

# Electricity System Operator Performance Panel

## Working Paper

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### Overview:

In order to improve how the Electricity System Operator (ESO) manages the changing electricity system in consumers' interests, we have introduced a new regulatory and incentives framework. The incentive scheme has changed from a mechanistic ex-ante scheme limited primarily to short-term balancing costs, to an evaluative ex-post scheme covering the ESO's full range of short and long-term responsibilities. The new scheme came into effect from April 2018.

Feedback from, and engagement with, a broad range of stakeholders will be key to ensuring the new scheme functions as intended and the ESO is effectively incentivised to deliver good outcomes.

Both Ofgem and the ESO will seek feedback on an ongoing basis to help support this, and to ensure stakeholders have a clear voice in holding the ESO to account. Furthermore, as a central part of the new scheme, we will establish an independent panel of experts, who will assess the ESO's performance and provide recommendations to Ofgem on whether any incentive payments or penalties should be paid. This working paper provides an update on the setup of this new Performance Panel, and invites trade bodies and industry associations to nominate a voluntary representative to be part of the Panel.

## Associated documents

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Ofgem, [Policy Decision on the Electricity System Operator Regulatory and Incentives Framework from April 2018](#), February 2018

Ofgem, [ESO Roles and Principles Guidance Document – Version 2.0](#), February 2018

Ofgem, [ESO incentives – Notice of proposed modifications to the special conditions of the electricity transmission licence held by NGET](#), February 2018

Ofgem, [Decision to modify NGET’s licence to introduce new ESO reporting and incentives arrangements from April 2018](#), March 2018

Ofgem, [The Electricity System Operator Reporting and Incentives \(ESORI\) Arrangements: Guidance Document](#), March 2018



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## Executive Summary

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Our rapidly changing energy system needs an Electricity System Operator (ESO) that proactively responds to system challenges and maximises consumer benefits across the full spectrum of its roles. We need the ESO to work more closely with its stakeholders and other energy sector parties to ensure there is a coordinated approach to system operation and planning. We also want a more dynamic ESO that readily responds and adapts to new developments.

To ensure this is the case, we introduced a new ESO incentives framework from April 2018. One of our key aims for the new framework is to facilitate more external involvement than previously. We want to pool the knowledge and experience of a wide array of industry parties and independent experts in order to comprehensively challenge the ESO on its performance. This is vital for tackling the information asymmetry between the ESO and ourselves.

A central part of the new scheme is an independent panel of experts, who will assess the ESO's performance and provide recommendations to Ofgem on whether any incentive payments or penalties should be paid. We put forward an outline of how the Performance Panel would function in our February 2018 decision on the ESO regulatory and incentives framework. This paper builds on this outline, providing an update on the setup of the Panel, including its structure and funding, our expectations of Panel members, and how Panel meetings would be conducted.

The Performance Panel (the Panel) would meet with the ESO at three key points during the annual cycle – to challenge the ESO on its forward plans at the start of the year, and at mid-year and end of year to evaluate its performance. Following the end of year review, the Panel would produce an evaluation report explaining its view of the ESO's performance, scored against up-front evaluation criteria. This report would form a recommendation to the Gas and Electricity Markets Authority (the Authority), who would then make the decision on any financial reward or penalty, up to a maximum cap and floor of  $\pm\text{£}30\text{m}$ .

The Panel should not be seen as a substitute for wider stakeholder input. The ESO's wider stakeholder community would provide vital input throughout the performance year.

The high-level framework for the Panel we propose in this working paper is as follows:

- The Panel will be a mix of independent experts recruited by Ofgem and voluntary industry representatives.
- The Panel will be chaired by Ofgem initially and eventually by an independent chair.
- The Panel will meet three times in an annual cycle – around the forward plan, mid-year and end-year review.
- Panel meetings to have open and closed sessions.



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- Panel members to commit a minimum of 6 days and up to 10 days.
- Ofgem to act as the secretariat.
- The Panel will be funded by Ofgem in the first year.

With the publication of this working paper, we invite voluntary nominations for industry representatives on the panel. Trade bodies and industry associations interested in nominating a representative for the Panel are requested to submit the form in Appendix 1 by 17<sup>th</sup> August 2018 to [ESOperformance@ofgem.gov.uk](mailto:ESOperformance@ofgem.gov.uk)

We will commence the recruitment process for independent representatives in early August. To ensure consumer views are robustly represented we will seek a representative from consumer groups. We welcome stakeholder views as to whether we should seek other additional consumer representatives for the Panel.

We will keep the structure and administration of the Panel under review during the first year, and we will make any necessary refinements along the way.

Following the publication of this working paper, we will continue work to put the Performance Panel in place for the first Mid-Year Review in November 2018. We do not expect stakeholders to formally respond to this working paper. However, we welcome stakeholder views and if there are particular comments you would like to share with us, please send us an email at [ESOperformance@ofgem.gov.uk](mailto:ESOperformance@ofgem.gov.uk)

# 1. The ESO Performance Panel

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## A) Purpose and Role

1.1. We have introduced a new incentive regime for the ESO - changing it from a mechanistic ex-ante scheme to an evaluative ex-post scheme - from April 2018. The scheme now relies on the assessment of an independent panel of experts to assess the ESO's performance, prior to Ofgem making a decision on whether any incentive payments or penalties should be paid.

1.2. This new panel would support the evaluative process. It provides industry with a platform to hold the ESO to account and adds greater transparency to the incentives decision-making process. It also acts to reduce the information asymmetry between the ESO and Ofgem.

1.3. As outlined in our final decision on the ESO regulatory and incentives framework<sup>1</sup>, the Performance Panel will act in an advisory capacity to help inform the Authority's decision-making process in respect of the ESO incentive scheme. In particular, the Panel of independent experts and industry representatives would play a key role in challenging and providing feedback on the ESO's forward plan and within-year performance (including through a 'Mid-Year Review' meeting). At the end of the year, the Performance Panel would evaluate the ESO's performance in relation to each principle using predefined evaluation criteria. This evaluation would form a performance 'scorecard'.

1.4. The score awarded by the Panel will act as a recommendation, which the Authority will consider when making a decision to financially reward or penalise the ESO up to a maximum cap and floor of  $\pm$ £30m.

1.5. The Authority commits to fully considering and taking into account the Panel's views and giving them due weight in the deliberation process, but will not be obliged to act on the recommendations made by the Panel. The final decision on incentive payment or penalty would be informed by the Performance Panel's recommendations, but would ultimately be taken by the Authority.

## B) Membership

1.6. We proposed earlier that the preferred membership structure would be a mix of independents and industry representatives.

1.7. We had set out our belief that an independent chair would be more likely to encourage panel members to take an appropriate level of ownership of the

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<sup>1</sup> Ofgem, [Policy decision on the Electricity System Operator regulatory and incentives framework from April 2018](#), February 2018

Performance Panel's activities. However, as this is a new framework, we proposed that Ofgem would act as chair initially to help guide the process. We could then potentially transition to an independent chair once the panel is more established.

1.8. Our current thinking on the composition of the Performance Panel remains the same as in our final decision. The Panel will be comprised of around seven voting members and a non-voting Chair; each referred to as a 'Panel Member' and together referred to as 'Panel Members'. The Panel will be a mix of voluntary industry representatives, consumer representatives and independent experts recruited by Ofgem. We envisage that the industry representatives could include generators, network operators, large demand users and emerging technology businesses.

1.9. Having representatives from a wide array of industry parties and organisations with help to comprehensively challenge the ESO on its performance. We expect the independent experts to bring a range of relevant experience, potentially from abroad or from other sectors. We expect to appoint 1-4 independent experts (depending on the quality of applications received). The industry representatives will be chosen to cover the broad spectrum of different industry participants and will bring more detailed knowledge on specific areas of the ESO's performance that year.

1.10. The Panel will be chaired by an Ofgem employee (Senior Civil Service level) for the first 3 panel meetings. We would review the success of these first few meetings and consider if the arrangements are established enough to transition to an independent chair.

1.11. The tenure of the membership will be fixed and we expect to review panel membership every 2 years. However, we aim to make consistent improvements to the functioning of the Panel and will make changes where appropriate – this may have an impact on the make up of the Panel.

### **C) Selection Process**

1.12. The Panel will be made up of independent experts and industry representatives.

1.13. The independent experts will be hired on merit through fair and open competition. The process would follow Ofgem's standard recruitment principles and appointed members will receive suitable remuneration.

1.14. We invite nominations from trade bodies and industry associations who would be interested in voluntarily representing the views of a particular stakeholder group such as generators, emerging technologies and large users. Those who are interested should submit a completed version of the form in Appendix 1 by 17<sup>th</sup> August to [ESOperformance@ofgem.gov.uk](mailto:ESOperformance@ofgem.gov.uk)

1.15. When filling the form in Appendix 1, please explain the process that will be followed in choosing the representative to sit on the Panel. Once a representative has been nominated, substitutes will be allowed only under exceptional circumstances.

1.16. The voluntary nominations received would be sifted by Ofgem. The primary criteria of sifting is to ensure that a wide spectrum of stakeholders are represented. If we receive nominations from two trade bodies representing the same stakeholder group, we will select the nomination which provides better evidence of eligibility in the form in Appendix 1.

1.17. To ensure consumer views are robustly represented we will seek a representative from consumer groups. We welcome stakeholder views as to whether we should seek other additional consumer representatives for the Panel.

## **D) Secretariat**

1.18. Ofgem staff will act as secretariat for the Panel. The secretariat will be responsible for:

- Coordinating with the Panel members and ESO.
- Organising the Panel meetings.
- Preparing relevant papers and reports.

1.19. The Secretariat will take notes at each Panel meeting and prepare the draft report. The draft report would then be circulated among the Panel members for comments and modifications. Once the draft report is approved by all the Panel members, it will be submitted by the Panel to the Authority for consideration as part of its decision on rewards or penalties.

## **E) Panel Members**

### **Role**

1.20. As outlined in the Final decision, the role of the Panel Member in a given year is to:

- In January/February (from 2019/20 onwards): provide its views on the scope and level of ambition of the ESO's Forward Plan, deliverables and performance metrics.
- In October: challenge the ESO and provide feedback on its performance as part of a Mid-Year Review.
- In June: perform an end of year evaluation of the ESO's performance during the previous year, and score the ESO for each of its Principles against the predefined scoring criteria.

1.21. To carry out this role effectively, Panel Members will be expected to liaise with the secretariat (for example to help manage time commitments).

1.22. The role of the Chair is to chair the ESO Performance Panel. This will involve:

- chairing Panel meetings.



- ensuring the Panel makes its recommendations according to the evaluation criteria.

### **Time commitment**

1.23. Approximately two days per year will be required from each Panel Member, for each Panel meeting. We intend to hold three Panel meetings (one each discussing the forward plan, mid-year performance and end of year performance). Panel members will be required to attend the all-day Panel meetings at Ofgem's London offices (10 South Colonnade, Canary Wharf, London E14 4PU). We would also expect Panel members to be available for an hour briefing session with Ofgem via teleconference before each of the Panel meetings.

1.24. In addition to the three Panel days, Panel Members are expected to spend time reviewing the evidence and submissions and preparing for the Panel meetings. We expect a maximum of 10 working days per year will be required from each Panel Member. This will depend on the volume and nature of submissions made by the ESO.

### **F) Panel meetings**

1.25. The daylong Panel meetings would comprise of 2 sessions. The morning session would be an open session where members of the public can attend and view proceedings. In this session of the Forward Plan meeting, the ESO would explain their planned deliverables and proposed performance metrics. For the mid and end of year review panel meetings, the ESO would present evidence on their performance for the relevant period. The Panel and members of the public would get an opportunity to provide feedback on performance and question the ESO in this session. The open session will make the incentives process more transparent. It will enable the wider stakeholder community to engage with the Panel and ESO easily.

1.26. The post-lunch session would be a closed-door session comprising two sections. In the first section, not attended by the ESO, the Panel will assess the submissions and evidence presented by the ESO. This will allow for a free exchange of views between the Panel members. In the next section attended by the ESO, the Panel could ask for further information or evidence if required. The ESO also gets another opportunity to present any additional information before the Panel makes its final recommendation.

1.27. Members of the public or ESO's stakeholders who are keen to attend this session will need to inform Ofgem and book their place in advance. Stakeholders interested in attending the Panel meetings should email Ofgem at [ESOperformance@ofgem.gov.uk](mailto:ESOperformance@ofgem.gov.uk) according to the timetable provided below. Ofgem would then get in touch with interested stakeholders regarding date, venue and registration for the meeting.

## Tentative Timetable of Panel Meetings

	Forward Plan review meeting	Mid-year review meeting	End of Year review meeting
Deadline for report/evidence submission by ESO	End of January	Mid October	Early May
Review/consultation period	4 weeks	2 weeks	4 weeks
Registration deadline for Open session	Mid February	Mid October	Mid May
Tentative meeting date	Early March	Mid November	June

## G) Evaluation Criteria

1.28. ESO Performance Panel will score the performance of the ESO in accordance with the guidance and criteria set out in the ESORI Arrangements Guidance Document<sup>2</sup>.

1.29. If the Panel members do not agree on the scores to be awarded, the voting exercise would determine the final scores. If the votes are equally distributed then the Chair would have the final say.

## I) Panel Funding

1.30. In the year 2018-19, the Panel will be funded by Ofgem.

1.31. We had earlier proposed that the panel would be funded through BSUoS charges through a pass-through in the ESO's licence. We will keep this option under review as the Panel develops.

## F) Conflicts of interest

1.32. Before involvement with the ESO Performance Panel, Panel Members would ensure that there are no conflicts of interest that, in the opinion of a fair-minded and well-informed observer, would suggest a real possibility of bias.

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<sup>2</sup> Ofgem, [The Electricity System Operator Reporting and Incentive Arrangements: Guidance Document](#), March 2018



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1.33. If a Panel Member has a direct or indirect interest which may be material or relevant, they should declare that interest to the secretariat, who may refer for a view to the Chair of the ESO Performance Panel.

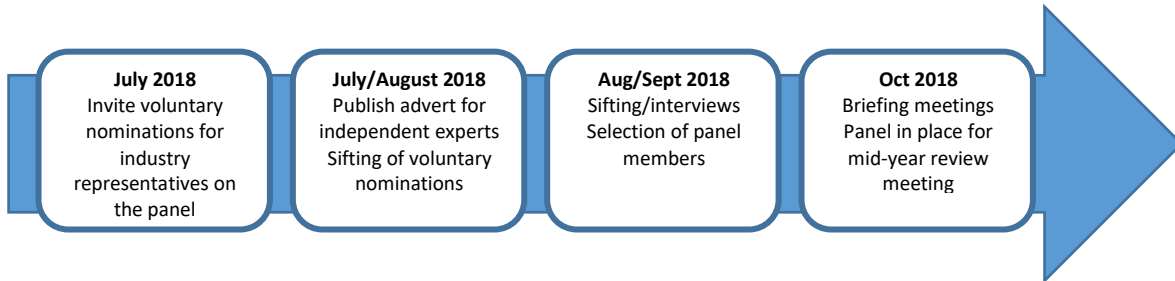
1.34. Panel members are expected to make every effort to represent views of the industry as a whole and not any single organisation.

## 2. Next steps

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2.1. Our timelines are built on having the Panel in place for the first mid-year review meeting in November 2018. To meet this timeline, our immediate next steps are focused around selection and appointment of panel members.

*Figure 1: Next steps*



2.2. With the publication of this working paper, we invite voluntary nominations for industry representatives on the panel. Trade bodies and industry associations interested in nominating a representative for the Panel are requested to submit the form in Appendix 1 by 17<sup>th</sup> August 2018 to [ESOperformance@ofgem.gov.uk](mailto:ESOperformance@ofgem.gov.uk)

2.3. When completing the form, please provide evidence on why the trade body or association is best suited to represent the views of one or more stakeholder groups of the ESO.

2.4. The voluntary nominations received will be sifted by Ofgem to ensure that different stakeholder groups are sufficiently represented.

2.5. We will publish adverts for a selection of independent experts in July/August 2018. This process will follow Ofgem's standard recruitment principles.

2.6. We plan to finalise the members of the Panel by September 2018.

2.7. The first mid-year review meeting will be held in November 2018 and stakeholders interested in attending the open session of the meeting should email [ESOperformance@ofgem.gov.uk](mailto:ESOperformance@ofgem.gov.uk) by 15<sup>th</sup> October 2018 to register their attendance. Ofgem will provide details on the date, venue and registration process in due course.



# Appendices

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## Appendix 1 – Nomination Form

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### Nomination Form

The information requested here will help us to understand the organisation's suitability in evaluating the performance of the ESO.

1. Name of the organisation
2. Brief description of role and purpose of the organisation (Please stay within 300 words)
3. Date the organisation was established (dd/mm/yyyy)
4. Registered Office Address
5. Head office address (if different from the registered office address)
6. Name and contact details of the CEO (or equivalent)
7. Contact details of the person we will get in touch with about this application
8. How many members does the organisation have in total?
9. Please provide a summary of the services provided by the organisation's members and the sectors within which the members operate (please stay within 300 words)
10. List of stakeholder groups you propose to represent at the Panel
11. Please provide a summary of the process you propose to follow when selecting a representative to sit on the Panel on your behalf (please stay within 300 words)
12. How will the organisation ensure that its advocacy or representation role will not cause any conflict of interest between advocating on behalf of its members, and in evaluating the ESO's performance (please stay within 300 words)