



ade

The Association for
Decentralised Energy

Combined Heat & Power
Demand Side Services
Energy Efficiency
Heat Networks

ADE Response Future System Operator (FSO) draft licences consultation 20 October 2023

Context

The ADE welcomes the opportunity to respond to Ofgem's Consultation on the Future System Operator (FSO) draft licences.

The ADE is the UK's leading decentralised energy advocate, focused on creating a more cost effective, low-carbon and user-led energy system. The ADE has more than 150 members active across a range of technologies, including both the providers and the users of energy equipment and services. Our members have particular expertise in demand side energy services including demand response and storage, combined heat and power, heat networks and energy efficiency.

Overall Evaluation

Generally, the licence conditions reflect the basic intent and statutory provisions of the Energy Security Bill 2022. However, that alone does not adequately reflect the wholesale transition the ESO is making from a private company to a public body. This transition necessitates greater demands within its licence conditions on transparency, accountability, and the recognition of the market power it holds. The FSO licences must aim to improve the areas of persistent industry and regulatory concern, namely initiating a change of culture rather than just a change of name.

Reforming how ENCC relates and interacts with the rest of the ESO is one such cultural change. While other areas of ESO have begun taking a more forward-facing approach during RIIO-2, issues with control room systems, digitalisation, and transparency have made reformative change impossible. Furthermore, when 'transparency' events are held, they are hallmarked by persistent pre-scripted broad responses that do not address the detail of the question asked. Likewise, control room often cite their core licence obligation as balancing the grid efficiently and economically and that any other obligations are peripheral. Going to our proposals in question 1, this could be taken to mean that control room do not consider the duty to treat all assets fairly or to prove that prima facie discriminatory actions are justified, are part of their licence obligations. Aside from and above the points raised in question 1, it is possible that a further licence condition may be needed to ensure the independent oversight of the ENCC.

Finally, we cannot simply forget the summary of the Zuhlke report, published as an Appendix of Ofgem's RIIO-2 BP 2 Draft Determinations. Not only were repeated calls made by ADE for Ofgem and ESO to hold a joint public session to discuss these results for those stakeholders perhaps not able to dedicate time to perusing regulatory appendices, ESO representatives were questioned about the report at a Parliamentary Select Committee where the only answer given was that they dispute some of the findings. For an independent audit to conclude half a billion pounds of investment raised concerns and that "Future System Operator needs are at risk" without any further public follow-up from ESO or the regulator hardly instils faith in the transparency and accountability mechanisms in place. Therefore, we strongly reiterate our calls for a public session to examine the audit in detail and allow the ESO to address what findings they dispute, rather than stakeholders having to root through another set of appendices.

Q1. Does the draft ESO licence capture the policy intent set out by the joint 'Proposals for a Future System Operator' and 'Future System Operator: second policy consultation and project update' consultations?

We do not believe Cond. C9, Part A, Para 2 should be added. Para 3 already implies that ESO can take technical differences into account when balancing and therefore Para 2 is superfluous. Beyond this however, the FSO is substantially and strategically different entity to the current ESO which

demands greater accuracy in its licence conditions that could result in discriminatory decision-making or market distortions. For example, the licence obligations should be sufficiently clear so as to prevent another incident of significant time and money being invested in a patently discriminatory service such as Balancing Reserve in 2022/23. The FSO licence should:

- Add 'design' of balancing services to the conditions under considerations, noting the proposal to remove references to technical differences.
- explicitly prohibit any design, procurement, or use of balancing services that disproportionately discriminate against certain technology types based on technical differences such as volume or being single or aggregated portfolios.
- Set out that the burden for proving that a design or procurement decision is necessary and proportionate is based squarely on the FSO, not industry. In other words, any design or procurement decisions that appear prima facie discriminatory should have a presumption of invalidity for the FSO to rebut, rather than requiring stakeholders to prove why decisions are wrong.
- Building on the above, set out that control room incapacibilities, as opposed to system or energy needs, are not a justifiable reason for discriminatory treatment of assets in the design, procurement or decision-making on balancing services.
- Finally, outline a proportionality test for the ESO to satisfy in cases of such conflicts.

Some examples of how this differs from current practice:

- Upon the entry of independent aggregators into the BM in 2019, NGESO introduced new operational metering requirements for small (sub-100MW) participants without industry consultation or regard to the regulatory metering requirements of individual assets. These mandate that operational metering is reported at 1 second intervals with 1% accuracy, as well as the monitoring of both real and reactive power. Despite repeated requests for over four years, ESO has not been able to provide an evidenced answer as to how the 1s/1% standard was arrived at. Although ESO Power Responsive is launching a live trial to test somewhat relaxed requirements to facilitate particularly domestic assets in the BM, ESO Control Room (ENCC) has yet to engage directly with industry on how the original standards were set or on how these new, still stringent, standards were reached and whether, or how long it will take for, these prohibitive barriers to be removed. The effect is the continued exclusion of smaller volume distributed assets from entering ESO markets despite the clear legislative intent behind the EV Smart Charge Point Regulations 2021 and the Energy Security Bill 2022. Without proper explanation to the contrary from ESO, these standards represent a disproportionate barrier to participation for smaller volume assets.
- In an effort to prioritise pace, NGESO opted for minimum viable products (MVPs) as opposed to fully rounded designs in their approach to ancillary service reform, launching their first reformed Frequency Response product, Dynamic Containment (DC), at the end of 2020. The requirement of 60-minute nominated baselines as the default parameter for new products resulted in many non-battery assets that could participate in the extremely fast responding Dynamic Frequency Response services being excluded. Although the alternative approach using derived data, as proposed by the ADE and its members, was well received by the ESO, the process to get this change in the Service terms that would enable this proposal to be advanced has taken over three years and will not be implemented until April 2024 at the earliest. Delays such as this undermine the objectives of market reform under RIIO-2 to remove barriers, increase participation and create competitive markets. The

longer certain types of aggregation are precluded from the market, the longer it will take to fulfil these objectives, including getting more low carbon assets on the system.

- The introduction of the Local Constraint Market (LCM) was widely praised as a pragmatic approach to one of the most constrained areas of the country. However, without consultation, NGESO elected to adopt an approach to Applicable Balancing Services Volume Data (ABSVD) that, although not formally discriminatory, substantively disadvantaged independent aggregators wishing to participate in the service in comparison to suppliers. In such cases, by attempting to correct the supplier's imbalance position for balancing actions taken in response to an instruction from ESO, the supplier is inadvertently being rewarded for aggregator actions and not obliged to pass this reward to the customer. As demand turn-up services become increasingly commonplace in a world where, according to the REMA Consultation, generation could exceed demand up to 50% of the time, it is imperative that all participants are able to provide these services in an equitable way and that past market orthodoxies do not undermine the decarbonisation journey. Speaking to a wider issue, it also highlights the danger of the limited participants often involved in trials or the design phase of services where these issues are best addressed to avoid MVP lock-in as discussed above.
- The Dispatch Transparency Tool to monitor BM skip rates is evidently not fit for purpose. While ESO repeatedly say that less than 1% of skips are unaccounted for, there is strong anecdotal evidence and ESO communications that indicate this is an underestimate. At a December event, certain points were communicated to industry demonstrating the subjectivity of dispatch decision-making. In particular:
 - o When the control room is busy and operators take an out-of-merit action because of its volume, this is not considered a 'true skip', rather they look to what caused the business for example, constraint, frequency. In the tool, therefore, the action is attributed to operational conditions not as a result of the limitations of manual dispatch.
 - o When making decisions on whether to dispatch 1x20MW unit or 20x1MW units, control room takes into account discrepancies in unit forecasts. Even though the probability of average discrepancy may be similar, it is easier for them to phone the 1x20MW in case of a fault than 5x1MW units.
 - o Since engineers can more readily recall the parameters of large volume assets rather than the duration of many small batteries, this can impact their decision-making.
 - o If engineers believe they may need fast acting units such as batteries at a later time they may opt not to accept their bids and offers in order to avoid them being unavailable later. However, if those assets are not later needed they are left unutilised.

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