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Dear Louise

Call for input on 2019-20 ESO Regulatory and Incentives Framework

This response is from SP Transmission (SPT), the onshore transmission owner for the South of Scotland. As a key stakeholder of the ESO, we welcome the opportunity to share our views on the 2019-20 Regulatory and Incentives Framework for the ESO.

We accept Ofgem's position that given the new ESO Framework was only introduced in April this year, it is premature to make fundamental changes to the scheme. We have therefore focused our views primarily on some of the key areas highlighted in Ofgem's call for input document.

The ESO Roles and Principles

At the Ofgem led ESO Mid-Year Review Open Session on the 20th November, the lack of evidence of how the GB electricity system is performing was a significant gap. The current ESO roles lack an explicit directive to ensure the security of supply in GB and this should be addressed going forward. We would therefore suggest that an additional role should be included or the existing role 1, "*Managing system balance and operability*", should be updated appropriately. It is incumbent on Ofgem to ensure the Regulatory Framework incentivises the ESO to meet the challenge of the energy transition, including the broad aspects of decarbonisation, decentralisation and digitalisation. It is inadequate that only one specific action on system security is listed, out of the twenty that comprise the Forward Plan Technical Annexe. This demonstrates there is a fundamental lack of focus in the existing Framework to incentivise this critical aspect of the ESO's role.

For example, the scope of the current ESO incentive does not include Black Start arrangements, which has seen high value contracts placed in this area¹. These contracts emphasise the need for increased transparency, and some form of metric and reporting to be included going forward. These

¹ <https://utilityweek.co.uk/national-grid-spent-113m-on-black-start-contracts-with-drax-and-sse/>

contracts also demonstrate the ESO is not always fast enough in recognising the issues that political and economic circumstances are introducing to industry and consumers alike, and to promote resolution of policy/ leadership gaps. Industry and consumers are therefore left with cost and risk (supply security). The ESO Regulatory Framework needs to incentivise the ESO to react to the rapidly changing environment and deal with risk, and reflect reducing costs and risks for consumers. The recent outcome of the Capacity Market² determination is further evidence of the significant challenge this presents. Ofgem and the Challenge Panel need to take cognisance of this. The possibility of early closures of large nuclear generation in the South of Scotland and North of England reinforces the need that the ESO need to be addressing this in their Forward Plan and reporting.

The Forward Plan process

We continue to hold the view that the current Regulatory Framework encourages a Forward Plan that can be over reaching and could detract the ESO from focusing on its day to day activities. For example, we have highlighted the opportunity for the ESO to develop a world-leading position in GB in power system modelling that facilitates competition. The ESO can take the lead in defining the models to overcome challenges such as confidentiality issues. This would give the industry as a whole, including TOs and alternative providers, the tools they need to propose solutions³. We have also highlighted, improvements to the transmission connections offer process, outage communication, support for single circuit connections and implementing the SO-TO funding mechanism to reduce whole system costs for outages⁴. These opportunities are entirely absent from the current Forward Plan and there is no evidence that they are being addressed.

The ESO Framework process should incentivise the ESO to develop metrics that drive the correct industry behaviour and are delivering the greatest benefits for consumers. It is not clear yet how the Framework is ensuring consumer benefit is being delivered through the current set of metrics or activities. Neither is it clear if system performance and security is improving, deteriorating or at risk if the credible future energy scenarios materialise. The ESO needs to develop appropriate metrics to evidence these parameters. A balanced scorecard approach would be appropriate.

The Forward Plan is fundamental to the new Regulatory and Incentives Framework for the ESO. It is important that this Plan is accurate and achievable to maximise consumer benefits across the full breadth of its activities. Given the importance of this Plan, stakeholders must be given sufficient time to consider, comment and challenge the proposals put forward by the ESO for its next Forward Plan.

In terms of transparency, we support Ofgem's suggestion that the ESO should report on its internal resources, highlighting how they may change in the coming year. Given the legal separation of the

² <https://www.gov.uk/government/collections/electricity-market-reform-capacity-market>

³ ESO Network Development Road Map Consultation_SPT response _final

⁴ 2018-03-05 SP Transmission response to ESO forward plan submission

ESO, we consider it appropriate that stakeholders get the opportunity to share views on whether the ESO is prioritising its internal funding on the right areas.

Given the significant reorganisation changes that the ESO is currently embarking on, we are keen that the ESO sufficiently communicates details of this reorganisation to stakeholders, and more importantly, how this reorganisation will impact on delivery of the Forward Plan. As a key stakeholder of the ESO, we would have expected much greater communication from the ESO on the extent and nature of this reorganisation.

Within-year reporting requirements

Given the ESO's remit to provide value to consumers, we would also expect to see specific details of additional consumer benefits the ESO is delivering against each of its deliverables, at both the Mid-Year and End-Year Review processes. The balanced scorecard approach, recommended above, should be adopted.

The Mid-Year Review and Panel Processes

We are supportive of the Mid-Year Review and ESO Performance Panel processes followed this year, and feel there is balanced representation on the Panel itself. We recommend that the Panel, and stakeholders alike, are provided with a 2-3 page high level monthly progress scorecard or update which builds up to the Mid-Year Review report and Final year-end report. The scorecard or update would not form part of any assessment but would be a tool to aide stakeholder engagement and understanding, without having to review the considerable number of documents which have been published by the ESO. Not only will this further increase transparency, it will also ensure that the ESO is afforded the opportunity to demonstrate its ongoing performance on a regular basis and is not relying on a 'big bang' approach, twice a year, to justify its performance.

The volume of documents published, associated with this incentive, makes it difficult for Panel Members and stakeholders to identify the relevant and important information in relation to the ESO's performance. This does not meet the ESO's Principle 1 to *"Support market participants to make informed decision by providing user-friendly, comprehensive and accurate information"*. We hope that the information made available can be streamlined and more suitably presented to Panel Members and stakeholders in future.

The Evaluation Process and financial incentives parameters

Ofgem have explained that the new Regulatory and Incentives Framework for the ESO is intended to apply "a more 'principles-based' approach to ESO regulation and moves away from the use of targeted mechanistic incentives, towards a broader, evaluative incentives approach. It aims to create

a much more proactive and outcome-focussed ESO, and encourages it to work flexibly with its stakeholders in order to maximise consumer benefits across the full spectrum of its activities.”⁵

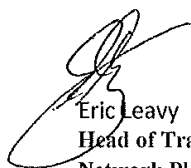
We fully support this direction of travel and consider it a more appropriate approach that reflects the increasing complexity and pace of change in the energy sector generally, and electricity network, specifically.

Incentive Payment/ penalty reconciliation licence change

The ESO’s proposals to allow the difference between its incentive forecasts, and the final incentive value, to be reconciled through adjustment to charges in the following year seems appropriate as this should benefit consumers in relation to reducing an element of the uncertainty in forecasting BSUoS charges.

Should you have any questions in relation to this response, please do not hesitate to contact me.

Yours sincerely,



Eric Leavy
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SP Energy Networks

⁵ Call for input on 2019-20 ESO regulatory and incentives framework October 2018