

To: All interested stakeholders

Email: [ESOperformance@ofgem.gov.uk](mailto:ESOperformance@ofgem.gov.uk)

Date: 30 October 2024

Dear colleagues,

**Decision on the National Energy System Operator's proposed amendments to the Terms and Conditions related to Balancing in relation to dynamic response services.**

On 30 August 2024, we<sup>1</sup> received a proposal from the Electricity System Operator<sup>2</sup> ("ESO") to make amendments to the terms and conditions related to balancing ("T&C") required by Article 18 of Commission Regulation (EU) 2017/2195 establishing a guideline on electricity balancing ("EBGL")<sup>3</sup>, as amended by the Electricity Network Codes and Guidelines (Markets and Trading) (Amendment) (EU Exit) Regulations 2019.

The proposal relates to updates to the 'Response Services Service Terms' ("Service Terms") and 'Response Services Procurement Rules' ("Procurement Rules") which forms part of the T&C for each of the Dynamic Response products – Dynamic Containment ("DC"), Dynamic Moderation ("DM") and Dynamic Regulation ("DR").

This letter sets out our decision to approve that these documents form part of the T&C required by Article 18 of EBGL, replacing any previous versions that formed part of the T&C for each service effective immediately, unless specified in our assessment below.

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<sup>1</sup> The terms "we", "us", "our", "Ofgem" and "the Authority" are used interchangeably in this document and refer to the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.

<sup>2</sup> This report was submitted by National Grid Electricity System Operator, at the time the holder of an Electricity Transmission Licence in Great Britain. As of 1 October 2024, National Grid Electricity System Operator has transitioned to become National Energy System Operator. We have confirmed with NESO that it still wants the submission to be considered.

<sup>3</sup> Commission Regulation (EU) 2017/2195 of 23 November 2017 establishing a guideline on electricity balancing (EBGL). EBGL came into force on 18 December 2018. Accessible at: <https://eur-lex.europa.eu/eli/reg/2017/2195/oj>

## Background

In accordance with Article 18 of the EBGL Regulation, the ESO was required to develop a proposal regarding the T&C for balancing service providers (“BSPs”) and balance responsible parties (“BRPs”).<sup>4</sup> On 8 October 2019,<sup>4</sup> we published our decision to confirm, upon satisfaction of certain conditions, that the T&C proposed by the ESO are the T&C required by Article 18 of the EBGL Regulation. On 25 June 2020, all the necessary conditions were met, and the proposed T&C came into force in Great Britain (“GB”). The dynamic response products are opt-in services for BSPs to receive payment from the ESO for the provision of balancing capacity, and to deliver balancing energy, acting quickly to help maintain system frequency around the target value of 50Hz.

DC is a fast-acting, post-fault service designed to arrest frequency in large-loss, low-inertia scenarios, delivering energy proportional to the change in frequency within  $\pm 0.5\text{Hz}$  of the target value in the event of a sudden demand or generation loss. The DC low frequency (“DCL”) product went live in October 2020, followed by the launch of the DC high frequency service (“DCH”) in October 2021.

DM and DR are pre-fault services wherein providers make automatic adjustments in generation (or demand). DR provides a constant power response across the operational frequency range, reaching full delivery at a  $\pm 0.2\text{Hz}$  frequency deviation. DM responds between  $\pm 0.1\text{Hz}$  and  $\pm 0.2\text{Hz}$ , providing additional power to stabilise frequency as it moves closer to operational limits. DM and DR were launched in March 2022.<sup>5</sup>

## The proposal

The ESO submitted its proposal to update the T&C for the three dynamic services on 30 August 2024 following a period of consultation on these changes which ran between 27 June 2024 and 29 July 2024.

The ESO’s consultation highlighted the changes to the proposed Service Terms and Procurement Rules, which describe the requirements for the provision of each of the services. To aid with the visibility of the T&C the ESO has also provided an updated mapping document.

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<sup>4</sup> See footnote 2 and our decision of 14 September 2018 <https://www.ofgem.gov.uk/decision/decision-assignment-transmission-system-operator-obligations-under-guideline-electricity-balancing-regulation-within-gb>

The key changes that the ESO proposed to update to various sections of the Service Terms and Procurement Rules are:

1. Removal of Maximum Ramp Rate
2. Availability description
3. State of Energy ("SoE") management rules – During service delivery
4. SoE rule – Submitting sell orders
5. Requiring operational metering and operational baselines at all times
6. Penalty Reform and Unit Suspension
7. Disarming and re-arming instructions outside contracted service periods
8. Maximum sell size
9. Zero Deadband for non-energy limited assets
10. Transfer: pay secondary provider
11. Updates to Schedule 3
12. Other housekeeping changes

Two of these submissions, 6 and 9, will not be implemented upon publication of the revised Service Terms and Procurement Rules. On further engagement, NESO<sup>5</sup> has confirmed that the provision under submission 9 will be enabled from 1 February 2025, but are unable to commit to a firm implementation date for submission 6.

We have reviewed the Service Terms and Procurement Rules proposed by the ESO to be part of the T&C and submitted to us in line with the requirements of the EBGL Regulation, the wider objectives of the Electricity Regulation and our statutory duties and obligations. We have also engaged with NESO to better understand its proposals in some areas, as well as the progress it has made towards the development of these services.

In making our decision, we have considered the responses to the consultation from industry stakeholders. The responses from industry were generally favourable of the changes that the ESO proposed. The ESO responded to questions raised by respondents appropriately and held bilateral engagements where this added further benefit. Where the industry made suggestions or disagreed with proposals, the ESO took these on board if relevant, making amendments or removing sections.

The ESO designed and submitted their proposed revisions to be assessed independently. Therefore, we have assessed them independently from each other. Rejecting one submission is not a rejection of all and we will decide whether to accept or reject each submission separately. This is a change in approach from previous Dynamic Services Article

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<sup>5</sup> NESO is the Independent System Operator and Planner in Great Britain.

18 submissions, where we assessed all proposed revisions as one submission. We support NESO submitting proposals for Dynamic Services in regards to Article 18 in this way going forwards due to the flexibility it provides.

## **Our assessment**

### 1. Removal of Maximum Ramp Rate

The ESO proposed removing the Maximum Ramp Rate which is currently set at 5% of contracted MW per minute. A Maximum Ramp Rate may have driven higher prices due to constraining opportunities for wholesale market participation and more efficient SoE management. These prices would have been passed onto consumers.

The ESO received significant support from respondents to this change, many citing that this creates a more level playing field. The ESO made clear in their submission that this change will be in effect as soon as the updated Service Terms and Procurement Rules are published in response to several respondents asking for an implementation delay. We note that the ESO shared the details of this change earlier in 2024,<sup>6</sup> and agree that these terms should be brought in line with practice as soon as possible.

We approve this change and note that it primarily benefits batteries, which are now no longer limited by having to artificially stagger their response. Respondents have stated that this change allows for a more efficient service delivery and will lead to a more efficient market overall. These benefits will reduce the cost to consumers by simplifying optimisation for participants.

### 2. Availability description

The ESO have proposed clarifications on available / unavailable declarations in the Service Terms. These clarifications include when and how providers should declare their position.

A majority of respondents supported this change, several did not share positions and none were opposed. One respondent suggested some amendments to the proposed Service Terms, which the ESO responded to and updated.

We approve the changes being proposed, and note that NESO will publish a Guidance document that demonstrates how SoE levels will be monitored throughout service delivery. We expect this Guidance document to be published alongside the updates to the Service Terms.

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<sup>6</sup> You can access the webinar at: <https://www.neso.energy/document/317986/download>

### 3. SoE management rules – During service delivery

This proposal is designed to clarify the Service Terms on SoE rules during service delivery, reinforcing that units must protect SoE at all times so that they never drop below the minimum SoE requirement for both import and export. Compliance will be assessed on the basis of a unit maintaining its SoE within an allowed range, rather than how much energy is deliberately recovered per settlement period. Units must maintain a minimum capability to deliver the service.

The original proposal consulted on by the ESO included 5 changes that covered prescriptive energy recovery requirements, capabilities and actions to recover energy, when Response Units must have contracted response energy volumes and what happens when providers have made every effort to abide by the SoE rules but no longer have the contracted MW during service delivery.

A majority of respondents supported this change, though several highlighted areas of ambiguity and uncertainty across all 5 changes and concerns around compliance and enforcement. The ESO have since added further clarity in response to this feedback.

The main revision between consultation with industry and submission to Ofgem is the shift towards SoE management rules maintaining an acceptable SoE level rather than providing a prescriptive energy recover requirement. Units' compliance will be assessed on their ability to maintain SoE within an allowed range, aligning the T&C closer to the policy intent than the original proposal. The ESO also clarified their intent on SoE management across successive service periods, and have noted that stacking bids and substantive service delivery can create challenges in managing SoE across service periods. We expect NESO to work with providers to better understand the likelihood of these scenarios emerging.

We approve this submission and note that NESO will publish additional guidance which aims to provide worked examples and further clarity for providers. We expect that this will be published alongside the Service Terms. We also expect NESO to monitor the results of this change going forwards, and have been assured that the capability to do so is already in place.

Enforcement of this submission takes effect from 1 February 2025. Whilst we do not support grace periods in general, we understand that this grace period is intended to allow providers a chance to understand and make adjustments to comply with the Service Terms as there have been amendments between what was shared in the consultation and what was submitted to Ofgem. We expect BSPs / BRPs to comply with the T&C once these are

published and once any adjustments have been made to allow for this, regardless of whether NESO enforce against these immediately.

#### 4. SoE rule – Submitting sell orders

This proposal looks to formalise the percentage amounts of offered quantity that providers should reserve in their sell orders in order to manage SoE effectively by including it in the Procurement Rules. Currently, these quantity percentages are only included in guidance. The intent for providers is that they must not submit sell orders with offered quantities that would prevent SoE management. Therefore providers must reserve (not include in offered quantity) sufficient capacity in their unit that allows them to manage their SoE in accordance with the SoE management rules.

Respondents were all supportive of the change, though one was concerned that the numbers showed a preference for two hour duration batteries. NESO have stated they do not consider their proposal favours longer duration batteries as these figures focus on capacity rather than duration but will keep these figures under review.

We approve this update to the Procurement Rules as it improves NESO's ability to maintain system security, and provides them with assurance that the service paid for is available. We note that NESO have committed to publishing additional worked examples in the Guidance document alongside the updated T&C. We expect this to improve clarity and understanding for industry.

#### 5. Requiring operational metering and operational baselines at all times

This proposal will require providers to submit both operational metering and operational baselines at all times, not just for periods when they are contracted. This change mainly affects non-Balancing Mechanism Units ("non-BMU"), as Balancing Mechanism Units ("BMU") already submit this data in accordance with the Grid Code.

Respondents were mostly in favour, though there was opposition to the change. This opposition mainly centered on not understanding the rationale for this change, but also suggested that non-BMUs would be disproportionately affected due to the different cost drivers for these units compared with BMUs. We note that the ESO held further engagement with respondents on this matter, and have clarified the proposed terms do not provide for enforcing adherence to background submission of baselines. Furthermore, the ESO have clarified in detail the rationale for change in their submission to us, addressing concerns raised by respondents.

We reject this change to the Procurement Rules because the text under section 6A does not align with the intent submitted by the ESO, and the change itself has an unknown implementation date. We note that the original consultation for this change states that the ESO “do not intend that this requirement would be effective until a date specified by the ESO.” This intent was correctly written into the submitted Procurement Rules under section 6A. However, in the subsequent submission to us, the ESO stated they “do not intend to enforce this requirement until a date...”, but that the change itself will be live upon publication of the new Procurement Rules. The text under section 6A remains the same as consulted on, and does not account for the fact that it is only *enforcement* that doesn’t commence on publication of the updated T&C.

Whilst we have no issues with the policy itself, due to a lack of clarity around the timeframe for implementation and enforcement and the mismatch between the intent in the submission to Ofgem and the wording in the Procurement Rules, we cannot approve this submission in its current form. It is in consumer interest that the T&Cs contain clear and accurate rules and requirements for BSPs / BRPs. We encourage NESO to submit a proposal for this change once they are clear on implementation timeframes.

#### 6. Penalty Reform and Unit Suspension

This proposal seeks to introduce a new penalty regime to address instances of non-compliance through a progressive series of actions. The ESO have stated that this will allow them to provide more effective and proportionate deterrents against non-compliance.

A majority of respondents were in favour of this submission, though many provided feedback to the ESO seeking further clarity on monitoring, reporting, appeals and the rationale behind the severity of the penalties. Whilst the ESO covered several points in their submission to us, we note that NESO have committed to providing additional guidance and further transparency to address all feedback going forwards.

We reject this submission on the grounds that the date of implementation is unknown. Whilst we found no issue with the idea of a tiered penalty regime, and understand the rationale and changes put forwards by the ESO, we do not support unknown implementation dates, nor changes that come into effect too far in the future. We have sought clarity from NESO on an implementation date and have been told that significant work still remains before implementation, but consultation feedback has provided valuable input to support development. We encourage NESO to submit a proposal for this change once it is clear when it will go live.

#### 7. Disarming and re-arming instructions outside contracted service periods

This proposal will enable NESO to send instructions to service providers to disarm or re-arm outside of contracted service periods so that the instruction is effective from the start of the next contracted service period.

Almost all respondents were in favour of this change, though many asked for a lead time before implementation to be introduced to allow them to update their IT to accommodate.

We approve this change, considering it introduces flexibility to the control room through the ability to send an instruction at the point where a security case to disarm / re-arm is identified prior to the start of service periods. For clarity, this requirement goes live once the updated T&C is published, but enforcement of this requirement will begin on 1 May 2025. Whilst we do not support grace periods in general, we understand that the intent for this delay will allow BSPs / BRPs to carry out any necessary development work prior to enforcement. We expect BSPs / BRPs to comply with the T&C once these are published and once any developments have been made to allow for this, regardless of whether NESO enforce against these immediately.

#### 8. Maximum sell size

This proposal will increase the maximum sell size that can be submitted for DR and DM from 50MW to 100MW, in line with the existing DC limit. The intent is to remove any optimisation barriers for large assets, and reduce complexity by aligning maximum sell sizes across all Dynamic Services.

A majority of respondents were in favour of this change, though we note that several wanted it increased further to 300MW. The ESO stated that this limit cannot be increased further due to the procured volumes in DM and DR, and that they didn't want a large proportion of this volume to be contracted to one unit. Furthermore, having response spread around the country leads to better performance when responding to faults.

We approve this change, and are satisfied with the comments the ESO provided against consultation responses.

#### 9. Zero Deadband for non-energy limited assets

This proposal enables non-energy limited Response Units to nominate a Zero Deadband, encouraging a wider range of technology types to participate in Dynamic Services. Currently, synchronous, non-energy limited units cannot adhere to the deadband provision as it's currently written due to technical capabilities. This prevents them participating in these markets.



Respondents to this consultation either supported the proposal or did not state their position. As such, we assume that no respondents opposed the change, but those that did not explicitly state their support abstained from sharing their position either way. Some respondents suggested that this change did not meet the policy intent due to response time requirements remaining a barrier. The ESO recognised this issue, and have stated that prospective participants will need to demonstrate capability to provide the service. Whilst we understand that this remains a barrier, enabling even one additional participant into the market is of positive value to consumers.

We approve this proposal, and note that NESO have confirmed through further engagement with Ofgem that this provision will be enabled from 1 February 2025. Therefore this change will not be implemented immediately, but we expect NESO to give notice in writing to Registered Auction Participants before implementation, as committed to in the Procurement Rules. This submission is the only approved submission that will not be implemented on publication of the updated T&C, but will come into effect from 1 February 2025.

#### 10. Transfer: pay secondary provider

This proposal enables NESO to transfer availability payments to secondary providers where there is a transfer of response contract.

Almost all respondents were supportive of the change. We note that the ESO responded to a point of feedback from one respondent, which asked for NESO to allow transfers to more than one unit, and are satisfied with the ESO's rationale for not taking that feedback on board in this submission.

We approve this change, noting that NESO has welcomed further discussion with stakeholders to explore the possibility of allowing transfers to more than one unit.

#### 11. Updates to Schedule 3

The ESO consulted on three changes under this submission:

- 1) Settlement formula – updated to accurately reflect the penalties for negatively priced bids.
- 2) Metered Response formula – updated to separate the performance calculation when delivering high or low frequency services in bi-directional contracts.
- 3) Switching from unavailable to available in bundled services – clarification on switching from unavailable to available in bundled services and the grace period given to these.

Almost all respondents were supportive of each change. We are satisfied with the ESO's responses to the feedback provided by respondents, and note that this feedback has led to amendments in the submission to Ofgem.

We approve this submission, and agree that these changes bring clarity to their respective areas. NESO have committed to working with industry on change 3 to better understand technical challenges to this for certain participants.

#### 12. Other housekeeping changes

We approve the housekeeping changes proposed by the ESO and agree that these add clarity and aid understanding for industry.

### **Our decision**

We are approving the following submissions:

1. Removal of Maximum Ramp Rate
2. Availability description
3. State of Energy ("SoE") management rules – During service delivery
4. SoE rule – Submitting sell orders
7. Disarming and re-arming instructions outside contracted service periods
8. Maximum sell size
9. Zero Deadband for non-energy limited assets (change implemented from 1 February 2025)
10. Transfer: pay secondary provider
11. Updates to Schedule 3
12. Other housekeeping changes

We are rejecting submission 5 'Requiring operational metering and operational baselines at all times' and submission 6 'Penalty Reform and Unit Suspension'. We believe both these submissions are positive changes, and found no issue with the policy intent behind them. But the lack of a clear implementation and / or enforcement date as well as the mismatch between the intent in the submission to Ofgem and the wording in the Procurement Rules in submission 5, leaves too much ambiguity and uncertainty for both Ofgem and BSPs / BRPs.

Considering our rationale above, we conclude that the ESO's proposal meets the requirements of Article 18 of the EBGL Regulation. Therefore, for the approved submissions, we confirm that the Response Services Procurement Rules and Response

Services Service Terms as mapped by the ESO forms part of T&C pursuant to Article 18 of the EBGL Regulation.

### **Next steps**

We encourage NESO to publish the revised documents consulted on as soon as practical. We note that NESO have committed to publishing an additional guidance document that covers a variety of the changes submitted to us. We expect that this gets published alongside the revised Service Terms and Procurement Rules.

NESO has stated an intent to provide grace periods of varying length for submissions 3, 5 and 7, and are aiming to provide notice to industry before starting enforcement. We do not generally support grace periods and encourage NESO to begin enforcement as soon as is practicable. In future we expect NESO to have the capability to monitor and enforce the rules from the date of implementation. Our approval of these amendments signifies that these clauses are now in effect and we expect BSPs / BRPs to comply with all approved clauses from the date of this letter, except for submission 9, which will be implemented from 1 February 2025.

If you have any queries regarding the information contained in this letter, please contact Matthew Fovargue ([matthew.fovargue@ofgem.gov.uk](mailto:matthew.fovargue@ofgem.gov.uk)) in the first instance.

Yours faithfully,

**Adam Gilham**

Head of National Energy System Operator Regulation

For and on behalf of the Gas and Electricity Markets Authority.