

Decision

Adjustments to the Electricity Market Reform Delivery Body Allowances

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We are deciding on adjustments to allowances for National Grid Electricity System Operator to fulfil its role as the Delivery Body for Electricity Market Reform. These allowance adjustments apply only to the period April 2016 to March 2021 and are based on the RIIO (Revenue = Incentives + Innovation + Outputs) price control model and relate to the efficient delivery of additional requirements requested of the Delivery Body.

According to National Grid Electricity System Operator's Licence Special Condition 7D, we have made this decision using information submitted to us by National Grid Electricity System Operator and responses to our consultation on our proposals which ran from 13 August 2019 to 10 September 2019.

This document outlines our original proposals, key themes from the responses to our consultation and our decision including any implications of this decision. We also set out our proposals for a mechanism to deal with future uncertainty in Delivery Body funding requirements for this period.

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Executive summary

Overview

In August 2014 the Government appointed the National Grid Electricity System Operator (NGESO) as Electricity Market Reform (EMR) Delivery Body (DB) to deliver the Capacity Market (CM) and Contracts for Difference (CfDs) regimes. Ofgem is responsible for setting the allowances and incentives for this NGESO function as well as overseeing the delivery performance. We aim to ensure that the DB are sufficiently funded to deliver this crucial role for the GB energy system to a level of excellent performance.

In line with the regulation of network companies, we are applying the principles of the RIIO (Revenue = Incentives + Innovation + Outputs) price control framework to drive benefits for consumers in relation to EMR. Under this framework, the onus is on regulated companies to demonstrate the cost-efficiency and long-term value for money of their business plans through proposing funding, outputs (or deliverables) and, where appropriate, incentives.

In September 2015¹, we decided on funding for the DB for the period April 2016 to March 2021. However, we recognised that the EMR framework may evolve during this period, hence an Uncertainty Mechanism (UM) was introduced into NGESO's Licence in Special Condition 7D.10(b). This allowed NGESO to submit an application for additional funding for specific activities required to manage this change. According to Special Condition 7D.12(b), we must determine any adjustments to allowed expenditure by the end of September 2019.

We accept that the CM in particular has evolved since April 2016 and consider this UM an opportunity to provide additional allowances for activities not included in the 2015 decision. NGESO submitted information to us in May and June 2019 which we assessed and developed our proposals for adjustments to allowances. We published our consultation on proposed allowance adjustments on the 13 August 2019 which ran until 10 September 2019.

No additional allowances were proposed to be provided to deliver the core EMR role, observing that the DB could outperform their allowances over this total period by managing future spend in the Total Expenditure (TOTEX) consideration. In addition, due to the historical underspend against allowances on OPEX and reduced forward spend on the current Information Technology (IT) administration system, the 'Portal', it was anticipated

¹ [Decision on revenue, outputs and incentives for NGET plc's roles in Electricity Market Reform](#)

that the EMR DB could increase spend on resources, thereby improving service provision to market participants.

We proposed to allow additional allowances of £9.36m² for NGESO to fulfil the role of EMR DB for the period April 2016 to March 2021 out of a total of £17.11m requested. We proposed to provide £7.36m for justifiable and efficient historical investment in the Portal. Recognising the continuing critical feedback on the functionality and flexibility to change of the Portal, we also proposed to allow £2m initially out of an estimated £2m to £5m cost to develop a replacement IT administration system by April 2021. We also intended to include a future UM to allow the DB to claim necessary additional costs where justified and efficient.

Consultation and Decision

We received 10 consultation responses from industry and EMR Delivery Partners, broadly in favour of our proposals. A response was also submitted by the DB in which they disagreed with several aspects of our proposals.

Most respondents raised the issue of the DB not delivering its core services to the expected standard; with many encountering challenges and issues. Many felt that increasing resource spending would lead to a higher level of service. The DB stated that they are finding the most efficient solution across Operational Expenditure (OPEX) and Capital Expenditure (CAPEX) to deliver the outputs defined in their business plan and have continuously delivered improvements and efficiencies that have enabled them to keep OPEX relatively stable, but that there was no headroom for increased OPEX within the proposed allowance adjustment. We confirm that we will not adjust TOTEX allowances for the core EMR role and encourage the DB to increase OPEX spend if appropriate to deliver the requested service to EMR applicants.

Responses from industry broadly agreed with Ofgem's assessment of spend on the Portal, including the scope of assessment and application of an efficiency measure due to the high level of spend that is not reflected in an improvement to the quality and services of the Portal. The DB disagreed with our assessment of spend on the Portal, submitting further evidence to explain why historic spend was related to new requirements not originally set out in the initial funding decision. In response to this additional evidence, we have decided to include further allowances for investment in the Portal totalling £0.45m, incurred in Summer 2019, to deliver necessary policy driven investment. We think other requests for inclusion of further allowances were included in the scope of the core EMR role and hence

² All values shown in this document are in 2014/15 prices

cannot be justified. Therefore, the total allowances provided to the DB to cover increased spend on the Portal total £7.81m.

A number of responses agreed that continuing to upgrade the existing Portal may not reflect value for money, however they also highlight the need for the system to retain functionality for current users. The DB support the proposal to avoid additional regulatory changes that would require implementation in the Portal, however they highlight that minimising change risks the ability to undertake any urgent additional changes being delivered in response to any changes required in light of the European Commission's decision on CM State aid approval, or to maintain service to market users, as well as the cost of any future change. We remain of the view that further changes to the portal now would not offer value for money, we will not provide any additional funding associated with this IT system. However, we do recognise the potential for urgent policy changes which may require investment in the Portal in order to implement and would expect full communication between EMR Delivery Partners and BEIS regarding triggering any further investment. We proposed to deal with such changes through the future UM.

A number of respondents welcomed the proposed step change in functionality, user experience and flexibility that should be achieved by a replacement IT administration system by April 2021 and agreed that the DB should prioritise this work. Many responses reflected a firmly held desire that the scope and design of the new IT system must be managed efficiently, well-directed and consulted on with industry and stakeholders with a strong focus on user experience. Some respondents expressed their concerns with the DB, as part of ESO, delivering the replacement IT system and recommended that the DB should explore other contractual and technological solutions. The DB agreed that, as far as possible, priority should be given to the replacement IT system. We therefore maintain our proposal to provide additional allowances of initially £2m to deliver the replacement IT administration system by April 2021. We also recognise the views from industry and therefore expect the DB to fully engage with stakeholders and explore alternative solutions to deliver this solution and will monitor progress in this area carefully. Furthermore, we will monitor the process that the DB takes to delivering the replacement IT system and encourage the DB to focus on user experience and flexibility to future policy change.

Several industry responses agreed with having a future UM given that the total cost to deliver the replacement IT system is uncertain. The DB welcomed the proposal of a future UM, however they requested that it should not be limited to the system refresh, and to allow the DB to recover any other additional efficient spend. As a result of uncertainty in both policy change and associated with the delivery of a new IT system in the remainder of this allowance period, we recognise the need for the DB to collect additional costs and will consult on applying a further UM into NGENSO's licence to complete at the end of this

regulatory period. We expect the DB to be economic and efficient with in any future investment in the Portal and to employ manual processes to avoid system change where possible, consulting with Ofgem on any additional costs and potential risks going forward. Furthermore, the future UM will apply only to spend from October 2019 to March 2021. For the provision of additional costs associated with the replacement IT system, we will seek feedback from system stakeholders and consider evidence of effective delivery against requirements.

Next Steps

As a consequence of this decision we will adjust allowances by £9.81m over the period April 2016 to March 2021, applying to current and historical spend on the existing IT administration system, the Portal and the delivery of a replacement IT administration system by April 2021. Adjustments to the allowed revenues will now take place through the usual processes.

We will continue to work closely with the DB to drive performance and value for money. Ofgem are also considering the appropriate future funding approach for the wider NGESO from April 2021 and will include allowances and incentives for the EMR DB in this consideration.

1. Introduction

What is this decision on?

Background

- 1.1. The National Grid Electricity System Operator (NGESO) undertakes the role of administering the Electricity Market Reform (EMR) policy initiatives. EMR aims to provide allowances for renewable technologies via the Contracts for Difference (CfDs) framework, and sufficient generation via the Capacity Market (CM). This NGESO function is defined as the Delivery Body (DB). In order to achieve this role, NGESO employs a team of staff and a number of Information Technology (IT) systems are either managed in house or licences paid for.
- 1.2. Ofgem regulates these schemes to deliver secure decarbonisation at the lowest cost. A key aspect of this regulation is to set appropriate allowances for NGESO to deliver their EMR function efficiently and effectively. In January 2015, the DB submitted a Business Plan to outline costs associated with delivering EMR from April 2014 to March 2021. In September 2015, following consultation, we published our decision³ on allowances, outputs and incentives for this period. This decision provided fixed allowances of £12.7m to cover costs up to March 2016 and £33.7m for the remainder of the period.
- 1.3. It was acknowledged that there was significant uncertainty in the role of the EMR DB when allowances were set in 2015. A number of areas were identified where additional cost may be required during the period April 2016 to March 2021. These included specific and high impact changes to the CM and CfD regimes as well as the delivery of an IT system replacement. We had concerns around the provision of upfront sums to NGESO to fund scope changes that might not happen as this could provide windfall gains. To address this, we included a UM to deal with costs that may arise from specific areas of change or DB outputs during the period but are uncertain at this time. Special Condition 7D of the NGESO's Licence sets out the arrangements and criteria for seeking an adjustment to allowances in May 2019 (under 7D.10).

³ See Related Publications

- 1.4. Since 2015, the management and operation of the CM has seen extensive change due to changes in the number and type of participants as well as framework changes. The CM has evolved from a market of large projects from established energy market participants to a greater proportion of smaller projects from less established energy market participants; significantly increasing the complexity and resource effort required from the DB. In addition, framework changes to the CM Regulations⁴ and Rules⁵ that have been implemented by Ofgem and the Department for Business, Energy & Industrial Strategy (BEIS) have also increased the complexity of the DB role. An annual rule change process has been conducted by Ofgem and packages of regime changes have been consulted on and implemented by DECC/BEIS. A supplementary CM Auction has been required to be held, however conversely a much reduced number of CfD Allocation Rounds have been held.
- 1.5. In 2019 the pace of change has continued with disruption caused by the suspension of the CM whilst a further investigation to provide State Aid clearance is undertaken by the European Commission. In addition, BEIS and Ofgem have undertaken Five Year Reviews on the CM framework as planned.
- 1.6. In our decision letter of September 2015, Ofgem acknowledged that “It is difficult to specify exactly in advance what ‘major changes in the scope of EMR’ would be and what Ofgem would give written approval to”. Consequently, this UM, to be determined in summer 2019/20, could be used as a ‘light touch’ review of additional costs incurred up to that point in respect of major changes in the scope of EMR not included in the current allowances. We also outlined that we would expect each change to be sufficiently substantive so as to have been subject to discussion (and possibly consultation) with DECC/BEIS, Ofgem and industry stakeholders prior to implementation. The cost of these major changes (in aggregate) should be in excess of the existing de-minimis amount of £1.2m as included in Special Licence Condition 7D.7. Furthermore, any submission for additional allowances would be considered on a case-by-case basis.
- 1.7. This UM was implemented through a licence change to Special Condition 7D.10 (b) of NGESO’s Licence. According to this licence condition, a submission for additional

⁴ [The Electricity Capacity Regulations 2014](#); [The Contracts for Difference \(Allocation\) Regulations 2014](#)

⁵ [Capacity Market Rules](#); [Contracts for Difference Allocation Framework](#)

allowances was received by the 31st May 2019 and an Ofgem Decision is required to be made by 30th September 2019 following consultation.

1.8. The following Decision document therefore sets out our determination on adjustments to ESO's allowances to carry out the EMR DB role over the period April 2016 to March 2021 based upon the RIIO price control model, where justified and efficient. Our decision was achieved through considering all items of additional allowance requests as follows:

- Each request must have been justified as additional to the core role of the DB for which they are already funded;
- Each request was considered on a case by case basis;
- The efficiency of the delivery of change was considered;
- Taking industry feedback into account.

1.9. As well as providing additional funding, this allowance adjustment assessment seeks to drive continuous improvement in the efficiency and performance of the DB. Recent industry feedback has highlighted issues with the Portal and that improvements should be prioritised in areas of the EMR processes, particularly relating to prequalification to the CM.

Our decision making process

1.10. We received a submission from the NGESO on the 31 May 2019 and further requests for information were made over June 2019. In this submission, additional allowances of £17.1m was requested to cover the total difference between original allowances of £33.7m and anticipated total spend of £50.8m over the period.

1.11. Spend on existing IT systems was significantly increased by £17.86m, while OPEX, primarily for resources, was reduced by £5.75m over the period. In addition, a range of £2m to £5m was outlined in order to replace the current IT system, the Portal, to deliver a step change in functionality, user experience and adaptability by April 2021.

1.12. In August 2019, following the submission from the NGESO, we consulted on our proposals to adjust allowances to fulfil its role as the DB for EMR. We proposed to

allow £7.36m to cover costs associated with investments to the EMR Portal and £2m to allow the EMR DB to begin scoping and delivering the replacement IT system.

1.13. Our consultation closed on the 10th September 2019.

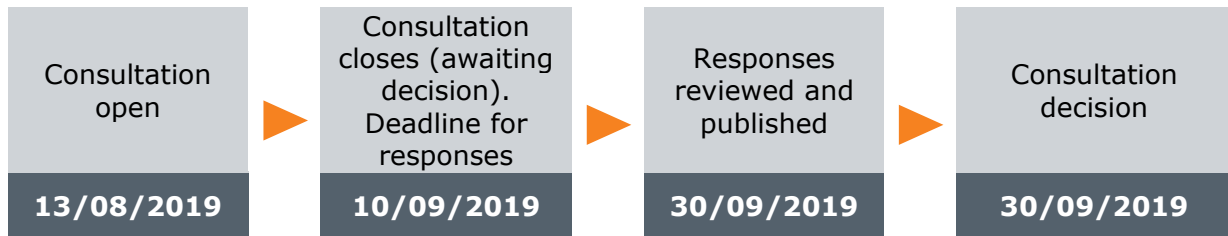


Figure 1: Decision-making stages

1.14. In total, we received 11 responses. Nine responses were from industry participants, one was from another Delivery Partner in EMR and one from the DB. Two responses were marked as confidential and all others can be found on our website.

1.15. In this document, we outline our specific proposals based upon the assessment of the DB’s requests for additional allowances alongside relevant specific feedback from our consultation. We then set out our decisions, and any implications. All cost values referred to in this consultation are in 2014/15 prices. This relates to the financial year of the original EMR DB Business Plan.

Related publications

Allowances and Uncertainty Mechanism Provision

Consultation on proposals for adjustments to allowances (August 2019):

https://www.ofgem.gov.uk/system/files/docs/2019/08/consultation_on_proposals_for_adjustments_to_revenues_for_the_emr_delivery_body.final_.pdf

Previous allowances/ incentive consultation (April 2015):

<https://www.ofgem.gov.uk/publications-and-updates/consultation-initial-proposals-setting-revenue-outputs-and-incentives-national-grid-electricity-transmission-plc-s-roles-electricity-market-reform>

Decision on allowances and incentives (September 2015):

<https://www.ofgem.gov.uk/publications-and-updates/decision-revenue-outputs-and-incentives-nget-plc-s-roles-electricity-market-reform>

Consultation on licence change to include reopener clause (September 2015):

<https://www.ofgem.gov.uk/publications-and-updates/statutory-consultation-proposed-licence-modifications-nget-s-special-condition-7d>

Decision on licence change to include reopener clause (October 2015):

<https://www.ofgem.gov.uk/publications-and-updates/decisions-modifications-nget-s-special-licence-conditions-4a-4l-and-7d-nget-plc-s-roles-electricity-market-reform>

Annual Performance Reports on the EMR Delivery Body in relation to the Capacity Market

2018: <https://www.ofgem.gov.uk/publications-and-updates/annual-report-delivery-body-s-performance-its-functions-relation-capacity-market>

2017: <https://www.ofgem.gov.uk/publications-and-updates/report-emr-delivery-body-s-performance-its-functions-relation-capacity-market-1>

2016: <https://www.ofgem.gov.uk/publications-and-updates/report-emr-delivery-body-s-performance-its-functions-relation-capacity-market-0>

Ofgem’s Five year Review Report (July 2019): <https://www.ofgem.gov.uk/publications-and-updates/report-our-five-year-review-capacity-market-rules-and-forward-work-plan>

Your feedback

General feedback

1.16. We believe that consultation is at the heart of good policy development. We are keen to receive your comments about this report. We’d also like to get your answers to these questions:

1. Do you have any comments about the overall quality of this document?
2. Do you have any comments about its tone and content?
3. Was it easy to read and understand? Or could it have been better written?
4. Are its conclusions balanced?
5. Did it make reasoned recommendations?
6. Any further comments?

Please send any general feedback comments to stakeholders@ofgem.gov.uk

2. Proposals and Consultation

Section summary

This section outlines our proposals for additional allowances based upon the assessment of NGENSO's additional allowance requests. Also included are the general issues raised by industry in response to our consultation document.

We outline our proposals and consultation responses in the main categories of spend of the Core EMR Role, IT CAPEX on the Portal and IT CAPEX to develop and deliver a replacement IT System.

Core EMR Role

Our Proposals

- 2.1. The DB have received TOTEX funding, covering the core EMR role based on expectations in 2015. Therefore, no additional allowances were proposed to be provided to deliver the core EMR role including both OPEX and CAPEX categories.
- 2.2. As previously stated in our consultation, it is expected that in the context of a high level and pace of change and complexity in the policy framework and market, an excellent service to applicants should be maintained. We previously demonstrated that over the period from April 2016 to March 2021, overall OPEX appeared to be a saving of £2.49m below allowances.
- 2.3. We identified scope to increase spend on OPEX if it were to provide an improved service to EMR applicants and to manage challenges that are likely to continue, such as facilitating the entry of new inexperienced applicants, delivering policy change and improving processes.
- 2.4. We therefore proposed that the DB should utilise some of the £2.49m projected OPEX saving over the period to improve service levels to EMR applicants.
- 2.5. We also outlined that no additional allowances would be provided for items of IT CAPEX spend that are related to the core role of EMR such as system improvements for user experience and compliance assurance.

Questions

Question 1: Do you agree with the consideration of TOTEX for the core role and exclusion from additional revenues?

Question 5: Do you feel that there is a basis for increased spend on resource by the DB in order to maintain a high level of service to applicants and why?

Consultation Responses

- 2.6. Respondents agreed with the principle of TOTEX spend across OPEX and CAPEX, and that the EMR DB should not be provided additional funds to carry out the core role as envisaged and funded for in 2015.
- 2.7. A number of respondents commented that there is basis for increased spend on resource to provide a higher level of service to applicants. Most respondents raised the issue of the DB not delivering its core services well; an example provided was issues during the CM prequalification process. A particular response noted the expectation for consistent specialist knowledge from the DB. In particular, they have witnessed a high turnover of staff leading to a lack of understanding that has eroded confidence in the EMR DB. The issue of the DB's resource allocation was raised a number of time, with emphasis on providing an improved service to market participants and value for money from the service.
- 2.8. The DB responded by stating that they have managed spend on a TOTEX basis, finding the most efficient solution across OPEX and CAPEX to deliver the outputs defined in their business plan. Additionally, they noted that they have continuously delivered improvements and efficiencies that have enabled them to keep OPEX relatively stable.
- 2.9. The DB added that the rule changes required by BEIS and Ofgem for 2019/20 will result in an overspend against combined CAPEX allowance for the remaining two years; thus leaving no headroom for increased OPEX if allowances are not adjusted accordingly. Without sufficient headroom, the DB state they would be unable to outperform without pushing further above the proposed allowances.

IT System CAPEX – EMR Portal

Our Proposals

- 2.10. The DB requested additional allowances of £1.52m to cover the continuing build of the Portal in 2016/17. It was proposed that no additional funding would be provided as this was already funded prior to April 2016 through a previous allowance decision.
- 2.11. The DB requested additional allowances for items of system spend associated with policy and externally driven changes. This request was a total of £8m of potential additional allowances.
- 2.12. Based on an assessment of average system development 'day rate' costs, we identified the DB was approximately 8% higher than reasonable industry standards. We therefore suggested an 8% efficiency measure be applied to the total £8m requested, to represent an apparent inefficiency of delivery through the DB's system development contract. This resulted in a recommended allowance reduction of £0.64m and a proposed total allowance for IT CAPEX on the existing Portal of £7.36m.
- 2.13. To avoid further inefficient spend, it was proposed that given the high cost of change, no further policy driven changes should be delivered in the existing Portal. However, we proposed that any significant urgent policy changes that impact pre-agreed DB costs would be considered under the proposed future UM.

Questions

Question 2: Do you agree with Ofgem's assessment of spend on the administration system (the 'Portal')?

Question 3: Do you have any opinion on the level of ESO spend on the current administration system (the 'Portal')? Please explain these views.

Question 7: Do you agree that the change implemented in the current administration Portal should be minimised to ensure value for money?

Consultation Responses

- 2.14. Numerous responses agreed with Ofgem's assessment of spend on the Portal, noting that the DB was funded for the complete build of the Portal prior to April 2016.

- 2.15. Additionally, a number of respondents stated that the performance of the Portal has been poor and the system has not been meeting the needs of its users. The poor performance of the Portal has been especially noted during the prequalification window where IT systems have been running exceptionally slowly along with system delays.
- 2.16. Many of the responses highlight the issue of the high expenditure on IT CAPEX against allowances; with a number of responses stating the level of spend has not been reflected in an improvement to the quality and services of the Portal.
- 2.17. A number of responses agreed that continuing to upgrade the existing Portal may not reflect value for money. Many state that additional allowances to bring changes to the existing Portal should only be provided if the benefits to its users outweigh the cost. Furthermore, many highlight the need for sufficient financial provisions to remain in place to ensure continued usability of the system for current users and to avoid and detrimental stress events.
- 2.18. Respondents have noted that the Rules and Policy framework is too complex and unclear with the need to review the CM Rules and Regulations to simplify and provide clarity. Also stated is that this has impacted the effectiveness, and may have impacted the efficiency, of historical system change.
- 2.19. A Delivery Partner outlined that a number of system changes are expected to be delivered to the Portal in order to be able to fully implement and automate rule change OF12. They have stated that manual workarounds, with associated costs will be required and that financial risk applies to these workarounds.
- 2.20. The DB disagreed with our assessment of spend on the Portal, requesting that we reconsider our assessment in a number of areas:
- **Continuing to build the system in 2016/17:** The DB stated that whilst the original business plan anticipated that the bulk of the system build would be delivered during 2015/16, the DB were required to deliver significant changes in Rules and additional requirements during that period. This led to a re-profile of the work programme and thus delaying the initial build to free up capacity to implement the rule changes during 2015/16 and early 2016/17.

- **Those system changes which Ofgem have considered to be ‘out of scope’ (included in the core EMR role):** The DB has highlighted changes to the EMR portal that they considered to be over and above their core role:
 - Some changes were due to a larger than expected increase in the number and nature of EMR participants and also the need for greater additional cyber security provisions due to the changing nature and scale of cyber threats since the introduction of EMR.
 - Some historical system changes were required in response to requests from the DB’s Delivery Partners. The DB note that these changes were necessary as the Delivery Partners had not confirmed their requirements when the Portal needed to be built, or the Delivery Partners asked for later changes as they continued to develop their processes.
 - Some rule changes and new requirements were introduced under a disrupted delivery process. The disruption caused by continuing rule changes meant that, in some cases, solutions had to be delivered that met minimum requirements but then required further changes later on.
 - Some changes previously identified as general improvements are distinctly policy driven and the DB are committed to CAPEX spend to deliver during 2019/20. These specifically related to rule change OF12 and interaction with other Delivery Partners. In relation to our proposal that the DB are able to outperform against current allowances, the DB suggest that these commitments, driven by BEIS and Ofgem requirements, leave no opportunity to outperform.
- **The 8% efficiency measure:** The DB state that the assessment did not fully take into account the circumstances and changing requirements in which they had to develop the EMR portal. The DB therefore deemed it inappropriate to compare the EMR system development to an ‘average system development’ cost.

2.21. The DB support the proposal by Ofgem and BEIS to avoid additional regulatory changes that would need to be implemented in the current EMR portal. However, the DB have raised their concerns regarding minimising change to the current Portal, highlighting the issues regarding this:

- There are a number of remaining requests from Delivery Partners for changes to the system to fully implement rule change OF12 (relating to 2.20).

- Minimising change to the Portal will risk any additional changes being delivered in response to a European Commission decision on CM State Aid clearance, and the delivery of any urgent changes required to maintain service to market users.
- Reducing change capacity on the Portal to zero would mean that no additional change could be delivered, and there could be mobilisation impact in terms of cost and time, should further changes become necessary.

IT System Capex – Replacement IT System

Our Proposals

- 2.22. Recognising the critical feedback on the functionality of the existing Portal, the DB, with appropriate funding in place, has committed to delivering a replacement IT administration system by April 2021. It was proposed that additional allowances of £2m be allowed at this stage to cover the base cost of delivering the new system.
- 2.23. As further changes to the existing Portal are not cost effective, we proposed that the DB should prioritise the replacement IT administration system to bring about a step change in functionality and flexibility that is required by market users.

Questions

Question 6: Do you agree that the priority should be achieving a step change in IT system functionality and change implemented in the current administration Portal should be minimised in order that this happens by April 2021?

Consultation Responses

- 2.24. Many responses welcomed the commitment of the DB to deliver a replacement IT administration system to achieve a step change improvement by April 2021 and our proposal that they should prioritise this work. Respondents emphasised the need for delivery of this system by April 2021 to avoid any implications with late delivery.
- 2.25. Further, a number of respondents agreed with prioritising a step change in IT system functionality, but without risking the usability of the existing portal and any urgent changes that are required.

- 2.26. Many respondents strongly state that the scope and design of the new IT system must be managed efficiently, well-directed and consulted on with industry and stakeholders throughout with a strong focus on user experience.
- 2.27. A number of parties expressed their concerns with the DB, as part of ESO, delivering the new replacement IT system. Some recommended that the DB should explore other solutions including innovative contractual and technology solutions (e.g. emerging flexibility platforms).
- 2.28. The DB agreed that, as far as possible, priority should be given to the replacement IT system and that change in the existing portal should be minimised where appropriate. They have also stated that the step change improvement should be outcome based and not prescribed to a particular solution.

Future Uncertainty Mechanism

Our Proposals

- 2.29. Recognising that the total cost to deliver the replacement IT system is uncertain, a future UM was proposed to assess any additional efficiently incurred costs.
- 2.30. It was also proposed that any significant urgent policy changes that impact pre-agreed DB costs would also be considered under the proposed future UM.

Questions

Question 8: Do you agree with a future uncertainty mechanism to account for the uncertainty in developing a new IS administration system?

Consultation Responses

- 2.31. Several industry responses agreed with having a future UM given that the total cost to deliver the replacement IT system is uncertain.
- 2.32. A number of stakeholders stated their desire to be able to have a say in further system changes to the Portal which would be considered in a future UM to maintain functionality.

2.33. The DB welcomed the proposal of a future UM, however they requested that it should not be limited to the system refresh, and allow the DB to recover any additional efficient spend.

Application of additional allowances

Our Proposals

2.34. We demonstrated the application of allowance adjustments in each year 2016/17 to 2020/21.

Consultation Responses

2.35. Some industry respondents commented that it is necessary for Ofgem to set out how these additional allowances would be applied and therefore the impact to market participants.

2.36. In addition, clarification was requested on when the additional allowances would be recovered.

3. Decisions and Implications

- 3.1. According to the principles set out in the Consultation, we do not feel that providing further allowances where items of spend were foreseeable in 2015 and within the anticipated scope of the EMR role is justified.

Core EMR Role

- 3.2. As set out in our Consultation document, with the intention of this being a light touch review, this allowance adjustment does not seek to adjust TOTEX spend for the core EMR role and therefore we are not minded to reopen OPEX spend. We maintain this view following consultation.
- 3.3. However, recognising that the DB is below spend against allowances and considering consultation responses received, we encourage the DB to utilise some of the £2.49m projected OPEX saving over the period to improve service levels to EMR applicants.
- 3.4. Also, unless otherwise stated, we will not provide additional allowances associated with spend on the Portal viewed to be consistent with the core role of the EMR DB.

IT System CAPEX – EMR Portal

- 3.5. The DB has challenged the inclusion of a number of areas of historical spend on the Portal within the core EMR DB role. We consider these items of spend were foreseeable in 2015 and within the anticipated scope of the EMR role. This is applicable to:
- Additional allowances for parts of the initial build which had to be delayed due to regulatory change. As previously explained in the Consultation document, the DB has been funded for build of the Portal prior to April 2016 as per the September 2015 decision document and no further allowances will be provided.
 - The core EMR DB role for which funding has been provided. The DB has identified 'change in circumstances' such as the 'larger than expected increase in the number of EMR participants' and 'changing nature and scale of cyber security threats since the introduction of EMR' as items above this core role. They have also identified 'New/ Changing Delivery Partner requests' to embed known processes. Allowances were provided in September 2015 to fund

reasonably expected system improvements, hence no additional allowances will be provided.

- The DB has also identified a 'Disrupted Delivery Process' as driving a cost increase in system investment. The direct cost impact of this is not clear from the DB's additional detail submission with their consultation response. Furthermore, the process for rule change implementation and time available for general system improvements was apparent when the September 2015 decision was made. Consequently, we will not be providing additional funding to cover this category of spend.

3.6. We also consider the 8% efficiency measure applied to spend on the Portal as appropriate. The response from the DB does not contain sufficient evidence to adjust our consideration that the level of spend on IT development is above what would be reasonably expected. Some responses from market participants were supportive of the application of this measure stating the investment in the system did not represent value for money.

3.7. We recognise that the scope and cost of some system changes associated with implementing the Rule change OF12 that were developed and implemented over Summer 2019 was not available to be able to be included in the original DB submission. The additional submission received outlining the scope and cost of these system changes justifies this spend in sufficient detail for us to be able to consider providing allowances. The DB has detailed £0.489m of additional cost associated with these changes and the necessity to implement them for a Delivery Partner to be able to carry out their processes. Consistent with all additional allowances for the EMR Portal, an efficiency measure of 8% will be applied.

3.8. A number of further system changes have been identified as required in order to fully automate settlement processes for Rule Change OF12 in the EMR Portal. We recognise a Delivery Partners request for the completion of these system changes and the need for manual workarounds and increased risk until implemented. It is apparent that the cost associated with the workarounds is far exceeded by the cost of delivering this system investment in the Portal. Therefore, considering cost effectiveness, we will not be providing additional allowances to cover this investment. We anticipate that any financial impact that comes about from this risk would be collected through the normal revenue collection process for the Delivery Partner. We also expect these processes to be fully automated in the replacement IT system to be delivered in April 2021.

- 3.9. In this decision, due to the poor value for money associated with change to the EMR Portal, we therefore will not provide any additional funding associated with this IT system going forward. However, we do recognise the potential for urgent policy changes which may require investment in the EMR Portal in order to implement. Should any system changes be essential to retain functionality and implement urgent policy change, we would expect communication between Delivery Partners and the DB to demonstrate the costs associated with these changes to enable validation of the value for money of any further investment. Ofgem will not consider further allowances for any investment the Portal that has not been discussed and agreed.
- 3.10. Therefore, the total allowances provided to the DB to cover increased spend on the EMR Portal total £7.81m. This allowance adjustment will apply to the year in which it was spend by the DB as shown in Table 1.

IT System Capex – Replacement IT System

- 3.11. Having considered all comments in the consultation responses associated with a replacement IT administration system, we recognise the strong desire for a step change in system functionality and user experience and consider that providing £2m initial allowance to the DB to deliver this solution is appropriate.
- 3.12. However, we are conscious that a number of respondents commented on the lack confidence they have in the DB as part of NGENSO delivering a usable and adaptable system in time and to good value. We therefore expect the DB to explore alternative solutions to deliver this requirement including utilising wider industry parties and service providers to provide innovative and good value technology solutions. We will monitor progress in this area carefully. In order to achieve the outcomes in the required timescales, the replacement system should be delivered by April 2021 in advance of the CM prequalification process. This will enable Delivery Partners to coordinate interacting processes and all EMR applicants to familiarise themselves with any new user interfaces in advance of CM prequalification.
- 3.13. We will also monitor closely user and Delivery Partner involvement in the design and development of the replacement IT system. We are aware of the frustration with some industry parties in the lack of usability of the DB's and wider ESO systems. Therefore, we encourage the DB when developing the replacement system to focus on user needs to enable ease of access to the CfD and CM regimes.

3.14. Policy and market change is expected to continue across EMR, therefore the replacement IT system should be highly flexible and be able to react in a timely and efficient manner to necessary change requirements.

3.15. These additional allowances will apply in 2020/21 as shown in Table 1.

Future Uncertainty

3.16. As a result of both policy uncertainty in the remainder of this allowance period and associated with the delivery of a new IT system, we recognise the need for the DB to collect these additional costs.

3.17. Although the timing of a future UM window is challenging, we anticipate additional costs will be certain and the DB can make an application for these costs by late 2020. We will assess and consult on this submission for further allowances and make a decision in advance of the end of the regulatory period.

3.18. To manage remaining policy uncertainty, a consideration of cost effectiveness should be taken and further investment on the Portal made only where economic and efficient. As such, we expect the DB to minimise any system change and to employ manual processes where appropriate. We expect the DB to consult with Ofgem regarding any further system change to the Portal and any expected additional costs.

3.19. Costs associated with the replacement IT administration system should be communicated to Ofgem during development. In particular, Ofgem should be alerted to any escalation beyond the £2 to £5m range or potential delay in delivery. We will seek feedback from system users and consider evidence of effective delivery against requirements with any future allowance provision.

Application of additional allowances

3.20. These additional allowances will be applied in the year incurred by the DB as shown in Table 1. Adjustments to allowances will commence in 2020/21. The total additional allowances applied in each year will be added to the Balancing Services

Use of System (BSUoS)⁶ total and charged to industry on the basis of usage of the system (in MWh).

- 3.21. Indicatively, should this total £9.81m be recovered from both generation and demand within one year across a total annual electricity system usage of 300TWh, it will have an increase on BSUoS charges of around £0.02/MWh.

Table 1- Total adjusted EMR Delivery Body allowances

All figures in 2014/15 prices	2017	2018	2019	2020	2021	TOTAL
Allowances	7.15	6.80	6.68	6.66	6.41	33.70
Decision on adjustment to allowances	2.39	2.26	1.06	2.10	2.00	9.81
Adjusted allowances	9.54	9.06	7.74	8.76	8.41	43.51

⁶ [Balancing Services Use of System \(BSUoS\) charges](#)

4. Conclusion and next steps

- 4.1. This document sets out our determination on adjustments to allowances for NGESO to carry out the role of EMR DB. We take into account submitted information by the EMR DB and responses to our consultation in coming to this decision.
- 4.2. We will adjust allowances by £7.81m applying to current and historical spend on the existing IT administration system, the 'Portal' and by £2m to deliver a replacement IT administration system by April 2021. Reconciliation of historical allowances will now take place through the usual processes and future allowances applied to the appropriate years for collection through BSUoS charging.
- 4.3. In addition, we have decided to apply a further UM at the end of the RIIO-T1 price control period. We will need to apply text to the NGESO licence in order for this to be formally in place and hence we will now carry out a Licence Change process including consultation. We would anticipate that this licence change is in place by the start of the 2020/21 financial year.
- 4.4. We will continue to work closely with the DB to drive performance and value for money. In particular, we will monitor any further spend on the Portal and the process to develop the replacement IT administration system, including consideration of alternative approaches and full engagement with industry.
- 4.5. Ofgem are considering the appropriate allowances and funding mechanisms for the wider NGESO and will include allowances and incentives for the EMR DB in this consideration. We will also consider the removal of the data sharing 'ring fence' around the EMR DB in order to achieve greater efficiency of working with the rest of NGESO.
- 4.6. Furthermore, we recognise the feedback from this consultation that there is a need to simplify and provide clarity to the Rule and Policy framework. Our report on the Five Year Review, and the forward work plan included, sets out our strategy for changing the Rules and regulatory framework to reduce both complexity and regulatory burden. We will continue to deliver on our forward work plan⁷ and to work closely with BEIS in implementing any necessary policy changes.

⁷ [Report on our Five Year Review of the Capacity Market Rules and Forward Work Plan](#)

Appendix 1 – Abbreviation definitions

In order of appearance:

NGESO: National Grid Electricity System Operator

EMR: Electricity Market Reform

DB: Delivery Body

CM: Capacity Market

CfDs: Contracts for Difference

RIIO: Revenue, Incentives, Outputs

UM: Uncertainty Mechanism

OPEX: Operational Expenditure

CAPEX: Capital Expenditure

TOTEX: Total Expenditure

IT: Information Technology

BEIS: Department for Business, Energy & Industrial Strategy

DECC: Department for Energy & Climate Change

BSUoS: Balancing Services Use of System