Modification proposal:	**Connection and Use of System Code (CUSC) CMP353: Stabilising the Expansion Constant and non-specific Onshore Expansion Factors from 1st April 2021**		
Decision:	The Authority[1] directs that 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:	2 December 2020	Implementation date:	1 April 2021

Background

Generators and demand users pay for the ongoing costs of the transmission network via Transmission Network Use of System (TNUoS) charges. These charges are a combination of cost-reflective forward-looking charges and residual charges. Cost-reflective TNUoS charges are designed to reflect the different costs of demand and generation at various locations on the transmission network, to incentivise the efficient use of the system.

The expansion constant is an input to the TNUoS charging methodology. It reflects the annuitized £/MW/km cost of 400kV overhead line and acts as a multiplier to the 'nodal' TNUoS prices (the relative costs of adding 1MW of generation at each point on the network, or 'node'). The expansion constant directly affects the locational signals that users face.

The expansion constant is set at the start of each Price Control period and is based on projects built in the previous price control period. It is then adjusted for inflation in each year of the Price Control period. The expansion constant for the next Price Control period has been calculated based on the current definition in the CUSC and, due to a lower number of built projects in RIIO-1 and the relatively high cost of these in comparison to the projects in previous periods, it has increased significantly. The RIIO-1 expansion constant value used in the calculation of the 2020/21 tariffs was set at £14.93/MW/km, whereas the RIIO-2 expansion constant has increased by 83% to £27.38/MW/km under the baseline

The modification proposal

CMP353 was raised by National Grid Electricity System Operator ("NGESO") on 29 October 2020 and seeks to change relevant parts of Section 14 of the CUSC to stabilise the expansion constant at the start of the RIIO-2 period. The expansion constant value used would, under this proposal, be the RIIO-1 value plus relevant inflation until such time as further changes are made.

The Proposer considers that this is an imminent issue that if not urgently addressed may cause a significant commercial impact on parties, consumers and other stakeholder(s). On 30 October 2020, CUSC Panel determined that this Modification Proposal should

[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.

The Office of Gas and Electricity Markets
10 South Colonnade, Canary Wharf, London, E14 4PZ **Tel** 020 7901 7000
www.ofgem.gov.uk

proceed directly to Code Administrator Consultation, and agreed to the timeline put forward by the Code Administrator on that basis. This resulted in a binary assessment of the proposal, without Workgroup Alternative CUSC Modifications. On 3 November 2020 we granted urgent status[3] to this CUSC Modification Proposal because we were satisfied that the progression of this modification proposal related to an imminent issue that if not urgently addressed may have caused a significant commercial impact on parties, consumers, or other stakeholder(s).

The Proposer expects this modification to have a positive impact on CUSC Applicable Charging Objectives (a), (c) and (e) and to be neutral against the remaining Objectives. In their view, this proposal would better facilitate competition by preventing significant and unexpected changes to parties' charges. They also believe that affording NGESO the time to conduct a review of the methodology underpinning the expansion constant would be better than the baseline in respect of reflecting developments in transmission businesses, by avoiding the implementation of charges that may not reflect such developments. The Proposer further considers this change to be a better facilitator of charging methodology efficiency as it affords time for a broader review and deeper understanding of that methodology.

CUSC Panel[4] recommendation

At the CUSC Panel meeting on 24 November the CUSC Panel unanimously considered that CMP353 would better facilitate the CUSC charging objectives and the Panel therefore recommended its approval.

Our decision

We have considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 25 November 2020. We have considered and taken into account the responses to the industry consultation on the modification proposal, which are attached to the FMR[5]. We have concluded that:

- implementation of the modification proposal will better facilitate the achievement of the Applicable Objectives of the CUSC;[6] and
- directing that the modification be made is consistent with our principal objective and statutory duties.[7]

Reasons for our decision

We consider this modification proposal will better facilitate CUSC charging objective (a) and has a neutral impact on CUSC charging objectives (b), (c) and (e).

The majority of respondents to the Code Administrator Consultation were supportive of implementation and stated that they believe the scale of the change to TNUoS tariffs was unexpected.

[3] https://www.ofgem.gov.uk/system/files/docs/2020/11/cmp353_-_authority_decision_on_urgency_0.pdf
[4] The CUSC Panel is established and constituted from time to time pursuant to and in accordance with section 8 of the CUSC.
[5] CUSC modification proposals, modification reports and representations can be viewed on NGESO's website at: https://www.nationalgrideso.com/industry-information/codes/connection-and-use-system-code-cusc/modifications
[6] 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
[7] 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.

The Office of Gas and Electricity Markets
10 South Colonnade, Canary Wharf, London, E14 4PZ **Tel** 020 7901 7000
www.ofgem.gov.uk

Such unexpected changes in charges are, in our view, detrimental to competition. Many generators and Suppliers use the published TNUoS forecasts for business planning purposes. For Generators, this can include decisions on repowering or plant closure, as well as future investments. We believe that when significant changes occur, without sufficient notice, and with varying distributional effects, there could be harm to competition because TNUoS-liable parties cannot respond to such changes in a timely manner.

We note that two respondents to the Code Administrator Consultation ("CAC") stated that stakeholders were aware that NGESO's TNUoS forecasts were using a 'placeholder' expansion constant value and that some change was therefore to be expected. Whilst we agree that industry were aware of the nature of the value included in NGESO's forecasts, we do not believe that an 83% uplift in the value of the expansion constant could have been foreseen by industry.

Stakeholders could have used the published models to test what tariffs would be under different expansion constant values. The data used to calculate the expansion constant is not publicly available, and as such, we do not believe that they could have forecast, with any degree of accuracy, the value that would actually apply. In practice, this means that stakeholders may have been wholly reliant on the forecasts NGESO published and could not have foreseen the significant increase in their charges.

(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

The vast majority of respondents to the Code Administrator Consultation stated that the proposal better facilitated Applicable Charging Objective (ACCO) (a) as, in their view, preventing, or mitigating the effect of, a significant and unexpected change in locational charges would support competition. Some respondents highlighted that while generators in some zones in England and Wales would see an increase in credits received, TNUoS charges will increase by approximately 60% in Scotland, creating what they believed was an inequity treatment for generators based on their location.

Our position

We agree that this CUSC Modification Proposal better facilitates competition than the baseline. Material and unpredicted changes in Generation TNUoS charges can undermine competition where there is significant variance in the effects between generators without objective justification, where generators could not have reasonably foreseen such changes.

Our starting position is that cost-reflectivity is beneficial to competition as users face charges that relate to their own commercial choices, for instance where to locate, or the type of technology of their generating plant. These signals should encourage users to make efficient decisions in future. Differences in charges between locations, or between technology types where it can be evidenced that they drive differing costs, are justifiable on cost-reflectivity grounds. We do not, however, consider that the wide range of charge variances resultant of the change to the expansion constant is necessarily cost-reflective, per NGESO's concerns regarding the inputs to the expansion constant methodology. We further believe that combined with the short notice provided to industry by NGESO of the tariffs that would apply in April 2021 without CMP353, the baseline methodology is detrimental to competition. We believe that this is compounded by the uncertainty as to the extent to which the methodology underpinning the calculation of the expansion constant reflects the appropriate TO investments.

The Office of Gas and Electricity Markets
10 South Colonnade, Canary Wharf, London, E14 4PZ **Tel** 020 7901 7000
www.ofgem.gov.uk

(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)

There were varying views from respondents on the impact CMP353 would have on cost reflectivity. One respondent to the Code Administrator Consultation was of the view that delaying the review of the expansion constant does not better facilitate ACCO (b) as they believe the tariffs will not be cost reflective for at least the next year. This view was echoed by one other respondent who also stated that in their view, this proposal suppresses the locational signal sent to network users. One respondent was concerned that the higher estimated RIIO-2 expansion constant did not truly reflect the current drivers of network investment and costs and using this increased figure to set 2021/22 TNUoS charges could result in tariffs that are not cost reflective. One respondent noted that NGESO stated in August 2020 that they had material reservations about the robustness of the data they have received to calculate RIIO-2 expansion constant and factors.

Our position

Having considered the views of the respondents, we believe that the proposal is likely to be neutral in regards to ACCO (b).

Whilst the new value of the expansion constant has been derived using the relevant project costs, we do not have sufficient evidence that the individual projects used in the calculation reflect the generality of transmission investments. We therefore cannot be confident that the resultant expansion constant value is reflective of the generality of costs of transporting 1MW over 1km.

NGESO has raised this proposal to afford them the time to determine whether the current methodology underpinning the expansion constant reflects the appropriate projects and asset costs. Given that it cannot be stated that the projected value of the expansion constant is cost-reflective, we consider this proposal overall to be neutral to ACCO (b).

(c) that, so far as is consistent with sub-paragraphs (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

Some respondents to the Code Administrator Consultation felt that the proposal, to the extent that it provides time to consider the propriety of the current expansion constant methodology, is positive against ACCO (c). We note, however, that one respondent stated that with more Price Control emphasis on non-network solutions, significant increases in the expansion constant and factors would be, in their view, likely to happen again in future.

Our position

We believe that CMP353 likely has a neutral impact on ACCO (c). The projected expansion constant reflects specific assets that have been built over the last ten years, which may not be reflective of typical transmission investments. Stabilising the expansion constant will allow for a review of the current methodology, to ensure that the

methodology underpinning the calculation of the expansion constant takes into account relevant data. As this proposal allows time for a review, whilst maintaining the RIIO-T1 value of the expansion constant, we believe it to be neutral to ACCO (c).

(e) promoting efficiency in the implementation and administration of the system charging methodology

The majority of respondents agreed that this proposal better facilitates the achievement of ACCO (e). One of the respondents highlighted that a review of the methodology carried out between now and the new price control period in April 2021 would most likely result in inefficient outcomes. Another respondent believed that stabilising the expansion constant and factors until the methodology is reviewed will result in an improved efficiency and understanding of the charging methodology. One respondent also noted that the legal text does not specify a time to revert to the baseline methodology if no other solution is found.

Our position

To the extent that CMP353 is a temporary solution to an underlying concern about the charging methodology, we understand the argument that it may be less efficient than the baseline in the short term. We believe that taking the time to re-evaluate this element of the methodology to ensure it is fit for purpose should improve efficiency in the long term and that this proposal effectively minimises the costs incurred by industry during that review. We therefore consider this proposal to be overall positive against ACCO (e).

We do, however agree that NGESO have not specified how long they intend the solution to last, and that such information is important for industry in understanding their future liabilities. We note that as the data underpinning the calculation of the expansion constant is not publicly available, TNUoS-liable parties are not able to forecast the expansion constant value that might apply.

We expect NGESO to share a detailed plan with us, by 31 January 2021, outlining the timescales and scope of their review of the expansion constant methodology, including the effects on rezoning as outlined in our recent decision to approve WACM2 of CMP325. We would like to understand the extent to which this review will feature as part of CMP315[8] (a CUSC Modification Proposal which seeks to review the assets included in the calculation of the expansion constant), or whether it will be undertaken separately to that proposal. We would also like to understand whether – and how - transparency in the processes underpinning the expansion constant calculation could be improved.

Decision not to conduct an Impact Assessment

In our letter regarding urgency on 3 November 2020, we decided that the modification should be treated as an Urgent CUSC Modification Proposal. In that letter, we noted that '[w]e are satisfied that the progression of this modification proposal is related to "a current issue that if not urgently addressed may cause a significant commercial impact on parties, consumers, or other stakeholders(s)".

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

[8] https://www.nationalgrideso.com/document/142656/download

The Office of Gas and Electricity Markets
10 South Colonnade, Canary Wharf, London, E14 4PZ **Tel** 020 7901 7000
www.ofgem.gov.uk

with the … generation, transmission, distribution or supply of electricity." Where this applies, the Authority is obliged to carry out an impact assessment.

The Authority has not found it necessary to reach a decision on the implications of the reasons set out in our letter for the application of its Section 5A duty. This is because of the exceptions to this duty. These apply if it appears to the Authority that the urgency of the matter makes it impracticable or inappropriate for the Authority to comply with the Section 5A duty.

The Authority considers it is both impracticable and inappropriate to conduct an Impact Assessment under our Section 5A duty for this decision. The timeline for decision proposed in the FMR does not allow for a full Impact Assessment, but in any event, the proposal seeks to prevent TNUoS-liable parties from being exposed to significant fluctuations in their charges stemming from the 83% increase in the expansion constant, in the immediate term. Our decision will provide market participants with more stable charges whilst a broader review is conducted. We have noted the TNUoS tariffs provided by NGESO in their proposal and consider that these provide sufficient information to make a decision without further analysis. Therefore, we believe that conducting an Impact Assessment in this instance would serve no useful purpose.

Decision notice

In accordance with Standard Condition C10 of the Transmission Licence, the Authority, hereby directs that modification proposal CMP353: *Stabilising the Expansion Constant and non-specific Onshore Expansion Factors from 1st April 2021* be made.

Andrew Self
Deputy Director, Electricity Network Charging & Access
Energy Systems Management and Security
Signed on behalf of the Authority and authorised for that purpose

The Office of Gas and Electricity Markets
10 South Colonnade, Canary Wharf, London, E14 4PZ **Tel** 020 7901 7000
www.ofgem.gov.uk