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ESO Response to Ofgem's Consultation on the draft Forward Work Programme 2023/24

Dear FWP Consultation team,

Thank you for the opportunity to respond to your consultation on Ofgem's draft Forward Work Programme for 2023/24 outlining the strategic priorities, projects and programmes which will be the focus for the coming year ahead.

Who we are

As the Electricity System Operator (ESO) for Great Britain, we are in a privileged position at the heart of the energy system, balancing electricity supply and demand second by second.

As the UK moves towards its 2050 net zero target, our mission is to drive the transformation to a fully decarbonised electricity system by 2035, one which is reliable, affordable, and fair for all. We play a central role in driving Great Britain's path to net zero and use our unique perspective and independent position to facilitate market-based solutions to the challenges posed by the trilemma.

Our transformation to a Future System Operator (FSO) is set to build on the ESO's position at the heart of the energy industry, acting as an enabler for greater industry collaboration and alignment. This will unlock value for current and future consumers through more effective strategic planning, management, and coordination across the whole energy system.

Our key messages

- Ofgem has a critical role to play in enabling industry to deliver against the great changes and challenges of the coming years, and we are keen to support Ofgem in this.
- A significant amount of strategic investment will be required to meet the demands of full electricity decarbonisation by 2035, and net zero across the whole economy by 2050. At the same time consumers are experiencing a major cost-of-living crisis, with energy costs at an unprecedented level.
- Whilst we recognise the importance of focusing on the energy cost crisis, we urge Ofgem to continue to work with the ESO and wider industry on the longer-term reforms that are critical to enabling a safe, secure energy system of the future.
- We agree with Ofgem's approach to the Consumer Interest Framework. This echoes the consumer priorities we identified in our own stakeholder engagement activities. Consumers want an affordable energy bill based on fair prices, energy that is available when needed from resilient infrastructure, a decarbonised system that is fit for the future delivered through a low-cost transition and an energy system that is safe and secure achieved through adherence to quality and standards.

- We welcome Ofgem prioritising the facilitation of infrastructure investment, including connection reform, work on multi-purpose interconnectors, and delivery of strategic investment from the holistic network design (HND) including 50GW of offshore wind by 2030. We are keen to work with Ofgem on these areas as well as on finalising the 'early competition model'.
- We agree that market reform including access and charging reforms should be a strategic priority with the objective of incentivising parties to locate and dispatch in the right place. We support the inclusion of considering wholesale market and future interconnector arrangements which we believe is important with the growth in interconnector capacity expected over the coming years.
- With regards to reforms of governance arrangements, as we transition to a Future System Operator (FSO) we look forward to working with Ofgem on the development of the necessary regulations and licence to establish and enable its effective performance.

We look forward to engaging with you further. Should you require further information on any of the points raised in our response please contact Adelle Wainwright, Regulatory Policy Manager at adelle.wainwright@nationalgrideso.com. Our response is not confidential.

Yours sincerely

Gareth Davies

RIIO and Regulation Senior Manager

Appendix 1 – Consultation Question Responses

Question 1 What are our views on Ofgem's Consumer Interest Framework and its use?

We agree with Ofgem's approach to the Consumer Interest Framework. This aligns with the consumer priorities we identified in the stakeholder engagement activities as part of the creation of our BP2. Consumers want an affordable energy bill based on fair prices, energy that is available when needed from resilient infrastructure, a decarbonised system that is fit for the future delivered through a low-cost transition and an energy system that is safe and secure achieved through adherence to quality and standards.

We believe that consumers are fundamental to the energy transition. In a decentralised energy structure, they become ever more important as a key part of the solutions needed to deliver a secure, reliable, and cost-effective decarbonised system.

Question 2 Are the Strategic Priorities the ones Ofgem should focus on in 2023/24 and beyond?

Short term priorities

We recognise the importance of focusing on the short-term priorities outlined in the draft Forward Work Programme; **ensuring prices are fair, creating resilience across the energy sector and monitoring and enforcing quality and standards.**

Amid the energy price crisis, attention will rightly be directed towards the most pressing and immediate issues. Having published an early view of Winter in July 2022 to help the market to understand the risks and continue to prepare, we also took additional measures such as the successful negotiation of coal contracts to retain approximately 2GW of coal fired generation that would otherwise have closed. Collaborating closely with suppliers, aggregators, industry, Ofgem and BEIS we also introduced the innovative Demand Flexibility Service to incentivise customers to reduce consumption at periods when margins are tight. We realise that these issues will continue to be a priority for the year ahead and will build on the work undertaken to manage the challenges of this winter, to plan for and mitigate against the challenges which we may face in 2023 and into 2024.

A focus on the short-term priorities should be balanced with strategic change to support the transition to net zero and ensure GB's energy security in the longer term.

Longer-term priorities

Looking beyond the more immediate issues we agree with the longer-term priorities **to facilitate infrastructure investment**, including reform of the existing connections process, **to develop and deliver market reforms** and to **reform governance arrangements**. We see consistency and synergies between the Strategic Priorities Ofgem have outlined in the consultation with the ESO's objectives and ambitions.

We welcome Ofgem prioritising the facilitation of infrastructure investment, including connection reform, work on multi-purpose interconnectors and delivery of strategic investment from the holistic network design (HND) including 50GW of offshore wind by 2030.

The current crisis reinforces the need for a long-term vision and strategy for net zero markets. Ensuring we deliver a clean, reliable, and secure system requires efficient and coherent electricity markets and we were pleased to see a consultation from the Department for Business, Energy & Industrial Strategy in October 2022 and the inclusion of Consumer Empowerment and Consumer Fairness in the vision for electricity system presented within it. We welcome the inclusion here of the longer-term priority to develop and deliver market reforms which enable greater flexibility and support the continued growth of renewable generation.

Following the Government announcement at the end of November 2022 to commit to delivering its Energy Bill, we are pleased that the legislation to establish the FSO will continue its passage through parliament, with the expectation that the FSO will go-live in April 2024. This is a significant step for us in the transition to our new role at the heart of the energy system. We look forward to working with Ofgem as we move into this role and the development of the necessary regulations and licence to establish and enable its effective performance.

Question 3 Are the Projects and Programmes the ones Ofgem should focus on in 2023/24 and beyond?

Our response comments only on areas relevant to our role in the industry and we have not commented on projects or programmes beyond our involvement.

Under the short-term priority of **ensuring prices are fair** Ofgem outline the following projects and programmes.

- **Government Bill Support**
- **Vulnerable Customer**
- **Retail Market Reform**
- **Consumer Price Protections**

Whilst most of the activities highlighted in the short-term priorities relate to elsewhere in the sector, we agree that these are priority areas and as the ESO will continue to be efficient and play our part in minimising costs to consumers.

Under the short-term priority of **Creating Resilience across the Energy Sector** Ofgem outline the following projects and programmes.

- **Security of supply**

Building on the preparation and work undertaken to ensure that we in the ESO are set up to deliver through winter 2022/23 we will continue to work with Ofgem and industry to support a secure energy supply for winter 2023/24 and beyond.

- **Cyber**

As operators of critical national infrastructure, we recognise the vital importance of cyber resilience. We have appointed a Chief Information Security Officer (CISO) directly accountable to the ESO Executive Team (ESOET) who will continue to work with Ofgem in this space.

- **Power Market Liquidity**

We welcome the intention to work with BEIS on issues around wholesale power market liquidity. We see a clear need to investigate and better understand the extent to which liquidity in forward markets is accessible and useful, or not, in achieving the outcomes needed from a well-functioning wholesale market.

- **Financial Resilience and Controls**

Whilst these do not relate directly to our sector, we recognise they are priority areas for Ofgem.

Under the short-term priority of **setting, monitoring, and enforcing standards** Ofgem outline the following projects and programmes.

- **Compliance and enforcement**

We agree that Ofgem should continue with their compliance and enforcement activities to protect consumers and agree with the focus being on areas that are of the greatest potential harm to consumers.

- **Heat Network regulation**

We expect heat networks to have a role in the decarbonisation of the energy system and to play a role in consumer flexibility as outlined in our Future Energy Scenarios 2022. Whilst numbers of connected customers are still relatively low it is likely that this will continue to grow, and it is timely to set-up the regulatory framework in advance of the expected plans from government in 2024.

Under the longer-term priorities of **facilitating infrastructure investment** Ofgem outline the following projects and programmes.

- **Enable time critical investment in infrastructure**

Building on the delivery of the Holistic Network Design in July 2022, the ESO is now working on the Holistic Network Design Follow-up Exercise (HNDFUE) to consider additional offshore farms in Scotland and in the

Celtic Sea. The new network needs from the HNDFUE will be further assessed against a range of alternative options in the next iteration of the Network Options Assessment (NOA) later in 2023. The output of the HNDFUE and the next iteration of the NOA will form the second iteration of the 'Transitional Centralised Strategic Network Plan' (tCSNP2).

In response to feedback the methodology for the HNDFUE provides for a more collaborative and efficient design process and we look forward to working with Ofgem, BEIS and industry as it progresses.

Regarding the implementation of the second electricity distribution price control, we agree that Distribution Network Owners (DNOs) must be sufficiently funded to carry out whole electricity system activities which we have included as part of our own RIIO-2 BP2 deliverables and to support the connection of new low carbon power sources whilst meeting increased demands through the electrification of transport and heat.

We also expect that interconnector capacity will grow over the next decades and play a major role in both decarbonisation and system security and look forward to the conclusions of the 'initial project assessment' for new interconnectors and pilot project for multi-purpose interconnectors.

We are acutely aware of the issues inherent in the current connections process which was designed for a very different energy system to the one we currently operate in, and which will be vastly different to that of the future. We are keen to work closely with Ofgem and wider industry in reforming the connections process. In October 2022, we opened the Transmission Entry Capacity (TEC) Amnesty window. This will run until April 2023 and in July 2023 we plan to communicate the next steps. This is one element of the reforms and actions needed to facilitate infrastructure investment and enable faster, more efficient approaches for those wanting to connect to the transmission system. Working with stakeholders we understand the need to implement more effective Queue Management arrangements and know the vital role this plays in delivering value to consumers and enabling a decarbonised, decentralised system.

- **Future network regulatory framework**

Having an optimal regulatory framework in place across the sector creates the conditions needed for the energy industry to achieve the growth needed to deliver decarbonisation targets and maintain security of supply, efficiently and effectively for all consumers. Regulatory arrangements need to ensure that the sector minimises cost and maximises value wherever possible to support a "just transition", where affordability and fairness remain imperatives to a successful net zero outcome.

The RIIO model was designed to deliver a sustainable energy sector, provide long-term value for money, and encourage innovation and timely delivery. It has succeeded in enabling substantial investment, innovation and efficiency and generated significant consumer value since it was launched in 2010. However, the scale and pace of change that is facing the energy system means that there is certainly a case now for considering alternative regulatory models. Whatever model is chosen, frameworks need to be sufficiently complementary and flexible to allow for decisions to be taken across vectors in a coordinated way.

It is already recognised that the ESO's bespoke regulatory model is designed to allow the organisation to adapt to a changing energy landscape, as well as prioritise wider system and consumer interests in decision-making. Given the scale and pace of change anticipated across the sector, it will be equally important for this flexibility to continue through the coming years as we become the FSO, and the framework should ensure that roles and responsibilities are clearly defined.

We look forward to continuing to work with Ofgem on finalising the 'early competition model' and to the final determinations on our own Business Plan 2 submission to take us through the next period in our evolution.

- **Nuclear Regulated Asset Base (RAB) model**

The design of the nuclear RAB model should ensure that nuclear is incentivised to respond to wholesale price signals. BEIS's Review of Electricity Market Arrangements (REMA) and our Net Zero Market Reform (NZMR) programmes should also be considered. Historically nuclear power plants have operated at baseload providing security of supply when renewable output was low. Additionally, the RAB model must be designed to ensure that consumers are not exposed to the risk that system reinforcement is funded both through this model and through regulatory arrangements with Transmission Owners.

- **Carbon Capture Utilisation and Storage (CCUS) RAB model**

CCUS is one of a range of flexible technologies identified in FES needed to integrate renewables and maintain security of supply.

- **Hydrogen**

Hydrogen will be a crucial part of the whole energy system soon. In FES 2022 it is needed in all net zero scenarios to provide inter-seasonal flexibility. Alongside taking a whole energy system approach, an independent Future System Operator which does not financially benefit from transportation or storage infrastructure can demonstrate impartial decision-making that places consumer fairness and value at the heart of its activities. We believe that it is important that the FSO takes a prominent role in the planning and optimisation of a Hydrogen network and look forward to continued engagement on this with Ofgem and government, including the development of the framework for the new Centralised Strategic Network Plan through the Electricity Transmission Network Planning Review.

Under the longer-term priority of **developing and delivering market reforms** Ofgem outline the following projects and programmes.

- **Enabling markets for flexibility**

Enabling markets for flexibility is a key element in ensuring energy supply and demand are balanced and security of supply criteria are met, as the energy system decarbonises. It is vital therefore to ensure the continued roll-out of smart metering which is a key enabler to consumer participation in flexible markets as demonstrated in the Demand Flexibility Service we launched to incentivise customers and businesses to reduce their power consumption at certain times. Smart Meter data is necessary to understand consumer behaviour and access to this data enables innovation across the industry. A new regulatory model for the Data Communications Company (DCC) should make roles and responsibilities clear and provide clarity on data ownership and the mechanisms by which open data is accessed.

Along with ensuring that customers are protected in emerging competitive markets for smart energy appliances and demand side response mechanisms, we think that there is merit in building in mechanisms to protect the energy system itself from potential risks from remote load controllers such as a randomised delay now with more sophisticated tools being delivered as markets mature.

- **Wholesale market reforms & charging arrangements**

We agree that reform is needed to put effective signals in place to incentivise parties to locate and dispatch in the right place, at the right time. We believe that nodal pricing could deliver maximum value for consumers and accelerate decarbonisation and combined with centralised dispatch is the most effective way to coordinate the energy system and enable the market to resolve system constraints. A clear vision and well managed transition addresses much of the uncertainty that significant market reform creates for investment. Whilst we continue to reform operability markets on the transition to net zero, improving wholesale market design and including interconnector arrangements will result in much better outcomes.

Alongside market reform we are supportive of a review of the TNUoS methodology and believe that these should be undertaken in a coherent and holistic approach.

Under the longer-term priority of **Reforming Governance Arrangements** Ofgem outline the following projects and programmes.

- **Future System Operator and local governance**

Becoming the FSO is a critical step to help deliver a reliable and clean energy transition for all. We look forward to continued collaboration with Ofgem, government and industry through this period as we become established at the heart of the energy system. Assuming responsibility for new and enhanced roles to drive progress towards net zero, deliver value for consumers by enabling potential cost reductions through improved whole energy system decision-making, and supporting energy security, we believe that the FSO should be set up at pace to begin delivering these essential roles.

We will continue to engage on the future of local institutions and governance to understand our role to support any reforms as part of the 'minded to' position.

- **Energy Code reform**

We are supportive of the proposed plans to develop the approach to implement energy code reforms and have responded to the recent Call for Evidence on this topic.

- **Energy Sector digitalisation**

As the ESO, we believe that digitalisation and data are core components of our transition towards reaching zero carbon operability. Our customers are depending on us to digitalise data and processes in a more democratised marketplace which is accessible to more and more people. Harnessing the benefits of digital technology will enhance our operations, enable participation in smart and sustainable markets, unlock consumer value through competition and help the drive towards a decarbonised, whole energy future. We welcome the intention set out in the draft Forward Work Programme to establish regulatory expectations, embed best practice, accelerate digitalisation innovation, and promote better cross-sector digital communication and collaboration.