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Louise van Rensburg
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Dear Louise,

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

We are pleased to respond to your call for evidence on potential improvements to the Electricity System Operator (ESO) regulatory and incentives framework and a proposed licence change aimed at reducing BSUoS charge uncertainty. SP Energy Networks is responding separately from its perspective as the onshore Transmission Owner for the South of Scotland.

Potential improvements before the 2019-20 scheme

We accept that before making any fundamental changes the ESO framework it needs to be allowed more time to bed in. However, in order to ensure that an economic, efficient, and co-ordinated electricity system is delivered, we believe incremental changes should be made to the guidance, the level of detail within the roadmaps, and the metrics around progress milestones. Our proposed changes below are aimed at making the information and data provided by the ESO more meaningful and easier to interpret in order to facilitate competition in the provision of services.

Proposed changes to the ESO Roles and Principles Guidance Document

Paragraph 1.27 of the 'ESO Roles and Principles' guidance states, *"We think the ESO could achieve 1.26 above by publishing on its website the high-level approach it takes to procure balancing services, including an explanation for the preferred make-up of the portfolio of products, the associated timeframe and reasoning for restrictions applying to each. We would expect the ESO to follow this approach for each contract entered into. If requested by the Authority, the ESO should be able to show clear documentation and if necessary justification of any deviation from this approach".*

This current guidance means that:

1. The ESO does not need to publish a detailed hedging strategy for balancing services, on the basis that it is considered commercially sensitive. However, we believe that this restriction goes beyond what could reasonably be justified on grounds of commercial sensitivity. It would promote competition and therefore benefit consumers if potential providers understand the risks the ESO is seeking to manage through its procurement of balancing services.

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2. In our view there remains limited transparency in the decision making process for accepting Balancing Mechanisms (BM) bids or offers. Industry is not given any insights into the full criteria for decisions taken by the Control Room, or retrospective information on the rationale underpinning bids and offers accepted. We believe more transparency in this area would promote competition in bid and offer prices. It would also increase the accountability of the ESO for the decisions it takes in the BM.

3. The price paid by the ESO for certain balancing services (including spinning reserve) is not published. We believe that the price paid for all services should be disclosed to aid competition from new entrants and to compel the ESO to develop competitive markets for service provision.

Accordingly we propose that paragraph 1.27 of the guidance should be amended as follows (changes highlighted in red):

> *"We think the ESO could achieve 1.26 above by publishing on its website the ~~high-level~~ detailed approach it takes to procure balancing services, including the strategy, the price paid and the location of all balancing and ancillary services, and an explanation for the preferred make-up of the portfolio of products, the associated timeframe and reasoning for restrictions applying to each. We would expect the ESO to follow this approach for each contract entered into. If requested by the Authority, the ESO should be able to show clear documentation and if necessary justification of any deviation from this approach".*

A possible exception to the above may need to be made for the procurement of black start services. The previous BSIS scheme of announcing the total pot available to National Grid put it at a disadvantage in negotiations with the very limited number of service providers in each black start zone. In our view, National Grid has not been innovative or forward thinking enough in developing a market for black start service provision, but greater transparency is still necessary where there is a well-functioning market in the relevant balancing service product.

Implementing the above amendment may require the removal of some confidentiality clauses within a number of balancing and ancillary service contracts. However, we believe that the administrative effort in doing so would be justified by the consumer benefits resulting from enhanced competition. We would be happy to discuss further where we believe greater transparency could lead to consumer benefits.

Roadmaps and milestone design

We welcome the publication of product roadmaps in the Future of Balancing Services project. These publications have given us an understanding of how the Balancing Market(s) may develop. However, the framework and performance metrics should ensure that the roadmaps contain sufficient detail to for us to engage meaningfully on the steps the ESO is taking to develop a competitive balancing services market for the future.

The performance metrics around the milestones should be designed to ensure they capture sufficiently any consumer detriment from sizeable drifts from the original timescales and solutions proposed. As an example, the Frequency Response roadmap indicated that the Frequency Response Auction Trial was supposed to commence in Q4 2018. However, the ESO has delayed the start until June 2019 as a result of complications in picking the right platform provider for the auction.

Forecasting accuracy

While the publication of new future forecasts (including demand and Balancing Service Use of System (BSUoS) charges) is useful, the accuracy of these forecasts is vital if they are to deliver consumer benefits. In our view, the 20% BSUoS accuracy range sets a rather low bar for an organisation that has been forecasting these charges for the last 14 years, and needs to be revisited.

The Forward Plan

We are pleased that the ESO started the process of engaging with its stakeholders about the 2019/20 plan earlier this year. We also support Ofgem's suggestion that the ESO should report on its internal resources. 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.

Within-year reporting requirements

Given the ESO's remit to provide value to consumers, we would expect to see estimates of the additional consumer benefits the ESO is delivering against each of its deliverables, at both the Mid-Year and End-Year Review processes. This consumer benefit metric should form part of an overall balanced scorecard type approach.

The Mid-Year Review and Performance Panel processes

To allow the Performance Panel and other stakeholders (that may be feeding into trade association representatives) to manage their time effectively, we propose that the ESO produces 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 should be designed to allow for areas of under- and over-performance to be identified quickly. Thinking about the scorecard now would also be an effective way of identifying gaps in the evidence and data the Performance Panel will require. It would facilitate a more structured request for information from the ESO.

Incentive payment/penalty reconciliation licence change (BSUoS)

We welcome the proposal for any differences between the incentive value recovered by the ESO from market participants and the final incentive value determined by Ofgem to be reconciled in Settlement Final bills for the Relevant Year t+1. We support Ofgem's view that this would benefit consumers by reducing the risk of unexpected BSUoS deviations and therefore market participants' risk premiums. We agree that this change is unlikely to have a significant detrimental impact on the cost reflectivity of charges.

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

Yours sincerely,

Richard Sweet
Head of Regulatory Policy