Guidance

The Electricity System Operator Reporting and Incentives Arrangements: Guidance Document (draft for consultation)

Publication date:	30 November 2022	**Team:**	ESO Regulation
		Tel:	020 7901 7000
		Email:	ESOPerformance@ofgem.gov.uk

The Electricity System Operator (ESO) sits at the centre of our electricity system and undertakes a number of different roles. We regulate the ESO to help ensure its actions align with consumers' interests. The ESO Reporting and Incentives (ESORI) Arrangements aim to create transparency around the ESO's performance and make it clearly accountable to its stakeholders. The arrangements are designed to encourage the ESO to make improvements to the way it performs its roles in order to maximise benefits for current and future consumers.

This Guidance Document for the ESORI Arrangements outlines the process and criteria for assessing the performance of the ESO; the reporting requirements placed on the ESO; and the methodology the Authority will use to determine an incentive reward or penalty each business plan cycle.

This ESORI Guidance Document (version 6.0) will come into effect on 1 April 2023 as part of the ESO's RIIO-2 price control. It will apply to the regulatory years 2023-25.

Version History

Version	Changes	Purpose	Publication date	Release date
0.1	n/a	Consultation on the 'ESO Reporting and Incentives Arrangements Guidance Document – Draft Version'	23 February 2018	n/a
1	Clarifications to wording and minor issues addressed following review of consultation responses	To issue the ESO Reporting and Incentives Arrangements Guidance Document	28 March 2018	1 April 2018
2	Clarifications and changes to the evaluation process for regulatory year 2019-20, following consultation with industry	To update and revise the ESO Reporting and Incentives Arrangements Guidance Document for 2019-20	25 March 2019	1 April 2019
3	Clarifications and changes to roles and evaluation criteria for regulatory year 2020-21, following consultation with industry	To update and revise the ESO Reporting and Incentives Arrangements Guidance Document for 2020-21	6 March 2020	1 April 2020
4	Clarifications and changes to align with the regulatory framework for the RIIO-2 price control	To update and revise the ESO Reporting and Incentives Arrangements Guidance Document for 2021-23	17 March 2021	1 April 2021
5	Clarifications and changes to the methodology of metric 1D	To correct the methodology of metric 1D	1 July 2021	1 April 2021
6	Correction to metric 2C EMR decision quality	To align metric 2C EMR decision quality with our Final Determination position	11 March 2022	1 April 2021
7	Clarifications and changes to align with the ESO's second business plan period in the RIIO-2 price control	To update and revise the ESO Reporting and Incentives arrangements Guidance Document for 2023-205	XX	1 April 2023

Contents

1. Introduction

1.1. This chapter sets out the background to the ESO Reporting and Incentives (ESORI) Arrangements, the purpose of this Guidance Document, and its status from a compliance perspective.

1.2. The ESORI Arrangements have been revised to complement the regulatory arrangements for the ESO under the RIIO-2 price control. This Guidance Document provides guidance around the processes and requirements involved in the ESORI Arrangements. In particular, it explains the processes and criteria used to assess the ESO's performance; the reporting requirements placed on the ESO; and the methodology the Authority will use to determine an incentive reward or penalty for each business plan cycle[1].

1.3. The ESORI Arrangements Guidance Document is issued by the Authority under Part C of Special Condition 4.3 (Electricity System Operator Reporting and Incentives Arrangements) of the ESO's licence. As set out in Special Condition 4.3.16, the Authority may make appropriate provision about or impose requirements in the ESORI Arrangements Guidance Document, which may include, but will not be limited to:

(a) the criteria against which the performance of the licensee will be assessed;

(b) the process that will be in place for assessing the performance of the licensee, including the role of the ESO Performance Panel in this process;

(c) the requirements the licensee must fulfil as part of the assessment process, including the information the licensee must provide and its attendance at ESO Performance Panel meetings;

(d) the information used for the performance assessment, including how the Business Plan and reporting during the business plan cycle will be used in that evaluation;

[1] The business plan cycle is the period for which the business plan is applicable. The first business plan cycle (BP1) covers the incentive scheme starting on 1 April 2021 and ending on 31 March 2023. The second business plan cycle (BP2) covers the incentive scheme starting on 1 April 2023 and ending on 31 March 2025.

(e) how the assessment of the performance of the licensee will be used by the Authority to determine ESORIt; and

(f) any other matters relating to the regulation, governance, or administration of the ESORI Arrangements.

1.4. This document may be revised and reissued in accordance with Part C of Special Condition 4.3.

1.5. Any subsequent material updates to this Guidance Document will be made following consultation with the impacted parties, including the ESO. As a key principle, any changes made within an incentive scheme, which materially change the way the ESO's performance is assessed, would not apply until the next scheme (unless there is agreement that a change is necessary, for example, to correct an error or to improve a process).

Compliance

1.6. Where provisions of this Guidance Document require the compliance of the licensee, the licensee must comply with those provisions as if the Guidance Document were part of Special Condition 4.3. However, we have also attempted to make this document accessible and informative to a range of stakeholders.

1.7. For the avoidance of doubt, this document is subordinate to the licence. This document does not change any definition or obligations contained within the licence and in the event of any ambiguity over the Guidance Document, the licence will take precedence.

1.8. The contents of this Guidance Document do not alter or supplement the ESO's compliance with its wider obligations under legislation, its licence or industry codes. References to 'baseline expectations' within this document are for the purposes of the ESORI Arrangements only.

2. The ESORI Arrangements process

This chapter provides an overview of the ESORI Arrangements. It provides guidance on the steps, processes and timings involved in the regulatory cycle.

Overview of the ESORI Arrangements

2.1. Our regulatory approach requires upfront clarity around the behaviours we expect of the ESO and places the onus on the ESO to engage with stakeholders to identify how to best meet and exceed these expectations in order to maximise benefits for consumers.

The ESO roles framework

2.2. Underpinning the ESO's regulatory framework is our ESO Roles Guidance (the 'Roles Guidance')[2]. The Roles Guidance is the key guide for understanding our performance expectations and forms a key point of reference for the ESORI Arrangements. The Roles Guidance sets out our expectations and how the ESO can exceed our expectations for each of its activities. It explains our expectations of how the ESO should best fulfil its licence obligations and is designed to align expectations between the ESO, the ESO's customers and stakeholders, Ofgem, and the ESO Performance Panel (the 'Performance Panel')[3].

2.3. The Roles Guidance also helps set the parameters for the ESO's Business Plan and the evaluation process. The three roles and associated activities are shown in Table 1.

Table 1: Summary of the ESO's roles and activities

Role	Role activity
Role 1: Control centre operations	a) System operation
	b) System restoration
	c) Information, data, and forecasting
	a) Market design

[2] The ESO Roles Guidance 2023-25 is published alongside this document.
[3] The Performance Panel is an independent panel of experts and/or stakeholder representatives, who will assess the ESO's performance and provide recommendations to the Authority.

Role 2: Market development and transactions	b) EMR
	c) Industry codes and charging
Role 3: System insight, planning and network development	a) Connections and network access
	b) Operational strategy and insight
	c) Optimal network investment

2.4. The ESO roles are outlined in more detail in our Roles Guidance published on our website. An updated version of the Roles Guidance will be published alongside this Guidance Document and will come into effect from 1 April 2023.

2.5. The ESO's performance will be evaluated per role using the evaluation process described in Chapter 3 of this Guidance Document.

The ESORI Arrangements

2.6. Under the ESORI Arrangements, the ESO must engage with its stakeholders and publish a Business Plan before the start of each business plan cycle. The Business Plan should outline the details of the ESO's costs, activities, and deliverables for delivering its strategy over two years of the RIIO-2 period[4]. The ESO will then report on its performance throughout the business plan cycle and at the end of the business plan cycle.

2.7. The Performance Panel will have a role in reviewing the ESO's Business Plan, challenging its within-scheme performance and performing an End of Scheme evaluation. The Performance Panel's performance evaluation will form a recommendation to the Authority, who will review all evidence available in order to determine a financial penalty or reward for the ESO for the relevant business plan cycle. When the ESO clearly demonstrates that its performance against the evaluation criteria has gone beyond 'baseline expectations', then this should be reflected in an incentive reward. Equally, where the ESO has clearly failed to demonstrate that it has taken the necessary actions against the evaluation criteria to meet baseline expectations, then this should result in an incentive penalty (further details can be found in Chapter 3).

[4] RIIO-2 covers the period starting 1 April 2021 and ending on 31 March 2026.

2.8. In summary, the ESORI Arrangements comprise of:

- A requirement on the ESO to engage with stakeholders in order to produce a Business Plan before the start of each business plan cycle. This should set out the details of the ESO's costs, activities, and deliverables during the business plan cycle to deliver its medium-term strategy across the RIIO-2 period and long-term vision for the energy system;

- Requirements on the ESO to produce within-scheme performance reports, including monthly reports, quarterly reports, six-monthly reports, a Mid-Scheme Report and an End of Scheme Report;

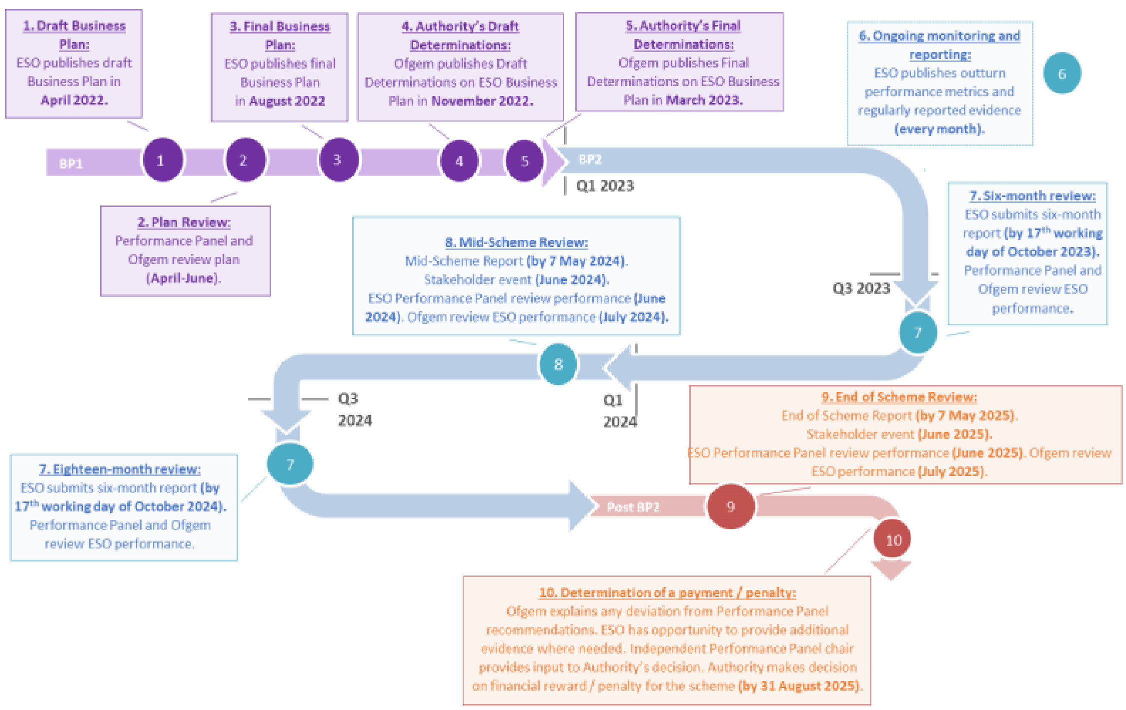
- The Performance Panel, formed of independent experts and/or stakeholder representatives with an independent chair, who will be responsible for reviewing the ESO's Business Plan and evaluating its performance based on clear ex-ante evaluation criteria;

- An 'evaluative' financial incentive, where the Authority will make a decision on a reward or penalty for the ESO at the end of the business plan cycle. This will be informed by the recommendation from the Performance Panel and be based on an ex-ante reward / penalty methodology.

Stages in the annual ESORI Arrangements cycle

2.9. Figure 1 provides an overview of the key stages and timings in the reporting and incentives process for the ESO's second business plan cycle (BP2). We provide guidance on each of these stages in the sections below.

Figure 1: Regulatory process for BP2 business plan cycle



Steps 1 to 5: The ESO Business Plan

2.10. The ESO must engage with its stakeholders to produce a Business Plan before the start of each business plan cycle. We provided further guidance on the process for developing the Business Plan, including the updated delivery schedule and the content required for BP2 in our Business Plan Guidance Document[5]. This included the following steps:

Step 1) The draft Business Plan: the ESO must engage with stakeholders to produce a draft version of its Business Plan, which includes the delivery schedule, and undertake a consultation on its contents.

Step 2) The Plan Review: as part of the consultation, the ESO Performance Panel will review the draft Business Plan and share feedback.

[5] ESO Business Plan: Guidance document: https://www.ofgem.gov.uk/sites/default/files/2021-11/Business%20Plan%20Guidance%20document%20final%20v3.pdf

Step 3) The final Business Plan: the ESO shall consider all stakeholders' responses to its consultation and then publish a final version of its Business Plan.

Step 4) The Authority's Draft Determinations: we will consult on our Draft Determinations on the final Business Plan, which shall include our grading of the ESO's delivery schedule; our proposals for a value for money assessment[6]; and key performance measures.

Step 5) The Authority's Final Determinations: following the consultation we will publish our Final Determinations, which shall include our final grading of the ESO's delivery schedule; our value for money assessment; and key performance measures.

Revisions to the Business Plan

2.11. We expect the ESO to remain flexible and adaptable throughout the business plan cycle and respond to changing situations. The ESO may deviate from the final published plan where it identifies opportunities for greater consumer benefits. Equally, if an action in the plan turns out not to be in consumers' best interests, then the ESO should change its approach and explain why.

2.12. Whilst the Business Plan document will not be revised once published (with the exception of the updates to the delivery schedule and/or costs described in Chapter 5), we expect any changing context and changes from the plan to be explained through the reporting throughout the rest of the business plan cycle. Any material changes to the deliverables during the year should be added clearly via an addendum to the Business Plan or within-scheme reports.[7]

Steps 6 to 8: Within-scheme monitoring and reporting

Step 6) Ongoing monitoring and reporting

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[6] For BP1 Ofgem set a cost benchmark. For BP2, Ofgem will undertake an ex-ante value for money assessment.
[7] Further details can be found in Chapter 7 of our RIIO-2 Final Determinations – Electricity System Operator Annex: https://www.ofgem.gov.uk/publications-and-updates/riio-2-final-determinations-transmission-and-gas-distribution-network-companies-and-electricity-system-operator

2.13. In order to create transparency around the ESO's performance throughout the business plan cycle, and to help stakeholders, the Performance Panel and Ofgem monitor the ESO's progress against its Business Plan, the ESO must publish on its website:

- Monthly updates of its performance (by the 17th working day of the following month)
- Quarterly updates (every 3 months) of its performance (by the 17th working day of the following month)

2.14. The ESO will also meet with Ofgem on a monthly basis to discuss the contents of these performance reports.

2.15. Further guidance is provided in Chapter 5 on the detailed reporting requirements during BP2.

Step 7) The six-month and eighteen-month review

2.16. The ESO will be required to publish a report at six months and eighteen months into the scheme, by the 17th working day of October in each year of the scheme.

2.17. The Performance Panel will give targeted feedback of the ESO's performance both at the six- and eighteen-month review stages. This will include views on what the ESO must do to improve their scores by the end of the business plan cycle. Ofgem will also communicate its view on the ESO's performance and provide a broad trajectory of performance every six months. The review undertaken by Ofgem and The Panel at these stages is intended to be an indication of progress. The Panel and Ofgem's views will be published on Ofgem's website.

2.18. We will not hold a formal stakeholder event every six-months or issue a call for evidence at this stage but will continue to engage widely with stakeholders throughout the incentive scheme.

2.19. Further guidance is provided in Chapter 5 on the reporting requirements for the business plan cycle reports.

Step 8) The Mid-Scheme Review

2.20. The ESO is required to produce and publish a report covering its performance during the first year of the business plan cycle, known as the Mid-Scheme Report, by 7 May in the second year of the business plan cycle.

2.21. Following a review period of at least two weeks (depending on the views expressed and evidence presented), the ESO will then be required to attend a meeting to present the evidence contained in the Mid-Scheme Report to stakeholders and the Performance Panel. This meeting will be arranged in June in the second year of the business plan cycle, four weeks after the Mid-Scheme Report is published.

2.22. For the avoidance of doubt, the Mid-Scheme Report removes the need for a six-monthly report at the end of the second quarter of the business plan cycle.

2.23. Following this meeting, the Performance Panel will consider the evidence and perform a full evaluation, providing scores of the ESO's performance mid-way through the business plan cycle. The Performance Panel will record its conclusions in a short summary report. This should include views on what the ESO needs to do to improve scores. Ofgem will also communicate its view on the ESO's performance and expectations for the ESO's two-year financial incentive outcome. As part of this review, Ofgem will undertake a reassessment of the ESO's IT investments to produce an updated Red-Amber-Green (RAG) rating based on the additional information submitted. The Panel and Ofgem's views will be published on Ofgem's website.

Steps 9 to 10: Final performance evaluation

Step 9) The End of Scheme Review

2.24. By 7 May in the year after the business plan cycle, the ESO will publish on its website, a report containing final evidence of its performance over the entire regulatory incentive scheme, known as the End of Scheme Report.

2.25. There will then be a review period of four weeks for stakeholders, the Performance Panel and Ofgem to review the final evidence. During this time, the Performance Panel and Ofgem may seek further clarifications from the ESO around its End of Scheme Report (for example, if there are any unclear or ambiguous points). The ESO should respond to these questions promptly and in line with the general guidance in Chapter 5.

2.26. Following this review period, the ESO will be required to attend a meeting to present the evidence contained in the End of Scheme Report to stakeholders and the Performance Panel. This meeting will be arranged by Ofgem for a date likely in the first week of June following the end of the incentive scheme.

2.27. The Performance Panel will consider all evidence presented and score the ESO's performance against each role, in line with the evaluation criteria in Chapter 3. We expect this to be a single score for each role to represent the majority views given by the Performance Panel members. Any notable differences between the members' scoring will be reflected in the commentary of the Performance Panel's performance reports and taken into account in our decisions. This report will be published on the Ofgem website.

2.28. Following the publication of the Performance Panel's recommendations, stakeholders including the ESO will have two weeks to submit any further representations regarding the Performance Panel's report. The Authority will consider the evidence available before reaching a final decision on the incentive reward or penalty.

Steps 10) Determination of a reward / penalty

2.29. The Authority will consider the Performance Panel's recommendations, as well as any other evidence received or collected, and decide on an appropriate reward or penalty for the ESO. The chair of the Performance Panel will provide input to, and be engaged in, the Authority's decision, though will not be party to the decision itself. The financial outcome will be calculated in accordance with the process described in Chapter 4. For the avoidance of doubt, the final decision will lie with the Authority who will form views based on the evidence available, including the Performance Panel's recommendation.

2.30. In advance of the Authority's decision being finalised, Ofgem will provide the ESO with an explanation of where it plans to deviate from the Performance Panel's scores, giving the ESO an opportunity to provide additional evidence of its performance where needed.

2.31. The Authority will produce its final decision on the incentive reward or penalty by 31 August in the year after the business plan cycle, or such later date that it considers appropriate. This decision will be published on the Ofgem website.

3. ESO performance evaluation criteria

The purpose of this chapter is to set out guidance for how the Performance Panel should evaluate the ESO's performance.

Setting performance expectations

3.1. The evaluation's scoring approach is based on an understanding of performance expectations for the ESO. For the purposes of the ESORI Arrangements, meeting our expectations equates to a level of performance expected from the ESO which would merit neither an incentive penalty nor an incentive reward.

3.2. The Roles Guidance is an overarching guide for understanding our performance expectations and forms a key point of reference for the ESORI Arrangements. The Roles Guidance sets out our expectations, and how the ESO can exceed our expectations, for each of its activities. It is designed to align expectations between the ESO, the ESO's customers and stakeholders, Ofgem, and the Performance Panel.

3.3. Ofgem's Final Determinations also provide clear, ex-ante performance expectations[8] through:

- Plan grading – Ofgem graded the delivery schedule for each role, with an explicit grading that aligns with the evaluation scoring for each role. This provides the ESO with an ex-ante expectation of our assessment of plan delivery if these deliverables are met. Where we considered the delivery schedule not sufficiently ambitious, we highlighted this to set a clear reference point and align expectations in the incentive process.

- Setting performance measures – Ofgem set all performance measures (including performance metrics, stakeholder satisfaction surveys and other reported evidence).

[8] Further details can be found in Chapter 3, Appendix 2 and Appendix 3 of our Business Plan 2 Draft Determinations – Electricity System Operator: published alongside this document.

We also set the performance benchmarks for performance metrics to give the ESO clarity on the level of performance that will meet or exceed our expectations.

- A value for money assessment – Ofgem assessed the ESO's proposed internal costs against our cost expectations and set up-front grading for each role based on the requested funding. This grading provides the ESO with an ex-ante expectation of our assessment of value for money based on the current information available. Where we considered costs to not meet our expectations, we highlighted this and the details of our concerns to set a clear reference point and align expectations in the incentive process.

3.4. In general, performance to date will be considered when setting baseline expectations for future performance. In compiling our Final Determinations, Ofgem reviewed previous Business Plan reports and performance to ensure continuity between the different business planning cycles.

3.5. For the avoidance of doubt, we expect innovation to be a core part of the ESO's business-as-usual activities and for this to be demonstrated through the ESO's planned deliverables. Undertaking innovation projects, whether funded through the ESO's main price control totex or through dedicated innovation funding, does not automatically qualify as exceeding expectations. The ESO's delivery of outputs and outcomes as part of innovation-funded projects will be considered as part of the performance evaluation. However, we have excluded innovation-funded projects from the cost benchmarks because these costs are funded through a separate Use it or Lose It (UIOLI) funding mechanism, reflecting the lower technological readiness of these projects.

Performance evaluation criteria

3.6. The Performance Panel will use five key inputs for all roles to evaluate the ESO's performance.

3.7. In determining a score for each role, the key criteria the Performance Panel should take into account are:

a) Plan delivery;

b) Metric performance;

c) Stakeholder evidence;

d) Quality of outputs; and

e) Value for money.

3.8. These criteria are designed to be considered together to establish an overall picture of the ESO's performance for each role. Below is the guidance the Performance Panel should consider to determine the ESO's performance in relation to each of the criteria.

a) Plan delivery

3.9. The Performance Panel should consider whether the delivery schedule has been successfully delivered on time and/or whether the ESO has delivered additional outputs in line with the expectations in our Roles Guidance. The Performance Panel should refer to Ofgem's Final Determinations, which grade the ESO's two-year delivery schedule to indicate the link more clearly between on track plan delivery and performance assessment.

3.10. The Performance Panel should consider where the ESO can clearly explain why a plan deviation was in consumers' interest or outside of its control. In addition, where the ESO has not produced an 'exceeding' delivery schedule (i.e. a delivery schedule graded as a 4 or 5), the Performance Panel should consider whether the ESO has demonstrated additional activities that would exceed expectations.

3.11. The Performance Panel should consider that the ESO has *outperformed this criterion* if the ESO has successfully delivered the key components of a 4- or 5-graded delivery schedule. Alternatively, the ESO could outperform this criterion if the ESO has outperformed a delivery schedule graded as a 3 or lower through delivering additional activities and outcomes that demonstrate the exceeding expectations guidance in our Roles Guidance. This may include the ESO clearly explaining the reasons why any major changes to the original delivery schedule timelines were in consumers' interest or outside of its control.

3.12. The Performance Panel should consider that the ESO has *underperformed this criterion* if the ESO has failed to deliver the key components of a 3-graded delivery schedule (or delivered only the key components of a 1- or 2-graded delivery schedule) and failed to successfully deliver additional activities that demonstrate the meeting expectations guidance in our Roles Guidance. This may include the ESO not clearly explaining the reasons why any major changes to the original delivery schedule timelines were in consumers' interest or outside of its control.

b) Metric performance

3.13. The Performance Panel should consider the ESO's outturn performance against the performance metrics and the ESO's reasons for this outturn performance. The numerical quantifications related to the metrics should be considered with the supporting explanations provided by the ESO of the actions it has taken to achieve the outturn performance. The Performance Panel should also consider any wider factors outside of the ESO's control that could have impacted the performance metric (such as weather, market trends, policy etc).

3.14. The Performance Panel should consider the ESO has *outperformed this criterion* if the ESO has exceeded expectations for the majority of its performance metrics and the ESO has demonstrated that its actions have driven positive outturn metric performance. Alternatively, the ESO may have significantly outperformed a certain metric that is particularly stretching or has high associated consumer value or the ESO may have provided strong, convincing justifications for any metrics where performance has not exceeded expectations.

3.15. The Performance Panel should consider the ESO has *underperformed this criterion* if the ESO has performed below expectations for the majority of metrics, and there are no strong reasons or mitigating circumstances for this. Alternatively, the ESO may have significantly underperformed a particular metric that has high associated consumer costs; or the panel may be unconvinced that the supporting explanations provided by the ESO demonstrate that its actions have driven positive outturn metric performance.

c) Stakeholder evidence

3.16. The Performance Panel should consider stakeholders' satisfaction on the quality of the ESO's plan delivery. This will include the results of the stakeholder satisfaction survey, views provided by stakeholders during the Mid-Scheme Review and End of Scheme Review processes, or any of the ESO's consultations or ad hoc surveys throughout the year. Ofgem may also provide the Performance Panel with any stakeholder views it has collected throughout the year. For example, through ongoing monitoring or consultations. The Performance Panel should consider the ESO's explanations for feedback received.

3.17. The Performance Panel should consider the ESO has *outperformed this criterion* if the 'exceeds expectations' category is the most common response category in the stakeholder satisfaction survey and/or there is a broad consensus[9] amongst stakeholders that the ESO has exceeded expectations for that role. The Performance Panel should also consider the ESO has outperformed this criterion if the 'meets expectactions' category is the most common response category in the stakeholder satisfaction survey, however, the 'exceeds expectations' category significantly outweighs the 'below expectactions' category amongst stakeholders. The panel should consider whether the ESO has provided sufficient justification and explanation of any negative stakeholder feedback. In addition, outperformance may be demonstrated if there is evidence that the ESO has actively sought and taken into account the feedback of stakeholders throughout the business plan cycle.

3.18. The Performance Panel should consider the ESO has *underperformed this criterion* if the 'below expectations' category is the most common response category in the stakeholder satisfaction survey and/or there is a broad consensus amongst stakeholders that the ESO has performed below expectations for that role and the ESO cannot provide satisfactory reasons for why this is the case. The Performance Panel should also consider the ESO has underperformed this criterion if the 'meets expectations' category is the most common response category in the stakeholder satisfaction survey, however, the 'below expectations' category significantly outweighs the 'exceeds expectations' category amongst stakeholders. In addition, underperformance may be demonstrated if there is evidence that the ESO has not actively sought and taken into account the feedback of stakeholders throughout the business planning cycle.

d) Quality of outputs

3.19. The Performance Panel should consider the actual benefits the ESO has realised from delivering its Business Plan (or any outputs additional to the Business Plan), considering the quality of the outcomes and outputs actually delivered. This should place particular focus on outputs where the quality of delivery is not measured through performance metrics (criterion b)) or stakeholder satisfaction (criterion c)). In particular, the Performance Panel should consider the ESO's regularly reported evidence and its six-monthly reporting against the

[9] 'Broad consensus' does not mean there needs to be complete unanimity and agreement amongst stakeholders about the ESO's performance. The Performance Panel should consider carefully whether the stakeholder feedback could be influenced by the particular interests of the party providing the feedback.

delivery schedule for each of its activities outlined in the original Business Plan cost benefit analysis (CBA). Where the benefits from CBAs cannot be clearly evidenced during the incentive scheme, the Performance Panel should explicitly consider 'how' the ESO has delivered its Business Plan in line with the expectations in our Roles Guidance.

3.20. The Performance Panel should consider both delivered outputs that produce benefits within the business plan cycle and delivered outputs that are expected to produce benefits in future periods. The Performance Panel should consider whether the ESO has taken concrete steps to progress its longer-term vision and medium-term strategy. For example, this may include considering whether the ESO's interim deliverables have taken account of the energy system's evolving characteristics and/or whether the ESO has adapted its activities flexibly to ensure deliverables have been delivered in a way that maximises benefits. The ESO could demonstrate this through explaining the rationale for adaptations and providing evidence of greater benefits that result from adaptations.

3.21. The Performance Panel should consider the ESO has *outperformed this criterion* if the ESO's reported evidence supports the realisation of the Business Plan's intended and identified benefits in most areas (for example, the regularly reported evidence shows a clear improvement in outcomes, in line with the ESO's medium-term strategy). This may include the ESO demonstrating that the actual outputs produced as part of an ambitious (ie 4- or 5-graded) delivery schedule deliver the ESO's outlined success measures and directly achieve the intended benefits as outlined in the original Business Plan CBA. The Performance Panel should also consider the ESO has outperformed this criterion if it produces outputs that demonstrate most or all the 'exceeds expectations' guidance in our Roles Guidance. Alternatively, the ESO may outperform this criterion if the ESO has produced additional outputs that clearly seek to maximise benefits for consumers. This may include the ESO quickly and proactively identifying changes to existing plans and course-correcting where needed.

3.22. The Performance Panel should consider the ESO has *underperformed this criterion* if the ESO's reported evidence does not support the realisation of the Business Plan's intended and identified benefits in most areas (for example, the regularly reported evidence does not show any improvement in outcomes). This may include the ESO failing to demonstrate that the actual outputs produced as part of a delivery schedule are of sufficient quality to achieve their intended benefits as outlined in the original Business Plan CBA. The Performance Panel should also consider the ESO has underperformed this criterion if it does not produce outputs that demonstrate the meets expectations guidance in our Roles Guidance. The ESO may also have underperformed this criterion if it has not delivered necessary additional outputs that seek to maximise benefits for consumers. This may include the ESO not identifying necessary changes to its original plan and course correcting when this is clearly needed.

e) Value for money

3.23. The Performance Panel should consider whether the ESO has delivered value for money, striking the optimal balance between maximising benefit delivered from outputs whilst minimising costs.

3.24. Our value for money assessment will represent Ofgem's view on the fair, value for money score for delivering the ESO's planned outputs at the proposed costs. Value for money is considered in the round, taking the other criteria into account and weighing them against the costs incurred by the ESO.

3.25. For all investments and business activities within a role, we consider value for money to include but not be limited to consideration of the following criteria:

- Business Suitability – spend is necessary and has been appropriately prioritised against other activities;
- Resilience and adaptability – future uncertainty has been appropriately considered;
- Ongoing efficiency – value is managed throughout the life of the work; and
- Governance, including delivery and management of risk – spend is controlled, risks are managed and robust oversight and accountability is maintained.

3.26. Specific technical criteria may also be considered where appropriate, for example for IT investments it may be suitable to consider aspects such as the foundational capability of those investments.

3.27. We will not automatically deem any overspend or underspend against the Business Plan forecasts as demonstration of poor or good value for money. Value for money will be assessed in conjunction with our assessment of the ESO's outturn delivery of its outputs.

3.28. The Performance Panel should consider that the ESO has *outperformed this criterion* if it can demonstrate that the criteria above have been met to a high standard and can evidence that best practice is being followed, using robust external validation to verify and drive improvement.

3.29. For IT Investments, this includes taking actions to address the concerns Ofgem has raised with particular investments. The ESO must demonstrate that the actions it has taken in line with the criteria.

3.30. The Performance Panel should consider that the ESO has underperformed this criterion if the ESO has failed to demonstrate that one or more of the criteria above have been met to standard levels of industry good practice.

Overall scoring for each role

3.31. The Performance Panel should assess the ESO's overall performance for each role. The Performance Panel should consider: all the performance measures and relevant reporting associated with the criteria, the grading applied to the delivery schedule as part of Ofgem's Determinations on the Business Plan, and the expectations in the Roles Guidance.

3.32. There is no explicit weighting associated with the evaluation criteria for each role. Instead, the criteria are the key aspects the Performance Panel should consider when carrying out an *overall* assessment of ESO performance for each role, recognising that there will be a degree of overlap between the criteria in practice. The criteria should be considered holistically to assess the ESO's performance. Ofgem and the Performance Panel will have discretion to consider areas of significant out- or underperformance when forming an overall view.

3.33. For each of the roles, the Performance Panel should score the ESO's overall performance on a scale of 1 to 5, where:

1 = Overall performance clearly does not meet performance expectations, for example the ESO has strongly underperformed most criteria

2 = Mixed overall performance and on balance the ESO mostly did not meet expectations, for example the ESO has net underperformance across the criteria

3 = Mixed overall performance and on balance the ESO mostly met expectations, for example underperformance and outperformance across the criteria balance each other out

4 = Mixed overall performance and on balance the ESO mostly exceeded expectations, for example the ESO has net outperformance across the criteria

5 = Overall performance clearly exceeds performance expectations, for example the ESO has strongly outperformed most criteria

3.34. There may be instances where the Performance Panel must consider evidence of competing positive and negative areas of performance within a role. In such cases the Performance Panel should use its expertise and informed judgement to evaluate where the overall balance of performance lies. For example, this may include consideration of the level of confidence in the reasons provided by the ESO for its outturn performance levels (e.g. how robust a certain mitigating factor is) or whether specific areas of out- or underperformance are more consequential for consumers than others.

3.35. In recommending a score, the Performance Panel should be mindful that these scores form the basis of a recommendation to the Authority on the level of incentive penalty or reward. The Performance Panel should record and explain its reasons for the scores it assigns for the ESO against each role and record its rationale in a report, as set out in Chapter 2. Although the Performance Panel is responsible for providing a recommended score of 1-5 for each role, it may wish to indicate within its report when a certain score was clear-cut or whether there was a close call between scores. This may be done through noting whether a specific score was ‘low’ or ‘high’. For example, the Performance Panel may wish to signal a ‘high 4’ score when the ESO has, on balance, exceeded expectations but outperformance is not quite considered strong enough to merit a score of 5. If the Performance Panel indicates that a specific score is ‘low’ or ‘high’, this will be considered by the Authority in its determination of an incentive reward / penalty.

4. Methodology for determining an incentive reward / penalty

This chapter describes how the Authority will determine an incentive reward / penalty for the ESO for a particular business plan cycle.

Determination of an incentive reward or penalty

Total incentive value

4.1. The maximum reward the ESO can achieve for BP2 is £30m and the maximum penalty is -£12m. These figures are the totals across BP2. As a default, this will be split equally among each of the three roles (+£10m upside and -£4m downside per role), as shown in Table 2.

Table 2: Financial incentive parameters for 2023-25

Role	Role 1 – Control centre operations	Role 2 – Market development and transactions	Role 3 – System insight, planning and network development
Role incentive range	+£10m to -£4m	+£10m to -£4m	+£10m to -£4m

4.2. We expect there to be a three-step process for determining the overall reward or penalty:

- Step 1) Authority review of scoring
- Step 2) Calculation of a default reward / penalty and incentive range
- Step 3) The adjustment process

Step 1) Authority review of scoring

4.3. The Authority will review the recommendation made by the Performance Panel, alongside any other evidence submitted. The chair of the Performance Panel will also provide input to, and be engaged in, the Authority's decision, though will not be party to the decision itself.

4.4. This scoring review will also consider the grading of the ESO's delivery schedule as part of Ofgem's Final Determinations and the Roles Guidance.

4.5. If there is a significant deviation between Ofgem's delivery schedule grading and the Performance Panel's report, then the Authority may consider whether this is justified by the ESO's outturn performance, evidence collected throughout the business plan cycle and any changing situations or context.

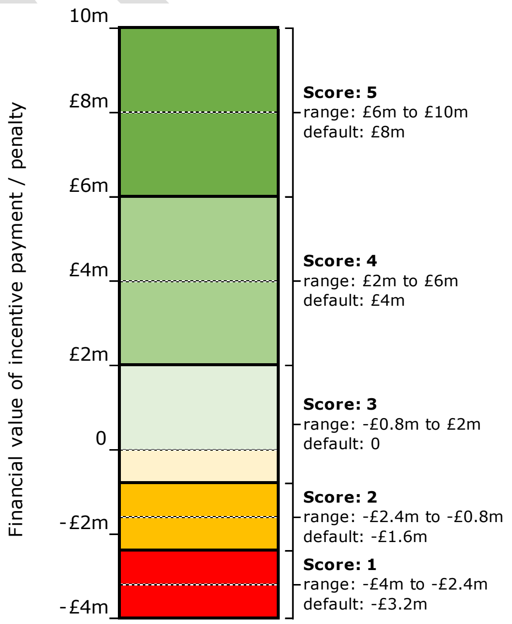
4.6. The Authority will inform the ESO of where it intends to deviate from the Performance Panel's scores. The ESO will then have an opportunity to provide additional evidence of its performance in these areas before the Authority finalises its decision.

4.7. The Authority will then determine a final score for each role using the criteria set out in Chapter 3.

Step 2) Calculation of a default reward / penalty and incentive range

4.8. Each score corresponds to a default incentive reward or penalty and has an associated financial range. These default values and ranges are shown in Figure 2.

Figure 2: Incentive scores and financial defaults / ranges



4.9. For example, Table 3 demonstrates that the following scores would result in the following default incentive reward / penalty and overall range:

Table 3: Worked example explaining default incentive reward / penalty and overall range

Role	Role 1	Role 2	Role 3
Score	4	3	2
Default payment (£m)	£4m	0	-£1.6m
Range (£m)	£2m to £6m	-£0.8m to £2m	-£2.4m to -£0.8m
Total default payment (min to max range)	**£2.4m** (-£1.2m to £7.2m)		

Step 3) The adjustment process

4.10. The Authority may consider whether the incentive payment should be adjusted from this default within each score bracket. The Authority may consider adjusting the default incentive reward / penalty in the following circumstances:

- **Evaluation of consumer costs / benefits:** the Authority may consider whether the default incentive reward / penalty is justified by the evidence of benefits / costs created for consumers (including a consideration of potential future benefits and rewards for commitments in previous business plan cycles). As a principle, the ESO should only receive an incentive reward if this is clearly outweighed by the benefits created for consumers. Equally, an incentive penalty should be informed by the costs created for consumers. The Authority may consider the evidence presented and judge whether the additional benefits / costs are justified by the incentive reward / penalty. If the Authority does not feel that this is the case based on the presented evidence, then it may adjust the payment up or down.

- **Close scoring decisions:** if there is a particularly close call between two scores (for example, performance is borderline between score 3 and score 4), then the Authority may decide to adjust the payment up or down to reflect this.

- **Comparison to Determinations:** the Authority may consider the grading of the ESO's delivery schedule as part of Ofgem's Determinations and whether the outturn deliverables were aligned with our expectations under the Roles Guidance.

4.11. Any adjustments made would remain within the incentive ranges determined for each role in Step 2). Any adjustments to the reward / penalty from the default amount will be made by calculating the mid-point from the default value to the upper or lower end of the incentive range. If a further adjustment is warranted, we will adjust the incentive value to the upper or lower end of the incentive range. For example, the ESO may get a score of 4 for Role 1. Therefore, the default amount associated with a score of 4 is £4m. If upon assessing the evidence, we consider that the ESO has demonstrated sufficient performance to warrant a higher incentive reward, then the ESO's incentive value will be moved up, and could receive either £5m (the mid-point from the default value to the upper limit of the incentive range) or £6m (the upper limit of the incentive range).

4.12. In practice, there may be crossover between roles (for example, the ESO may develop an innovative whole-system solution that increases balancing cost efficiency; or, for example, poor outage coordination could increase within-year balancing costs). In these circumstances, the Authority may consider whether adjustments should be made to multiple relevant roles.

5. ESO reporting requirements

This chapter outlines the reporting requirements on the ESO as part of the ESORI Arrangements and provides guidance on what these reports should contain.

Within-scheme reporting

5.1. As outlined in Chapter 2, there are several reporting requirements on the ESO as part of the ESORI Arrangements. The specific outputs the ESO should report on during BP2 is included in Table 4 below.

Table 4: Incentive scheme reported outputs for BP2

Criterion	Monthly Report	Quarterly Report	Six-month and eighteen-month Report	Mid-Scheme Report and End of Scheme Report
Plan delivery		Progress against plan delivery schedule	Progress against plan delivery schedule	Progress against plan delivery schedule
Metric performance	Outturn metric performance & supporting rationale	Outturn metric performance & supporting rationale	Outturn metric performance & supporting rationale	Outturn metric performance & supporting rationale
Stakeholder satisfaction			Results of stakeholder satisfaction surveys	Results of stakeholder satisfaction surveys Optional narrative on stakeholder satisfaction
Quality of outputs	Regularly reported evidence[10]	Regularly reported evidence	Regularly reported evidence	Report against the delivery schedule for each of the activities outlined in the ESO's original Business Plan CBA.

[10] Monthly reporting is not applicable to all regularly reported evidence. See Annex 2 for further details.

				Demonstration of how activities are delivered in line with ESO Roles Guidance expectations. Regularly reported evidence
Value for money		Update report on cost and delivery progress against roles and all ESO specific IT investments.	Update report on cost and delivery progress against roles and all ESO specific IT investments.	Update report on cost and delivery progress against roles and all ESO specific IT investments.

5.2. These reporting documents should be consistent in their structure in order for there to be comparison and read across from the Business Plan to the within-scheme reports and End of Scheme Report. This is to ensure that stakeholders and the Performance Panel can clearly track, review, and assess the ESO's performance throughout the business plan cycle. The ESO should engage with its customers and stakeholders and take into account any feedback on the content or structure of the reports. The ESO should structure these documents per role and subsequent activities in order to align with the evaluation process. The ESO must ensure it considers the supporting guidance for each role and activity outlined in the Roles Guidance document when structuring its reports for each role.

5.3. Further reporting guidance on what is expected for each of these reports is provided below. The ESO is required to publish all these reports on its website. Where there is any confidential or commercially sensitive information, this should be redacted.

5.4. The ESO must ensure to the best of its knowledge that the information provided in respect of the reports in this section are accurate and correct. Where the ESO identifies that the information provided is not accurate or correct, the ESO must notify the Authority and publish or resubmit corrected information as soon practicably possible, unless otherwise agreed with the Authority.

Guidance around specific requirements

Plan delivery

5.5. The ESO is required to update on its progress with its deliverables every quarter. This should include publishing updates against a deliverables tracker. All the deliverables included in the tracker should be clearly numbered and in a consistent format with the original Business Plan.

5.6. If any changes are made to the delivery schedule during the business planning cycle they should be clearly identified and outlined in the reporting documents (e.g. in a separate sub-section), so it is clear where additional amendments have been made in comparison to the original Business Plan. This can ensure Ofgem, stakeholders and the Performance Panel understand the reasons for any changes to plans in advance of its evaluation of the ESO's performance.

Performance measures

<u>Performance metrics</u>

5.7. The ESO is required to regularly report on performance metrics to enable stakeholders to track its performance over the course of the regulatory period. When reporting on performance metrics, the ESO should provide outturn metric performance data and supporting rationale.

5.8. The full list of performance metrics for BP2 is included in Annex 1.

<u>Regularly reported evidence</u>

5.9. The ESO should report on 'regularly reported evidence' to support the realisation of the Business Plan's intended and identified benefits.

5.10. We have outlined in Annex 2 the regularly reported evidence for BP2. This includes the methodologies to be used and the frequency of reporting required.

<u>Stakeholder surveys</u>

5.11. The ESO is required to commission surveys from an independent, reputable market research company. Stakeholder satisfaction surveys will measure satisfaction for each ESO role, focusing on the key activities within the role to track performance. We have outlined in Annex 3 the questions to be used for the stakeholder satisfaction surveys in BP2.

5.12. The surveys should be undertaken on a six-monthly basis, so that they can inform the ESO's six-monthly performance reviews. The key aspects of the survey, including questions, research methods, and types of participants will be approved by Ofgem.

5.13. We expect the surveys to be designed so that key drivers and themes of feedback are recorded and can be tracked over the course of the Business Plan.

Quality of outputs

Cost benefit analysis (CBA)

5.14. The ESO should report against the delivery schedule for each of its activities outlined in its original Business Plan CBA[11], focusing predominately on areas not picked up by performance metrics or regularly reported evidence.

5.15. Reporting should refer to the specified success measures from the original Business Plan CBA and the relevant performance measures. The ESO should also include clear justifications for any changes to the plan and a description of any sensitivity factors which may have impacted on the benefits calculated in the original Business Plan CBA.

5.16. The ESO should undertake this reporting for each of its transformational activities for which a CBA is quantified within the original Business Plan CBA. For any new activities not covered by the original Business Plan CBA, case studies should be presented detailing the consumer benefit of these activities. The ESO's calculation of these benefits should follow the requirements outlined in the section on 'General standards of conduct on reporting' below.

5.17. Where there are new material interventions or changes to arrangements, strong evidence should also include a clear demonstration that the ESO has, where appropriate, assessed multiple solutions to issues and chosen the ones that maximise consumer value. Where it is not practical to undertake a CBA, the ESO should provide a clear articulation of why a particular option was chosen, demonstrating that the ESO has assessed consumer value for each option. In addition, it should be clear that the ESO has not solely pursued an

[11] ESO Business Plan – Annex 7 – Metrics and measuring performance: https://www.nationalgrideso.com/document/158086/download

ESO-led solution without considering whether pursuing or supporting other industry initiatives could have resulted in greater consumer value.

Demonstration of Delivery in line with Roles Guidance Expectations

5.18. Where the ESO cannot clearly demonstrate the benefits from its Business Plan through other reporting (CBAs or regularly reported evidence), the ESO should demonstrate *how* the delivery of its delivery schedule meets our expectations in the Roles Guidance.

ESO value for money reporting[12]

5.19. The ESO is required to provide an update report on its costs and delivery progress each financial quarter to align with the quarterly reporting under the incentive scheme.

5.20. These reports will include a view of overall role costs but have a specific focus on IT and the delivery of IT investments. This will allow the ESO to regularly report its costs and delivery progress, highlighting cost variances or delivery changes from its plans. It will also function as a route to allow the ESO to provide additional evidence to address any concerns Ofgem raised as part of our ex-ante value for money assessment.

5.21. The ESO's reporting against value for money should be split into two sections:

- An update report; this should focus on a summary of overall role costs and a dashboard for each investment, highlighting costs and delivery progress. These dashboards can be supplemented by information for a role or investment to identify deviations from plans and cost forecasts or to highlight a key decision, improvement or change in risk profile. The primary focus of this section of the report is to provide surety to Ofgem regarding the progress of key investments. The structure used will be pre-agreed with Ofgem.

- Any additional information or evidence; the ESO can provide targeted details to answer specific questions asked, provide additional evidence on a topic or provide

[12] The Regulatory Reporting Pack remains the formal cost report for the ESO.

evidence of a change of plan, cost or assumption from their original plan to address areas of concern.

Updates to delivery schedule or value for money scoring within BP2

5.22. As outlined in Chapter 7 of the RIIO-2 Final Determinations – Electricity System Operator Annex, Ofgem may update the delivery schedule grading, performance measures and value for money scoring[13] within BP2 in response to material changes to the ESO's roles, responsibilities or structure within a Business Plan period. This could include material changes that, for example, satisfy one or more of the following conditions:

- substantial new or removed responsibilities that are underpinned by additional licence conditions,
- substantial new or removed responsibilities that change expected annual costs; and
- changes to roles or governance structures that require the ESO to set up new functions and/or materially change its approach to investment.

5.23. The ESO should discuss with Ofgem the changes to its roles, responsibilities, and structure. Where Ofgem agrees an update to the delivery schedule is likely to be merited, the ESO should provide a detailed submission on its proposed deliverables. The updated delivery schedule should be consistent with the ESO's final delivery schedule for BP2 submitted on 31 August 2022.

5.24. Ofgem will undertake a reassessment of the ESO's IT investments to produce an updated RAG rating based on any additional information submitted. Ofgem may update the value for money scoring on an annual basis, as part of the mid-scheme performance review. New information submitted less than six weeks ahead of a performance review may not be considered until the subsequent review point six months later.

Third ESO Business Plan

5.25. We expect to make a decision about the time period and regulatory arrangements for the third and final business plan cycle (BP3) under RIIO-2 by Q3 2023.

[13] For BP2, Ofgem will set an ex-ante value for money scoring for each role rather than setting a cost benchmark.

General standards of conduct on reporting

5.26. This Guidance Document also sets out general standards of conduct that should apply to all reporting performed by the ESO. These are that the ESO must ensure that:

- All reports are accessible and easy to understand, and give prominence to the most pertinent information;
- All reports provide a fair and complete picture of the ESO's performance, including both areas of out- and underperformance;
- Due care and attention are taken to ensuring that information provided in any reports are, to the best of the ESO's knowledge at the time of submission, accurate and complete;
- Where the ESO identifies that inaccurate information is being reported, the Authority must be notified, and corrections made to the report as soon as practically possible;
- Where material amendments are made to any information provided in a report, these amendments are clearly communicated to stakeholders and the Authority and are clearly identified in the reports; and
- It takes on board the Authority's and/or relevant stakeholders' feedback on the reports and factors this into the development of future versions (or provides a reasonable explanation for why feedback cannot be included).

5.27. Where the ESO provides estimates of delivered or forecast benefits in its report, it must in all cases:

- Include a transparent methodology showing how these benefits are calculated, including the inputs used and assumptions made;
- Clearly set out the period over which the benefits have accrued or will accrue; and
- Where the ESO has delivered balancing cost savings within BP2, this should be clearly cross-referenced with the reporting for the balancing cost metric (metric 1A Balancing costs).

Annex 1: Performance metrics 2023-25

Table 5 sets out the details of the performance metrics for 2023-25. Within this we have included annual performance benchmarks to further support transparency of the ESO's within-scheme performance. For the avoidance of doubt, the ESO's outturn performance against the performance metrics (and the ESO's reasons for this outturn performance) over the complete two-year period will be considered for the final incentive decision.

Table 5: Performance metrics set for RIIO-2

Role 1	
1A. Balancing costs	
Method	This metric measures the ESO's outturn balancing costs (including Electricity System Restoration costs) against a balancing cost benchmark. An *ex-ante* representative benchmark will be produced and then updated monthly to reflect appropriately the impact of renewable generation and the wholesale day-ahead price of electricity on balancing costs. The methodology includes the following elements: 1. Initial non-adjusted balancing cost benchmark: At the beginning of the year the non-adjusted balancing cost benchmark is calculated using the following methodology: i. Using a plot of the historic monthly constraint costs (£m) against historic monthly outturn percentage of demand met by renewable generation from the 36 months immediately preceding the assessment year, a best fit straight-line continuous relationship is set to determine the monthly *'calculated benchmark constraints costs'*. ii. Using a plot of historic monthly total balancing costs (£m) against historic monthly constraint costs from the 36 months immediately preceding the assessment year, a best fit straight-line continuous relationship is set, with the intercept value of that straight line used to determine the monthly *'calculated benchmark non-constraints costs'*.

	iii. An equation for the straight-line relationship between outturn renewable generation as percentage of demand and total balancing costs is then formed using the outputs of point 1(i.) and point 1(ii.). iv. The historic 3-year monthly average outturn percentage of demand met by renewable generation for each calendar month is used as the input to the equation in point (iii). The output is 12 *ex-ante*, monthly non-adjusted balancing cost benchmark values. The sum of these monthly values is the initial *'non-adjusted annual balancing cost benchmark'*. The purpose of this initial benchmark is illustrative as it will be adjusted each month throughout the year. 2. <u>Monthly *ex-post* adjustment to the balancing cost benchmark:</u> A monthly ex-post adjustment of the balancing cost benchmark is made to account for the outturn percentage of demand met by renewable generation and the outturn wholesale day-ahead price for electricity in each month. This is done by: i. The monthly value calculated for the *'calculated benchmark non-constraints costs'* in point 1(ii.) is replaced with a value based on the outturn day ahead wholesale electricity price, adjusted by a factor determined by the historic relationship of the day-ahead wholesale electricity price and historic non-constraint costs. This replaces the value previously used to construct the equation in point 1(iii.) ii. The value calculated in point 1(iv.) is recalculated using the updated equation in point 1(iii.), and by using the outturn percentage of demand met by renewable generation for that month instead of the historic averaged monthly values. The *'calculated benchmark constraints costs'* will also then be adjusted to account for the day-ahead wholesale price. The *'non-adjusted annual*

	balancing cost benchmark' is then updated by replacing the historic value for the relevant month with this *ex-post* adjusted value. We will exclude historic months from the calculation of the benchmark which can clearly be identified as outlier values. At this point, we consider only November 2021 to be classed as an outlier, based on significance of the relationship between outturn costs and the variables. *We welcome any views on the design of this metric itself, or on our view of the relevant variables to consider. We welcome suggestions for further variables which impact balancing costs and are outside of the ESO's control.*	
Performance benchmarks	*We will publish an addendum with the initial non-adjusted annual and monthly balancing cost benchmarks as soon as possible once the outturn data to the end of March 2023 is available. The benchmark will then be updated each month based on outturn wind conditions.*	
	Exceeds	10% lower than the *annual balancing cost benchmark*
	Meets	Within ±10% of the *annual balancing cost benchmark*
	Below	10% higher than the *annual balancing cost benchmark*
Reporting frequency	Monthly	
Associated reporting	Explicit reporting on key monthly drivers of costs, including: • any major network outages, and • any material changes in energy balancing prices.	
1B. Demand forecasting		
Method	Measures the average absolute % error between day-ahead forecast demand (taken from Balancing Mechanism Report Service (BMRS[14]) as	

[14] https://www.bmreports.com/bmrs/?q=demand/

<table>
<tr><td></td><td colspan="2">the National Demand Forecast published between 09:00 and 10:00) and outturn demand (taken from BMRS as the Initial National Demand Outturn) for each half hour period. The benchmarks are drawn from analysis of historical errors for the five years preceding the performance year.

5% improvement in historical 5-year average performance expected, with range of ±5% used to set benchmark for meeting expectations.

In settlement periods where Optional Downward Flexibility Management (ODFM) and/or Demand Flexibility Service (DFS) are instructed by the ESO, this will be retrospectively accounted for in the data used to calculate performance. The ESO shall publish the volume of instructed ODFM to enable this to be done.</td></tr>
<tr><td rowspan="4">Performance benchmarks</td><td colspan="2">We will publish an addendum with the performance benchmarks to include outturn data to the end of March 2023 once this data is available. Below is a description of the benchmarks.</td></tr>
<tr><td>Exceeds</td><td>Year 1: < 5% lower than 95% of average value for previous 5 years.
Year 2: As for Year 1, but with 5-year period refreshed.</td></tr>
<tr><td>Meets</td><td>Year 1: ±5% window around 95% of average value for previous 5 years.
Year 2: As for Year 1, but with 5-year period refreshed.</td></tr>
<tr><td>Below</td><td>Year 1: > 5% higher than 95% of average value for previous 5 years.
Year 2: As for Year 1, but with 5-year period refreshed.</td></tr>
<tr><td>Reporting frequency</td><td colspan="2">Monthly</td></tr>
<tr><td>Associated reporting</td><td colspan="2">The narrative on performance against the benchmark should compare to monthly indicative figures (calculated as 95% of the average value for the previous 5 years’ data for the same calendar month). This is an</td></tr>
</table>

<table>
<tr><td></td><td colspan="2">indicative process only and does not necessarily reflect the final annual figure.

The ESO should also include in their monthly reports:
• Narrative relating to the effect of Triad avoidance; and
• Notification of any missed / late publication of forecast data for the previous month, including the reasons for the missed / late publication.

The ESO should provide Ofgem with the forecasts and performance of any operational forecast used that account for the sensitivity of demand to anticipated market prices for electricity.</td></tr>
<tr><td colspan="3">1C. Wind generation forecasting</td></tr>
<tr><td>Method</td><td colspan="2">Measures the average absolute error between day-ahead forecast (between 09:00 and 10:00, as published on ESO Data Portal[15]) and outturn wind generation (as published on ESO Data Portal) for each half hour period as a percentage of capacity for BM wind units only. The data will only be taken for sites that did not have a bid-offer acceptance (BOA) during the relevant settlement period. The ESO will publish this data on its Data Portal for transparency purposes.

The benchmarks are drawn from analysis of historical errors of the five years preceding the performance year. 5% improvement in performance expected on the 5-year historical average, with range of ±5% used to set benchmark for meeting expectations.</td></tr>
<tr><td rowspan="2">Performance benchmarks</td><td colspan="2">We will publish an addendum with the performance benchmarks to include outturn data to the end of March 2023 once this data is available. Below is a description of the benchmarks.</td></tr>
<tr><td>Exceeds</td><td>Year 1: < 5% lower than 95% of average value for previous 5 years.</td></tr>
</table>

15 https://data.nationalgrideso.com/

		Year 2: As for Year 1, but with 5-year period refreshed.
	Meets	Year 1: ±5% window around 95% of average value for previous 5 years. Year 2: As for Year 1, but with 5-year period refreshed.
	Below	Year 1: > 5% higher than 95% of average value for previous 5 years. Year 2: As for Year 1, but with 5-year period refreshed.
Reporting frequency	Monthly	
Associated reporting	The monthly narrative on performance against the benchmark should compare to monthly indicative figures (calculated as 95% of the average value for the previous 5 years' data for the same calendar month). This is an indicative process only and does not necessarily reflect the final annual figure. The ESO should also include in their monthly reports: • The details if wind units withdraw availability between time of forecast and time of metering; and • Notification of any missed / late publication of forecast data for the previous month, including the reasons for the missed / late publication. Additionally, the ESO should publish on its Data Portal the following: Half hourly and unadjusted for BOAs for BM wind units only: • Day ahead wind forecast; • Metered wind outturn; and • Wind capacity. Half hourly broken down by BM wind unit: • Day ahead wind forecast; • The closest to real time wind forecast; • Metered wind outturn;	

	• An indication of whether in that half hour a BOA was issued for that site; • The associate volume specified in any BOA for that site; and • The locational tag to BM wind unit forecasts. The ESO should send all associated reporting to Ofgem in an appropriate time.	
1D. Short notice changes to planned outages		
Method	Measures the number of planned outages delayed by more than an hour or cancelled in the control phase (within day) due to process failure, per 1,000 outages.	
Performance benchmarks	Exceeds	Year 1: <1 Year 2: <1
	Meets	Year 1: 1 to 2.5 Year 2: 1 to 2.5
	Below	Year 1: >2.5 Year 2: >2.5
Reporting frequency	Monthly	
Associated reporting	Narrative on performance against benchmark.	
Role 2		
2Ai. Phase-out of non-competitively procured balancing services		
Method	Measures the overall % of non-competitive services expired or replaced with competitive alternatives as of 31/03/2023. This may include STOR contract expirations.	
Performance Benchmarks	[We are considering this area as part of our consultation. Please see our Draft Determinations for more details]	
Reporting frequency	Quarterly	
Associated reporting	The ESO should include in their reports: • A breakdown of spend for each of the following services: frequency response, reserve, reactive, restoration and constraints.	

	• A narrative on SO-SO trades made during the period, including measures it may have taken to avoid such trades.
2X. Day-ahead procurement	
Method	Measures the volume of products the ESO procures not earlier than in the day-ahead market.[16]
Performance benchmarks	[We are considering this area as part of our consultation. Please see our Draft Determinations for more details]
Reporting frequency	[We are considering this area as part of our consultation. Please see our Draft Determinations for more details]
Associated reporting	[We are considering this area as part of our consultation. Please see our Draft Determinations for more details]
Role 3	
3X. Connection offers	
Method	Measures the timeliness (measured against the ESO's statutory requirements) and/or quality (measured through right-first-time connection offers) of connection offers that would add value.
Performance benchmarks	[We are considering this area as part of our consultation. Please see our Draft Determinations for more details]
Reporting frequency	[We are considering this area as part of our consultation. Please see our Draft Determinations for more details]
Associated reporting	[We are considering this area as part of our consultation. Please see our Draft Determinations for more details]

[16] Following our decision to approve a derogation for mandatory and firm frequency response to be procured earlier than day-ahead, the ESO has a legal requirement to procure at least 30% of its services at day-ahead or closer to real time. However, our expectations are for the ESO to comfortably exceed this value. Our decision to approve the derogation can be accessed at: https://www.ofgem.gov.uk/publications/decision-grant-eso-derogation-requirements-article-69-electricity-regulation-and-exemption-requirements-article-323-ebgl-mandatory-and-firm-frequency-response

Annex 2: Regularly reported evidence 2023-25

Table 6: Regularly reported evidence set for RIIO-2

Role 1:	
1E. Transparency of operational decision making	
Method	% balancing actions taken outside of merit order in the Balancing Mechanism each month.
Quantitative expectations	n/a
Reporting frequency	Monthly
Associated reporting	The ESO's supporting rationale for % of actions taken outside of merit order including trends seen over the course of BP2. This should include an explanation of any steps being taken that may change the future trends. The ESO will also report three supporting statistics: • Monthly percentage of actions taken in merit order, or out of merit order due to an electrical parameter (e.g. voltage constraint); • Monthly percentage of actions that have reason groups[17] allocated; and • Monthly number of actions without a reason. Reporting to include narrative explaining the reasoning behind skipping beyond reason code.
1F. Zero Carbon Operability (ZCO) indicator	
Method	Measures the proportion of zero carbon transmission connected generation that the system can accommodate. The ZCO indicator is defined as:

[17] Reason groups are defined in the methodology published on the ESO's Data Portal (https://data.nationalgrideso.com/balancing/dispatch-transparency) and provide a descriptor for when an action is taken out of merit order.

	$$ZCO(\%) = \frac{(Zero\ carbon\ transmission\ connected\ generation)}{(Total\ transmission\ connected\ generation)} \times 100$$ Zero carbon generation is defined as electricity generation that produces zero carbon emissions at the point of generation. This includes hydropower, nuclear, solar, wind and pumped storage technologies. This regularly reported evidence will be structured as follows: Part 1: defining the maximum ZCO limit The ESO will define the approximate maximum ZCO limit (using a reasonable approximation of likely operating conditions), the system can accommodate at the start and end of BP2, explaining which deliverables are critical to increasing the limit. Part 2: regular reporting on actual ZCO Every quarter, the ESO will report the data on the ZCO provided by the market versus the ZCO following ESO actions. This should be presented at a monthly granularity. Part 3: updates on progress towards increasing the ZCO limit Every year, the ESO will provide detailed case studies on the periods where the market delivered the highest ZCO and the actions the ESO had to take in response. The ESO will provide updates of any actions that are expected to have a material impact on the ZCO limit or are expected to in the future. The ESO will report this as part of its Mid-Scheme and End of Scheme Reports.
Quantitative expectations	n/a
Reporting frequency	Part 1: In first quarterly report and End of Scheme Report Part 2: Quarterly Part 3: Annually (Mid-Scheme and End of Scheme Reports)
1G. Carbon intensity of ESO actions	
Method	Calculates the approximate gCO_2/kWh of actions taken by the ESO, considering the proportion of the total CO_2 emissions on the system which is a result of ESO actions.

	The ESO will use its carbon intensity forecast methodology[18] to estimate carbon intensity factors for each fuel type and interconnector import. The ESO will report on aggregated settlement period data. Full data will be available on the ESO Data Portal.
Quantitative expectations	n/a
Reporting frequency	Monthly
1H. Constraints cost savings from collaboration with TOs	
Method	Measures the estimated £m avoided constraints costs through solutions brought forward in STCP 11.4. Where applicable, these savings should be calculated in line with the methodology that will be developed as part of the new financial incentive on TOs (the SO:TO Optimisation ODI-F). In other cases, the ESO should state the assumptions used for its estimated savings. The ESO should provide additional narrative on any other solutions, such as outage planning actions, and the impact of these solutions on balancing costs.
Quantitative expectations	n/a
Reporting frequency	Quarterly
1I. Security of Supply reporting	
Method	Part 1: Excursions Monthly reporting on instances of any: i. frequency excursions outside 0.3Hz for more than 60 seconds. ii. voltage excursions outside statutory limits Part 2: Annual backward and forward-looking reporting

[18] The ESO's carbon intensity forecast methodology can be found at: www.carbonintensity.org.uk

	Annual summary of the ESO's compliance with its frequency control methodology and plans for any future changes to the methodology.
Quantitative expectations	n/a
Reporting frequency	Part 1: Monthly Part 2: Annual
1J. CNI outages	
Method	Number and length of planned and unplanned outages to critical national infrastructure (CNI) IT systems.
Quantitative expectations	n/a
Reporting frequency	Monthly
Role 2:	
2Aii. Balancing services procured in a non-competitive manner	
Method	Measures the volume and spend for non-competitive services for contracts signed after 31 March 2023. Legacy STOR contracts will be excluded but all SO-SO trades made and any other non-competitively procured services with contract award after this date will be counted.
Reporting frequency	Monthly
Associated reporting	The ESO should explain the rationale for the need to take actions including: • why competitive alternatives were not chosen; • why alternatives were not available (e.g delays to product reform programmes); and • actions being taken to increase availability of competitive alternatives.
2B. Diversity of service providers	
Method	Measures the diversity of technologies that provide services to the ESO in each of the markets covered by performance metric 2A (Competitive procurement).

	The ESO should report on total contracted volumes (mandatory and tendered), with the supporting narrative providing more detail about the % of the service that is procured through mandatory means. The data should be reported at a monthly granularity, which can be aggregated for each quarter to align with quarterly reporting. We continually assess the information that ESO provides for individual services against this RRE, and consider that there might be improvement through better alignment of the data across those services. The ESO will not need to publish data for Black Start providers for security reasons. This information will be provided to Ofgem bilaterally.
Quantitative expectations	n/a
Reporting frequency	Quarterly
2D. EMR demand forecast accuracy	
Method	Peak national demand.
Quantitative expectations	See Table 8 below
Reporting frequency	Following the end of the forecasted delivery year.
Scope	All forecasts that outturn post 1 April 2021 will be assessed against this measure.
2E. Accuracy of forecasts for charge setting	
Method	Measures the accuracy of Transmission Network Use of System (TNUoS) and Balancing Services Use of System (BSUoS) forecasts used to set industry charges against actual charges.
Quantitative expectations	n/a
Reporting frequency	TNUoS charges – Annually BSUoS charges - Monthly
Role 3:	
3A. Future savings from operability solutions	
Method	Forecast medium to long term benefits from new operability measures including:

	i. Saved balancing costs ii. Saved infrastructure costs iii. Monetised carbon reductions Underpinned by transparent benefit calculation methodology published by the ESO.
Quantitative expectations	n/a
Reporting frequency	Six-monthly
3B. Consumer value from the Network Options Assessment (NOA)	
Method	Measures the level of forecast savings created by the ESO through actions to encourage alternative solutions in the NOA (not including NOA pathfinders). Underpinned by a transparent benefit calculation methodology published by the ESO. Where forecasts savings are not available because a NOA process has not occurred, the ESO can instead provide and update on its actions over the preceding six-months to create additional value in the annual NOA.
Quantitative expectations	n/a
Reporting frequency	Six-monthly

Table 7: Quantitative performance expectations for regularly reported evidence 2D (EMR demand forecasting)

	Exceeding expectations	In line with expectations	Below expectations
2021-22 T-1	<2% peak demand accuracy	2% peak demand accuracy	>2% peak demand accuracy
2021-22 T-4	<4% peak demand accuracy	4% peak demand accuracy	>4% peak demand accuracy
2022-23 T-1	<2% peak demand accuracy	2% peak demand accuracy	>2% peak demand accuracy

2022-23 T-4	<4% peak demand accuracy	4% peak demand accuracy	>4% peak demand accuracy

Annex 3: Stakeholder satisfaction survey 2023-25

Survey method

The survey will be undertaken either by phone and/or online, dependent on stakeholder preferences.

Participants

The survey will be targeted at senior managers, decision makers and experts and will include a wide selection of relevant stakeholders who have had material interactions with the ESO's services. The exact survey participants will be determined by the ESO's stakeholder contacts database. We expect the ESO to maintain up to date contact details of its stakeholders.

Questions

The ESO will ask one question on stakeholder satisfaction for each role, outlined below:

"One of our ESO roles is focused on [Control Centre Operations], which includes key activities such as [real-time system operation], [system restoration] and [provision of data and forecasting].
Overall, from your experience engaging with ESO teams in these areas in the last six months, how would you rate the ESO's performance?

a) Below expectations / Meeting expectations / Exceeding expectations / Don't know
b) Please explain your reasoning."

The ESO's recent activities for each role should draw from the most relevant deliverables over the past six months of activity.

Annex 4: Glossary of ESORI Guidance terms

Table 8: Glossary of key terms used in ESORI Guidance

Element	Description
Activity	A subset of responsibilities within a role with specific expectations and deliverables attached to it.
Business Plan	Details the ESO's costs, activities, deliverables, and performance metrics for delivering its strategy over the first two years of the RIIO-2 period.
Business plan cycle	The business plan cycle is the period for which the business plan is applicable. The second business plan cycle (BP2) covers the incentive scheme starting on 1 April 2023 and ending on 31 March 2025.
Deliverable	A specific delivered output within an activity which has associated delivery dates and success measures.
Delivery schedule	A grouping of deliverables for either a role or the Business Plan.
ESO Performance Panel	A mix of independent experts and industry representatives that are responsible for reviewing the ESO's plans and performance, as well as performing an End of Scheme evaluation of the ESO's performance.
Evaluation criteria	The criteria used by the Performance Panel to measure the ESO's performance for each role.
Incentive scheme	The process over a business plan cycle to assess the ESO's performance against five key criteria, resulting in the award of a £m reward or penalty.
Long-term vision	The long-term vision covers the period from the start of RIIO-2 to 2030.
Medium-term strategy	The medium-term strategy is the five-year strategy covering the RIIO-2 period.
Performance benchmarks	Describes ex-ante what level of outturn performance is below, meets and exceeds expectations for each performance metric.
Performance measure	A measure of the ESO's performance, including performance metrics, stakeholder satisfaction and other regularly reported evidence.
Performance metric	A numerical measure of ESO performance which can be produced regularly, has a pre-defined methodology and has clear performance benchmarks.

Plan grading	Ofgem's grading of the delivery schedule for each role, designed to set a clear reference point and align expectations in the incentives process.
Regularly reported evidence	Evidence that should be regularly reported by the ESO to inform the evidence of benefits criterion in the evaluation criteria.
RIIO-2 period	RIIO-2 covers the period starting 1 April 2021 and ending on 31 March 2026.
Role	One of the three roles in the roles framework.
Roles framework	Sets out our expectations for how the ESO should comply with its obligations, and for RIIO-2, meet and exceed our incentives expectations under three roles: control centre operations; market development and procurement; and system insight, planning and network development.