
10 South Colonnade
Canary Wharf
London
E14 4PU

Kayte.O'Neill@nationalgridso.com
07769 643 146
www.nationalgrideso.com

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Call for input on 2020-21 ESO regulatory and incentives framework

Dear Maryam,

We welcome the opportunity to comment on the 2020-21 ESO regulatory and incentives framework. We support many of the changes which have been proposed and we have provided feedback on some specific points below. There are some items which we think need to be considered further where we have proposed some changes and details of these points and our proposals can be seen in the appendix to this letter.

Our understanding is that these changes would be introduced for the 2020-21 scheme year, and therefore would be applicable to the 2020-21 Forward Plan publication in March 2020, but not to the 2019-20 End of Year Report which will be produced in May 2020. It would be helpful if Ofgem could clarify this upfront in both the Roles and Principles document, and the ESORI guidance document.

We acknowledge that the ESO incentives scheme is still in the process of evolving, with both the ESO and Ofgem learning lessons from the 2018-21 arrangements. We welcome the constructive discussions we have had so far with Ofgem around incentives for RIIO-2, and hope to work towards a scheme where the ESO can be adequately recognised and rewarded for the value it delivers for consumers and stakeholders.

We have also made some more specific comments on the documents: please see the appendix to this response. Please do not hesitate to contact myself or Jenny Mills (jenny.mills@nationalgrideso.com) if you would like to discuss any of these points further.

Yours sincerely,

[by email]

Kayte O'Neill

Head of Strategy and Regulation

Appendix: additional specific comments

Specific feedback on incentives framework

Streamlining the ESO roles framework from four to three

We agree with the rationale for moving from four roles to three, recognising that whole system outcomes and competitive markets are concepts that apply throughout the ESO's activities.

The new framework proposes to change the name of role 1 from "Managing System Balance and Operability" to "Control Centre Operations". In our view, the new title is too specific, and does not refer to the activities within this role that take place outside of the control room itself, such as outage planning (which takes place across all timescales), and energy forecasting. We suggest that it may be more logical to retain the original title.

Streamlining how consumer benefits are considered as part of the evaluation criteria

We support Ofgem's proposal to merge the two consumer benefit criteria, as these are closely linked. We also welcome the recognition that for some roles, it may not be logical to report on both current and future consumer benefit, as for example the role may be mainly focussed on long-term activities for which the benefits have not yet materialised.

Additional reporting requirements

We support Ofgem's proposal for the ESO's reporting under the new framework to be structured by roles (rather than role areas).

We are happy to publish our cost forecasts by role at the Forward Plan stage, starting in March 2020. We note that there are also costs associated with supporting activities such as the Regulation, Customer and Stakeholder, and Assurance teams: we assume that these costs are out of scope for this reporting process.

However, we are concerned that it would not be feasible to report costs by role at as part of the end of year report. The ESO undergoes a thorough assurance and sign off process for the Regulatory Reporting Pack (RRP) which is published in July. As these processes would not be complete ahead of the End of Year Report being published in May, final cost numbers would not be available. We suggest that the ESO could report this data at the same time as the RRP is published in July, with the caveat that these are not the audited figures which appear in the final statutory accounts.

Additional specific comments on Roles and principles document

Future Energy Scenarios

We have a number of concerns with the section which relates to the Future Energy Scenarios (FES).

- Firstly, the proposed wording risks creating a level of rigidity in the annual FES process, which would reduce the ESO's ability to respond to changes in the operating environment and stakeholder requests. We have proposed some revised wording, to reflect the feedback we consistently hear from stakeholders and Ofgem that the ESO should be more agile in the way it operates.
- Wording such as "in detail" and "in full" could be interpreted to require a significantly increased compliance burden, for which the ESO does not currently have the resource. We currently provide evidence for our decisions and stakeholder engagement to Ofgem, and respond to ad hoc requests in detail, but providing full detailed evidence of every engagement and every decision would increase workload beyond current capacity.
- We removed specific mentions of Ofgem when describing our stakeholder engagement for FES input. While Ofgem is an important stakeholder and provides input to the Future Energy Scenarios, it is important to differentiate between Ofgem's role as one (key) stakeholder among many, and Ofgem's role in regulating the FES process (where it does not have a role in influencing the content of FES)

We would therefore like to propose the following revised text for the Future Energy Scenarios section:

1.45. The ESO is expected to engage with a wide a set of stakeholders, including Ofgem, to gather diverse views on topic areas in the Future Energy Scenarios. Furthermore, the ESO should record stakeholder views, in order to demonstrate the impact of stakeholder feedback on both the decision making and its influence on analysis alongside that of internal research and expertise. The ESO and Ofgem will agree in principle the breadth of stakeholder

engagement at the start of the annual FES process, with regular informal touchpoints throughout the process for ongoing updates.

1.46. The ESO should share with Ofgem its emerging thinking, accompanied with justification and stakeholder feedback where applicable and possible, ahead of major decisions in developing the Future Energy Scenarios framework.

1.47. The Stakeholder Feedback Document, with supporting discussion and additional materials should be provided to Ofgem to demonstrate the stakeholder input and how it has influenced the Future Energy Scenarios.

1.48. The ESO will discuss and agree any material changes to the FES process and annual plan, subject to resource considerations, before the process commences.

Onshore Competition

In paragraph 1.54 of the roles and principles document, Ofgem states *“For ‘late’ competition models we will continue to consider the roles and responsibilities of parties (including the ESO) in relation to the undertaking of preliminary works (including, but not limited to, works in relation to surveying, early design, planning permissions, and consents) for projects that meet the criteria for late model competition and are due to be constructed in the RIOT2 period and beyond.”*

We are concerned that this would require the ESO to undertake activities beyond those for which it is currently funded. We have not requested funding for such activities in our RIIO-2 business plan, as an impact assessment is required to identify the party and/or parties who are best placed to undertake some of these activities in a late model, for example preliminary works which would duplicate capability which already exists in the TOs. We propose that the wording in the Roles and Principles document should be limited to the ESO’s role in leading the Early Competition Plan, and the outcomes of this work should determine the ESO’s role in early or late competition. Alignment between the early and late models is essential.

Paragraph 1.54 also refers to the ESO’s support of future delivery models, for example “through its role in the NOA, as well as through information provision”. We continue to try to enhance our information provision, however it is important to note that some information which Ofgem may deem to be relevant may be owned by other parties, such as TOs. It may therefore be necessary to place similar obligations on TOs and DNOs, to allow expectations on data sharing to be met- this could include information on physical sites, and network capacity.

Other

Many “whole system” activities require the ESO to co-ordinate activities for which it has not been funded. Many activities are also dependent on other parties, such as DNOs, who do not have a reciprocal obligation on them to co-operate.

We note that all of the references to the licence seem to refer to condition C16, although many of the activities covered by the roles and principles are described in other parts of the licence. It may be useful for the document to contain more comprehensive linkages between the ESO licence conditions and the role framework.

We note that Principle 1.1 (support market participants to make informed decisions by providing user-friendly, comprehensive, and accurate information) is missing from the contents page, although we do not believe that this was Ofgem’s intention.

Additional specific comments on ESORI guidance document

Ofgem’s revised ESORI guidance document proposes to retain the scoring mechanism whereby the ESO is awarded a score between 1 and 5, with a score of 3 being “baseline”. As we have previously discussed with Ofgem, we are concerned that this scoring mechanism may be causing confusion, as a score of 3 out of 5 gives the impression of reasonable performance (e.g. a score of 60%) rather than of performance which does not merit an incentive reward. We would encourage Ofgem to revise their scoring framework for 2020-21 and beyond. Firstly, it would be good to set the mid point of the scoring scale to zero, to provide clarity that a central score of 0 represents baseline performance and an incentive payment of £0. It would also be helpful to introduce a wider scale, for example -5 to +5, to allow the panel to give a more nuanced score and be more specific about the financial impact of that score.

The revised scoring table on page 33 introduces the word “significant” to describe the amount of positive stakeholder feedback which would need to be received to merit a score of “excellent” for stakeholder evidence. We note that it is not always realistic to please all stakeholders, particularly when our overarching priority is to act in the consumer interest (which may not always be aligned with our stakeholders’ views and business models). The criteria should be amended to reflect this. However, we welcome Ofgem’s recognition that, where we have received negative stakeholder feedback, a justification for this feedback can be provided, for example where there was a strong rationale for not addressing the stakeholder’s request, and this was discussed with the stakeholder concerned.

In paragraphs 4.8 to 4.11, we believe that the addition of percentages to this table adds confusion. In particular, we do not understand the rationale for introducing the 10% increments.

Paragraph 4.12 refers to crossovers between roles. We note that under the new framework, all outage planning activities will sit under role 1 alongside balancing costs, and therefore this particular example of crossover should no longer apply.

In paragraphs 5.8 and 5.9, which refer to the long term vision, we believe that it is the topics listed in the roles and principles guidance document, rather than the guidance itself, which should be covered. Similarly, in 5.14, we believe that the performance metrics should be linked to roles rather than principles, and should ensure sufficient coverage of the topics listed in the guidance rather than the guidance itself.