneficial.</p> <p>Some customers may want to fix their tariffs for longer durations, such as two, or three years ahead, although we appreciate there are practical limits regarding how far in advance it would be reasonable to fix BSUoS tariffs.</p> <p>For a commodity charge £/MWh – a poor solution</p> <p>For the reasons provided above, it would be a relatively poor solution to collect BSUoS as a £/MWh volume charge, however, if it were to be collected in this way, then it would be more appropriate to use a longer fixed duration of 12 months. This would be to avoid unintended consequences which could arise from providing customers with a different £/MWh operational dispatch signal in the summer months compared with winter months. A six monthly fixed tariff would unfairly penalise customers whose demand profile may be weighted more to one season rather than another and it may also distort operational dispatch decisions</p>
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	<p>in some seasons more than others.</p> <p>A 12 month fixed duration would be consistent with the approach used by the largest low carbon policy revenue recovery charge, the Renewables Obligation, which is also fixed for 12 months, and set 6 months in advance.</p>
<p>5. Which approach discussed by the Task Force (TDR banded £/site/day or volumetric £/MWh) do you feel is most appropriate for Balancing Services Charges? Please consider your answer against the TCR principles and state your reasoning and evidence to support your answer.</p>	<p>The most appropriate charging base for BSUoS would be the same charging base as the TCR solution for the TDR banded on a £/site/day basis.</p> <p>The rationale is the same as Ofgem's decision regarding the TCR solution with some key points described below:</p> <p>Reducing harmful distortions: As we described in our answer to question 2, regarding grid defection, a fixed charge is more difficult to avoid and would reduce harmful market distortions. It would achieve this by reducing the incentive for customers to make economically inefficient investment and operational dispatch decisions in an attempt to avoid paying BSUoS revenue recovery charges.</p> <p>By contrast, a £/MWh charge is much easier to avoid, so would tend to overly incentivise both the investment in and operational dispatch of behind the meter generation. A volumetric charge would leave in place a distortion that behind the meter generation would still earn a BSUoS avoidance embedded benefit, providing a competitive advantage compared with generators connected to either the transmission network, or distribution network, or interconnectors, which would not be able to earn that same benefit.</p> <p>As we describe in our answer to question 3, a fixed charge per site would also reduce distortions caused by over, or under collection adjustments between years. This is because the ESO could more accurately forecast the charging base using sites, compared with supply volume, so a "per site" basis should result</p>

	<p>in less over, or under collection adjustments to future years. This could reduce supplier risk margins for longer duration fixed price contracts and reduce other unintended consequences which may arise from inaccurate BSUoS forecasting.</p> <p>Fairness: A fixed charge is fairer because it reduces the risk that revenue collection charges would otherwise tend to land disproportionately on those users who are least able to avoid them. Also, the same rationale for the choice of bands would apply to BSUoS; namely that it would tend to appear fairer that larger customers should tend to pay more than smaller customers.</p> <p>Proportional and practical: Using the same banding criteria as the TDR would be a proportional and practical result because these bands are already being created and communicated with customers. By contrast, if BSUoS were to use a similar, but different approach, then this would be unnecessarily confusing for customers and require unnecessary administrative burden for industry.</p>
<p>6. The Task Force noted limitations of the approaches covered in Q5, what other methodologies or improvements to the ones in Q5 could you recommend to tackle them? Please consider your answer against the TCR principles and state your reasoning and evidence to support your answer.</p>	<p>If there were a desire to improve the way that charging bands and their associated tariffs were calculated, then this should be done at a holistic level taking into account arrangements for TNUoS and DUoS as well as BSUoS.</p> <p>By contrast, it would not be practical, or proportionate to change the banding process for BSUoS in isolation from other charges.</p>
<p>7. Is 2years' notice of the changes prior to an implementation date appropriate? Please state your reasoning and evidence behind your answer.</p>	<p>We would request a relatively prompt decision from Ofgem and that any resulting CUSC modification be progressed in a timely manner to provide a clear signal to industry. This would provide industry with certainty at the earliest opportunity so suppliers and generators can take it into account in</p>

	<p>contractual arrangements, as well as giving suppliers notice of relevant changes required to their IT systems. Early certainty would also deliver the associated system benefits from reducing market distortions, as well as delivering benefits for customers as quickly as possible.</p> <p>Yes, it would be sufficient to have 2 years notice between an Ofgem final modification decision and the year in which the new tariffs would apply. By contrast, if the change results in ESO publishing tariffs with a “regular” notice of, say 12 months, then it would not be necessary to provide 2 years notice ahead of the ESO starting to publish new tariffs if this meant a total of 3 years notice between Ofgem decision and the tariffs applying.</p> <p>As per Ofgem’s decision to delay the implementation of the TCR changes to TNUoS demand residual, shorter notice than this would mean that many suppliers would not have sufficient time to reflect the new arrangements into customer tariffs. This would mean the projected benefits of the changes would not in practice be realised and it would expose suppliers to unreasonable risk.</p> <p>Sufficient notice is required from final modification decision to provide suppliers with certainty that the change will happen, how it will work and what the new tariffs are likely to be. By contrast, 2 years notice from an Ofgem “minded to” decision may not give suppliers sufficient certainty to accurately apply this to customer tariffs without significant risk margins, if they still had poor visibility of what the final tariffs are likely to be.</p>
<p>8. Should the Task Force consider any interim measures? Please provide details of any suggested interim solution including how it may deliver benefits to</p>	<p>As long as sufficient notice is given, then no interim measures would be required.</p> <p>However, there may be some benefit to customers from implementing some of the BSUoS Task Force recommendations at an earlier date than others. In particular,</p>

<p>consumers or help to mitigate specific challenges facing market participants, whilst limiting any windfall gains or losses between industry participants.</p>	<p>changing BSUoS to be a fixed charge set in advance could be introduced at relatively shorter notice and deliver some system and customer benefits early. If this remained levied as a £/MWh volume charge on an interim basis, then it should cause limited distributional impacts, because the fixed charge should be broadly in line with the value market participants were already expecting.</p> <p>By contrast, a longer notice period of 2 years would be required for the other elements of the Task Force recommendations, namely moving to be wholly from final demand and also to become a fixed charge £/site.</p>
<p>9. Do you feel that there any interactions with the Supplier Price Cap that need to be considered? Please state your reasoning and evidence behind your answer.</p>	<p>SSE is not commenting on this question because we no longer supply domestic customers subject to the price cap</p>
<p>10. The Task Force's initial recommendation is that Final Demand only will pay BSUoS. If this is the case, is the current RCRC mechanism is still appropriate? Please state your reasoning and evidence behind your answer.</p>	<p>Any consideration of RCRC is not dependent on eventual changes to BSUoS.</p> <p>If BSUoS does become wholly from final demand, this would not in itself result in the current RCRC arrangements becoming inappropriate.</p> <p>If there were a desire to consider changes to RCRC, then this should be considered separately, and would be outside of the scope of the BSUoS Task Force.</p>
<p>11. Is there anything further you think the Task Force needs to consider?</p>	<p>Not at this time</p>
<p>12. Please use this box to add any further comments that you may have</p>	<p>No further comments at this time</p>

