Report

ESO Performance Panel End of Year Review 2019-20

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The regulatory and incentives framework encourages the Electricity System Operator (ESO) to proactively identify how it can maximise consumer benefits across the full range of its activities. These arrangements include a defined set of role areas for the ESO; a requirement to develop forward plans (in conjunction with industry consultation); the publication of regular performance reports; an ESO Performance Panel (the Panel); and a move towards a broader, evaluative performance assessment (with associated financial incentives).

We are publishing this report as the secretariat for the Panel, detailing the Panel's end of year assessment of the ESO's performance for the 2019-20 regulatory period. This report reflects the views of the Panel, not Ofgem.

The Authority will use this recommendation alongside other evidence collated throughout the year to determine a financial reward / penalty for the ESO worth ±£30m.

Introduction

Overview of evaluation process

The ESO Performance Panel (the Panel) plays a central role in the ESO's regulatory and incentive framework. It challenges the ESO's plans before the start of the year, evaluates the ESO's performance after six months (the mid-year review) and then performs a final evaluation at the end of the year. Under the ESO reporting and incentives arrangements[1], the ESO published an end of year report on 7 May 2020[2], covering its performance across the twelve month regulatory period for 2019-20. The aim of the report is to update stakeholders on the progress the ESO has made against its deliverables, detail its outturn performance against its performance metrics; and provide evidence of the consumer benefits its actions have delivered this year or are expected to deliver in the future.

Following the publication of the end of year report, the ESO presented this evidence to stakeholders and the Panel at an end of year review event that was held on 3 June 2020. Due to the current social distancing measures, the event was held online via Webex. During the webinar, stakeholders and the Panel had the opportunity to question the ESO and provide direct feedback. The Panel then held a follow up session with the ESO to seek any further clarifications on the evidence provided.

The Panel reconvened on 12 June 2020 to complete its end of year assessment of the ESO's performance for the 2019-20 regulatory period. Again, this was held by webinar. The Panel assessed the evidence provided by stakeholders, the ESO and collected by Ofgem throughout the year and used the evaluation criteria below to provide end of year scores for each of the role areas. These scores and this Panel report are a recommendation to the Authority on the ESO's performance and will support the Authority, along with other evidence, to determine a financial incentive

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[1] The ESO Reporting and Incentives Arrangements Guidance document:
https://www.ofgem.gov.uk/system/files/docs/2019/03/esori_guidance_document_2019-20.pdf
[2] ESO End of Year report 2019-20: https://www.nationalgrideso.com/document/168786/download

reward or penalty. The Panel's evaluation should also inform the ESO on the areas where it is performing well and the areas where improvements could be made.

This report summarises the Panel's assessment of the ESO's performance in the year. This report reflects the views of the Panel, not Ofgem.

The ESO Performance Panel members

Ofgem chair:
- Cathryn Scott, Interim Executive Director, Systems & Networks *(Cathryn chairs the meetings but does not take part in the scoring and evaluation of the ESO)*

Consumer representative:
- Richard Hall, representing Citizens Advice

Industry representatives:
- Chris Kimmett, representing The Association of Decentralised Energy
- Matthew Deitz, representing Energy UK
- Lynne Bryceland, representing the Energy Networks Association

Independent experts: *(who bring a wide range of knowledge, skills and experience to the Panel)*
- Professor Jon Stern
- Ian Tait
- Robert Hull

The evaluation process

Approach

The Panel sought to use the evaluation criteria described below and the process described in Chapter 3 of the ESORI (Electricity System Operator Reporting and Incentive Arrangements) guidance document to assess the ESO's performance in relation to each role area[3], taking into account Ofgem's feedback in the formal opinion and stakeholder feedback collected to date.

Evaluation criteria

In determining a score for each role area, the Panel used five key considerations to evaluate the ESO's performance:

a) Evidence of delivered benefits

b) Evidence of future benefits / progress against longer term initiatives

c) Stakeholder views

d) Plan delivery

e) Outturn performance metrics and justifications

Scoring

For *each* of the three role areas, the performance Panel provided end of year scores for the ESO on a scale of 1 to 5, where:

1 = Weak

2 = Poor

3 = Average ('baseline expectations')

4 = Good

5 = Excellent

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[3] The ESO's Roles and Principles for 2019-20:
https://www.ofgem.gov.uk/system/files/docs/2019/03/eso_roles_and_principles_guidance_2019-20.pdf

ESO Performance Panel's assessment

Overarching messages

Overall the Panel reflected that the ESO's performance had improved since the mid-year stage for 2019-20 and compared to 2018-19. Whilst the Panel noted mixed performance across the ESO's different areas and deliverables, the Panel agreed that the ESO had, on the whole, met and in some cases exceeded the baseline expectations for a competent and efficient system operator over 2019-20. The ESO had progressed a number of priority areas well, and these had been met with mostly positive stakeholder feedback, which the Panel reflected in their scores. More generally, the Panel noted that the ESO's engagement with its stakeholders had improved in some key areas compared to last year, which is reflected in the stakeholder feedback received this year. There are areas for improved performance going forward, but the ESO had made good progress on collaborating with stakeholders and responding to feedback. There were a number of delays to deliverables this year, across all of the roles, and this is the main reason that prevented the ESO from reaching higher scores. The Panel will be looking to see strong progress in 2020-21 to the areas that have been delayed this year. In particular:

- For Role 1, the Panel were concerned about the increase in balancing costs over the benchmark. They want to see the ESO continue to provide even greater transparency on control room decisions, work proactively to progress the Loss of Mains programme, and justify its choice of short term actions to solve the operability challenges that are driving ever higher balancing costs.

- For Role 2, the Panel particularly want to see improvements to plan delivery, especially the ESO's code administration and implementation of Clean Energy Package obligations.

- For Roles 3 and 4, the Panel would like to see improvements to plan delivery, continued progress with the pathfinders (in particular further progress with the voltage pathfinders), more clarity and progress on expanding the NOA to include non-TO options and more collaboration and coordination with regards to whole system planning, including via the Open Networks Project.

There were a number of areas, highlighted in the main body of the Panel's report below, where the Panel would like to see stronger evidence of benefits submitted. In particular, the Panel would like to see more evidence that the ESO is taking tangible steps to drive down balancing costs.

Summary of assessment scores

The Panel provided a consensus score for each of the role areas. In some instances, the Panel wanted to reflect more detail in their scores. For example, a score of 3 denotes that the ESO is meeting baseline expectations, but the ESO's performance for a particular role may be, on the whole, just above expectations but not sufficient to be scored a 4. This is reflected throughout the report as a 'high 3' (or alternatively a 'low 3' to signal performance that was slightly below expectations but not considered to be a 2). This distinction provides further clarity on how the Panel evaluated the ESO.

In all instances, the scores should be read alongside the detailed feedback and the reasoning provided by the Panel members.

Role 1: Managing system balance and operability

- Principle 1: Support market participants to make informed decisions by providing user-friendly, comprehensive, and accurate information

- Principle 2: Operate the system safely and securely, whilst driving overall efficiency and transparency in balancing strategies across time horizons

This role requires the ESO to help the market to balance the system as much as possible. Where it does need to step in to take any actions to secure the transmission system, it should be considering impacts across time horizons, to ensure the actions it does take drive overall efficiency.

All panel members scored the ESO within the 3 category. There was a mixed view within this, with some panel members considering performance as a 'low 3', but the majority considered it to be a 'mid 3' or 'high 3'. At the start of the year and at the mid-year stage, the Panel felt that the majority of commitments in this

area reflected business as usual activities for the ESO. At the end of year, all Panel members recognised the ESO had made some improvements from last year and was moving on a positive trajectory. The Panel's discussion highlighted that different members assign emphasis to slightly different areas of over/under performance. In order to reach a consensus, the Panel noted that plan delivery and stakeholder feedback were significant considerations in their assessment of Role 1, alongside the ESO's handling of 9 August power outage and COVID-19.

- On the evidence of benefits, the Panel reflected that the evidence provided by the ESO was limited and the Panel would have liked to see more detail on the actions the ESO has taken during the year to proactively manage the challenges faced and how the ESO had driven down balancing costs in the short-term. Going forward, the Panel would like to see evidence of the ESO's proactive role in constraint management to ensure these costs remain efficient. The Panel reflected on the slow progress of the Loss of Mains programme which has benefits that should materialise within a short period and so a few Panel members felt that the delay to this work was significant.

- On plan delivery, Panel members reflected that the ESO had met priority deliverables relating to information provision (particularly the thermal constraints map and the Open Data Portal), but hadn't delivered expected activities related to addressing operational issues and providing transparency of control room decision making. The Panel felt the thermal constraints map and the Open Data Portal deliverables were important, were strongly welcomed by stakeholders and therefore showed good performance.

- The panel noted that the ESO had met its regulatory obligations in managing the system safely and securely during the power outage on 9th August 2019. Some panel members reflected that Ofgem's investigation conclusions criticised some areas of ESO performance (such as poor distributed energy frequency response monitoring processes and insufficient processes to ensure compliance of new generation connections). These panel members expressed the view that the ESO could have been more proactive ahead of the event in progressing measures (such as the Loss of Mains project and reviewing security standards) that may have helped reduce the severity of

the event. One member argued that the ESO had done all that could be reasonably expected of it on 9 August. The panel agreed that the ESO had been proactive and positive in responding to the follow-up actions from the Ofgem and E3C reports.

- On stakeholder feedback, the Panel noted that stakeholders were more positive compared to last year. The Open Data Portal was seen as a significant, positive milestone and was well received by all stakeholders. Despite the delays with this, the Panel noted that this was a step-change in terms of how ESO data is delivered and accessed. The Panel also noted a step-change in terms of ESO engagement with industry, which has improved significantly, but noted that the ESO needs to do more to increase transparency on the ESO's control room decision making. The Panel would have liked to see further information on the Platform for Ancillary Services (PAS) as this was an area that was highlighted in the mid-year review where some stakeholders expressed frustration with aligning their own systems to PAS and some confusion about what and when the ESO was expecting to deliver through PAS in future.

- The Panel reflected on the ESO's response to COVID-19 (but noted that this is more relevant for the 2020-21 year). Regarding COVID-19, the Panel focussed on the ESO's regular engagement with industry over the last two weeks of March 2020. The panel agreed that the ESO appeared to have reacted well to the pandemic's initial impact and communicated this well to industry.

- The Panel discussed the outturn of balancing costs over 2019-20 against the balancing cost metric and noted limited confidence in the validity of the ESO's performance benchmarks and the ESO's adjustment factors. The Panel focussed primarily on the outturn costs and the articulation of what the ESO did or didn't do to manage these costs. Some Panel members noted significant concern with the growth in constraint costs and noted that limited evidence was provided on the different tools/approaches the ESO used to manage the current system challenges. Some panel members were also not convinced by the ESO's explanation of the reasons for the higher than

expected balancing costs. However, one member thought that the outturn on balancing costs was not unreasonable given the various weather and other challenges faced by the ESO during 2019-20 and the difficulties regarding forecasts for balancing costs many months in the future. The Panel encouraged the ESO to provide more evidence in future in order to demonstrate that it is being forward looking and is driving down these costs. This would help it to achieve a higher performance score.

- The areas in particular where the Panel noted that the ESO needs to improve were: providing transparency on control room decisions (including appropriateness of data reporting, such as of Schedule 7A trades); progressing the Loss of Mains programme; and explaining its choice of short term actions to solve the operability challenges that are driving higher balancing costs.

Role 2: Facilitating competitive markets

- Principle 3 - Ensure the rules and processes for procuring balancing services maximise competition where possible and are simple, fair and transparent

- Principle 4 - Promote competition in wholesale and capacity markets

This role requires the ESO to encourage and facilitate competition in all markets that it can affect. This includes the balancing and ancillary services markets where the ESO is the lead and principal buyer and also includes the remaining markets that the ESO can affect (i.e., wholesale and capacity markets).

Overall the Panel reached a **consensus on a score of a 'high 3'**; reflecting that the ESO had made progress since the mid-year evaluation and had met baseline expectations by the end of the year. The Panel placed greater weighting on future benefits and stakeholder feedback in order to arrive at this score. At the start of the year, the Panel said that delivering reforms on time would be a key measure of performance under this role, with a large emphasis on stakeholder feedback. The Panel recognised that there has been mixed performance for this role over the year, but considered that the ESO had improved its engagement with industry, was moving in the right direction and had acted upon the Panel's mid-year feedback

(eg, to work toward the highest priority deliverables, provide evidence of delivered benefits and take some action to improve code administrator performance).

- The Panel commented that the benefits from the ESO's activities in Role 2 are likely to be witnessed in the medium-to-longer term and so the Panel's assessment was influenced significantly by their expectations for the delivery of future benefits. The Panel noted that it expects benefits to accrue in future from the deliverables that have been progressed this year. Activities such as BM wider access and the frequency response auction trial were expected to lead to significant longer-term benefits, which will feed into lower balancing costs for Role 1.

- On plan delivery, the Panel thought that the ESO had made improvements this year but the level of progress had been mixed and anticipated deliverables were not met in a number of areas (particularly the balancing services reform deliverables). The Panel noted a number of positive accomplishments this year, such as the frequency response auction trial, the development of the dynamic containment product and the market-based approach for the procurement of black start services (all of which had been well received by stakeholders). The progress made on BM wider access was considered to be positive but it was noted that this progress had been restricted by the lack of appropriate supporting IT developments. The ESO's implementation of the Clean Energy Package obligations (particularly related to STOR and Fast Reserve) had been poorly managed and communicated. The reasoning behind delays and lack of progress to the products roadmaps for reserve and reactive power was also unclear. The Panel recognised the pathfinder work is informing the reactive power roadmap but greater progress was expected in this area.

- On stakeholder feedback, the Panel noted a step-change in the ESO's engagement with industry compared to previous years, particularly in regard to the product design of dynamic containment and the improvements made to the frequency response auction trial.

- The Panel reflected on the ESO's poor performance in the code administration survey and noted the continuing trend of poor feedback in this area. Some Panel members acknowledged the ESO's actions taken to improve performance in this area and noted that it will be important to see improved stakeholder feedback in this area next year. The Panel noted good performance across the other Role 2 metrics.

- Going forward, the Panel expects the ESO to build on the improvements made this year and to deliver tangible progress next year that results in real change and improvements to the markets that the ESO is responsible for. The panel specifically want to see improvements to the ESO's code administration and implementation of Clean Energy Package obligations. The Panel will also be looking to see evidence of the benefits of Role 2 activities feeding into lower costs under Role 1.

Roles 3 and 4: Facilitating whole system outcomes & supporting competition in networks.

- Principle 5: Coordinate across system boundaries to deliver efficient network planning and development

- Principle 6: Coordinate effectively to ensure efficient whole system operation and optimal use of resources

- Principle 7: Facilitate timely, efficient and competitive network investments

Under this role area the ESO is expected to coordinate effectively with other parties to deliver the most efficient and economic outcomes for the whole system. This includes coordinating with others across network boundaries when undertaking network planning and development and coordinating with others in ensuring efficient whole system operation and optimal use of resources.

The ESO should enable competition in network investment to bring value for consumers in terms of capital and operational cost savings and drive innovation across the asset development and operations process, including financing. Competition may be demonstrated by, but not limited to, the creation of a strong

competitive field through attracting new entrants and new approaches to ideas, design, financing, construction and operation of network infrastructure and alternative solutions.

Overall the Panel reached a **consensus on a score of a 'high 3'**, noting that the ESO was slightly above baseline expectations for this area. At the start of the year and mid-year stage, the Panel said that it wanted to see whether the ESO was stretching itself in this area by assessing how the deliverables have been executed and whether the ESO is able to make tangible progress with the Forward Plan. The Panel noted the ESO's evidence of future benefits that will be delivered by the first phase of the Stability Pathfinder[4].

- The Panel recognised phase 1 of the Stability Pathfinder as implementation of a major milestone completed during 2019-20 and a significant factor in their assessment. The Panel considered the pathfinder work to be innovative and likely to generate significant future consumer benefits.

- On plan delivery, the Panel noted mixed performance of the deliverables; phase 1 of the Stability Pathfinder had been delivered but other pathfinders on voltage and constraint management have been delayed. The Panel recognised that this is a complex area and noted the ESO's justification for the delays, which was based on feedback. One Panel member noted that the ESO could have engaged more proactively with network operators to ensure the correct framework was in place to facilitate the pathfinder processes and delivery of the identified solutions, ahead of the running of the tender exercises. The Panel recognised that the ESO had delivered some improvement to the format of the Network Options Assessment (NOA) publication, however concerns were noted that third parties continue to be unable to provide options into the annual NOA process and there was still a limited number of non-TO options included in the NOA as 'ESO-led solutions'.

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[4] More information on the Stability pathfinder can be found at: https://www.nationalgrideso.com/research-publications/network-options-assessment-noa/network-development-roadmap

- On stakeholder feedback, the Panel recognised that the ESO has increased its interaction with stakeholders overall. The Panel agreed that the ESO's work on early competition was positive and had strong stakeholder engagement with TOs and market participants. However, based on stakeholder feedback received, there are further improvements to be made, particularly in taking a 'whole system' view and not focusing solely on ESO issues. The Panel agreed with stakeholders that the ESO had been less engaged with the Open Networks Project[5] compared to 2018-19 and the ESO must provide more transparency around its future plans/intentions for the execution of additional pathfinders.

- At the mid-year stage, the Panel noted that some performance metrics had no benchmarks, other benchmarks hadn't been explained and some of the benchmarks could have been more challenging. For the Panel to rely on the outturn of the performance metrics the ESO should provide more complete metrics, articulate why these metrics matter and how they demonstrate strong performance. The Panel noted year-on-year improvement to performance under metric 14: right first-time connection offers.

- Going forward, the panel would like to see continued progress with the pathfinders (in particular progress with the voltage pathfinders), more clarity on how the ESO will expand the NOA to include non-TO options and more collaboration and coordination in whole system planning, including via the Open Networks Project. Some panel members also expressed a view that the ESO needed to do more to evidence the validity of its cost-benefit approach to prioritising its work in this Role area, given its importance in addressing future network challenges.

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[5] More information on the Open Networks Project can be found at:
https://www.energynetworks.org/electricity/futures/open-networks-project/open-networks-project-overview/#:~:text=The%20Open%20Networks%20Project%20is,and%20communities%20in%20the%20UK