

Report

ESO Performance Panel Mid-Year Review 2020-21

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The Electricity System Operator (ESO) has a central role in our energy system. It performs a number of important roles, from the real time operation of the electricity transmission system, through to market development and advising on network investment.

The regulatory and incentives framework encourages the ESO to proactively identify how it can maximise consumer benefits across the full range of its activities. The framework uses an evaluative approach. This means we set up front expectations, and criteria, and make a final decision on incentives at the end of the regulatory year. This evaluation is based on an ongoing assessment of the ESO's performance, drawing input from stakeholders and our ESO Performance Panel.

We are publishing this report as the secretariat for the ESO Performance Panel, detailing the Panel's assessment of the ESO's performance at the mid-year review stage. This report reflects the views of the Panel, not Ofgem.

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Mid-year review 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.

Following the publication of the mid-year report¹, the ESO presented this evidence to stakeholders and the Panel at mid-year review event that was held on 17 November 2020. Due to the current social distancing measures, the event was held online via Microsoft Teams. During the session, stakeholders and the Panel had the opportunity to raise questions and provide direct feedback to the ESO. The Panel then held a follow up session with the ESO to seek any further clarifications on the evidence provided.

On 19 November 2020, the Panel reconvened to discuss and make its assessment of the ESO's performance over the first six months of the 2020-21 year. The Panel used the evaluation criteria below to provide **mid-year scores** for each of the ESO's role areas. For the avoidance of doubt, the scores do not inform an incentive reward or penalty at this stage. These scores are indicative and are to inform the ESO on the areas where it is performing well and the areas where improvements need to be made over the final six months of the year.²

This report summarises the Panel's assessment of the ESO's performance to date and some wider considerations to inform the ESO's priorities over the next six months and its performance reporting going forward. This report reflects the views of the Panel, not Ofgem.

The evaluation criteria

¹ ESO mid-year report 2020-21: <https://www.nationalgrideso.com/our-strategy/forward-plan/how-were-performing>

² More details on the scoring and evaluation criteria can be found in Chapter 3 of the ESORI guidance document: https://www.ofgem.gov.uk/system/files/docs/2020/03/eso_roles_and_principles_guidance_2020-21.pdf

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

- a) Evidence of consumer benefits
- b) Stakeholder views
- c) Plan delivery
- d) Outturn performance metrics and justifications

Approach

The Panel sought to use the evaluation criteria described above 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, taking into account Ofgem's feedback in the formal opinion³ and stakeholder feedback collected to date.

Scoring

For each of the three roles, the Panel provided *mid-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

³ Ofgem Formal Opinion 2020-21: <https://www.ofgem.gov.uk/publications-and-updates/ofgem-s-formal-opinion-electricity-system-operator-eso-forward-plan-2020-21>

Summary of ESO Performance Panel's assessment

Overarching messages

The Panel welcomed the information provided by the ESO in its mid-year report and stakeholder events, including videos summarising key performance issues from the period.

The impact from COVID-19 and the ESO's response was a key feature of the Panel's considerations. The Panel commended the ESO on its organisational response to the pandemic and on maintaining the security of the system, despite very challenging and unprecedented system conditions created by COVID-19. Nevertheless, the Panel was concerned about the major increase in balancing costs to date.

The Panel included consideration of the ESO's immediate crisis response and management under Role 1 and the preparation for known system issues⁴ under Role 2. The Panel thought the ESO's crisis response was strong but control of balancing costs was likely made more difficult due to ongoing delays in the implementation of technical and market improvements to tackle known system issues. The Panel acknowledged the positive stakeholder feedback on communication during the crisis, especially around the ESO's weekly meetings. More generally, the ESO appears to have improved its engagement with stakeholders in almost all areas and this was welcomed by the Panel.

The Panel noted that over the first six months of 2020-21, the ESO was granted regulatory flexibility⁵ for a number of deliverables due to the impact of COVID-19.

⁴ Known system issues include the Rate of Change of Frequency (RoCoF), the need for fast frequency response and system flexibility, new capabilities requirement for system stability as a result of embedded generation and voltage control (the increasing need for reactive power absorption). This is described in the ESO's System Operability Framework Report 2015: <https://www.nationalgrideso.com/document/63461/download>

⁵ On 24 April 2020, we issued an open letter to the ESO. In this letter, we set out a process for the ESO to demonstrate necessary delays in 'lower priority' ESO activities to enable the ESO's response to the COVID-19 pandemic. This framework of regulatory flexibility was put in place for an initial period

These deliverables experienced delays due to COVID-19 impacts that were outside of the ESO's control. Now that this period of regulatory flexibility has ended, the Panel would like the ESO to refocus on delivering all commitments in a timely manner, with a focus on identifying and delivering the highest value deliverables by the end of 2020-21.

The Panel also strongly welcomed the ESO's commitment to a forthcoming piece of work that will 'join the dots' to provide strategic oversight of how the various planned market reforms will come together and more clarity on the interaction between developments across Roles 2 and 3. The Panel would like to see more pace in delivering market reforms, whilst accepting the recognised challenges of implementing reforms, and would like the ESO to prioritise its focus to where it can deliver most consumer benefit.

The Panel encouraged the ESO to analyse the lessons learnt from the challenges experienced in the first half of this year, particularly as demand will continue to be low in 2021, and to provide evidence of embedding this learning.

Summary of scores

We have summarised the scores agreed by the Panel, following its assessment of the ESO's performance. 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'. Alternatively, a 'low 3' score signals performance that was slightly below expectations but not considered to be a 2.

In all instances, the scores should be read alongside the detailed feedback. This report captures the breadth of views that were expressed and the reasoning provided by the panel members.

Role area	Role 1	Role 2	Role 3
Score	4	2 (high)	3 (low)

Role 1: Control Centre operations

- Principle 1.1: Support market participants to make informed decisions by providing user-friendly, comprehensive, and accurate information;
- Principle 1.2: Operate the system safely and securely, whilst driving overall efficiency and transparency in balancing strategies across time horizons;
- Principle 1.3: Coordinate effectively to ensure efficient system operation and optimal use of resources.

This role requires the ESO to support the market to balance the system as far as possible. Where the ESO does need to take actions to secure the transmission system, it should consider impacts of its actions across time horizons, to ensure the actions taken drive overall efficiency.

Role 1 score	4
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The Panel agreed on a score of 4. The Panel reflected that overall the ESO was currently within the lower range of this score. The Panel's deliberations focussed mostly on plan delivery, stakeholder views and the outturn of performance metrics.

- The Panel considered the ESO's crisis response and management of COVID-19 under Role 1. The Panel thought the ESO reacted quickly to maintain the security of the system in the face of major organisational and operational challenges caused by low demand and high renewable output. The panel noted the swift introduction of the ODFM product as a good example of working with industry to deliver at pace. However there were questions about the cost-benefit of ODFM and other ESO actions such as the Sizewell

contract. The Panel was pleased to see the ESO embed some of COVID-19 practices into BAU, such as the weekly webinars (ESO Operational Transparency Forum). The panel noted that Emergency Response plans for the Control Room (staff, system operation, health and safety etc.) have been effective. However, emergency planning does not seem to have considered the wider impact on market operation.

- The stakeholder feedback suggested the ESO has improved its communication, particularly through the weekly Operational Transparency Forum, which was well received by stakeholders. Whilst the Panel welcomed improved and regular communications with key stakeholders, it did note that this improved communication has not necessarily translated to improved transparency. Stakeholders noted a need, in particular, for greater transparency on balancing costs and the ESO's control room decision making process.
- On the performance metrics, the Panel was particularly concerned by the significant increase in balancing costs, including whether these have been efficiently incurred and whether the ESO has considered all options available in the circumstances. The Panel felt that the evidence to explain why costs had increased to such a large extent was incomplete. The Panel expects the ESO to better explain the extent to which the additional balancing costs were driven by the impacts of COVID-19 as oppose to other, more foreseeable, factors such as the levels of wind/solar generation and the impacts of traditional low-demand periods (e.g. summer months and bank holidays). The Panel also expected greater justification for the ESO's relatively poor wind forecasting performance and to understand what actions the ESO will take over the next six months to improve this.
- By the end of the year the Panel would like to see greater explanation of what the ESO has learnt from the COVID-19 pandemic (especially dealing with low demand) and particularly what this means for the ESO's delivery of its zero carbon operability ambition by 2025.
- The Panel's score of 4 reflects the ESO's swift response to the COVID-19 crisis to maintain security of supply, and assumes that all possible steps were taken to minimise the balancing costs to date. To maintain a score of 4 the Panel expects the ESO to do all that it can to minimise further increases

in balancing costs over the final six months of the year and provide evidence of how it has done this at the end of year stage.

Role 2: Market development and transactions

- Principle 2.1: Ensure the rules and processes for procuring balancing services maximise competition where possible and are simple, fair and transparent;
- Principle 2.2 - 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 architect and principal buyer and also includes the remaining markets that the ESO can affect (i.e. wholesale and capacity markets).

Role 2 score	2 (high)
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The Panel agreed on a score of a 2. The Panel reflected that overall the ESO was within the higher range of this score and towards a 3 but hadn't demonstrated enough to meet baseline expectations for Role 2. The Panel deliberations focussed on plan delivery, stakeholder views, performance metrics and evidence of benefits when making this assessment.

- The Panel reflected that previous and ongoing delays to implementing balancing market reforms had limited the toolkit available to the control room to procure efficient balancing services in response to the COVID-19 pandemic and this had likely contributed to the significant increase in balancing costs. The 'roadmap' of ESO's market reforms remains unclear and there is ongoing uncertainty among stakeholders about what will be delivered and when, particularly for new frequency response products (Dynamic Regulation and Dynamic Moderation) and reserve products. The Panel noted that the ESO was granted temporary regulatory flexibility for TERRE, however the delays have extended beyond this period. New timelines for deliverables that were reasonably delayed by COVID-19 re-prioritisation have not been well communicated with stakeholders.

- The Panel encouraged the ESO to re-evaluate and write a realistic multi-year delivery plan, by identifying and prioritising the deliverables in order to give greater certainty that the most important actions will be progressed first. As part of this, the ESO should analyse the lessons learnt from the market challenges experienced in the first half of the year and provide evidence of embedding this learning. The Panel strongly welcomed the ESO's forthcoming piece of work that is intended to 'join the dots' between the various market reforms and provide more clarity on the timelines for future developments across Role 2 and Role 3. The Panel would like to see the ESO explain how the various market reforms will interact and for the ESO to prioritise implementation of the reforms that will deliver most consumer benefit.
- The Panel noted some improvement in stakeholder feedback on Role 2 and particularly welcomed improvements related to code administration. The panel also noted some good engagement with market participants; for example on developing the dynamic containment product, but noted that some stakeholders have said the soft-launch of dynamic containment has favoured some assets. The Panel would like the ESO to move beyond simply communicating progress to stakeholders and do more co-creation with stakeholders on the market design of new products, building on the experience during the pandemic, in order to address market issues and create a level playing field.
- On metrics, the Panel noted the poor overall performance on competitive procurement of balancing services. The Panel acknowledged the challenges faced in forecasting BSUoS during the COVID-19 pandemic but expects to see improvements over the final six months of the year. The Panel recognised the improvement in code administration satisfaction scores and in the absence of the CACOP survey considered these to be meeting expectations.
- On evidence of benefits, the Panel agreed that the case studies presented by the ESO equated to meeting baseline expectations. The Panel expects significant consumer benefits could be gained through delivery of the ESO's market reforms. At present, the Panel was not convinced that the ESO is prioritising activities that will deliver most consumer benefit.

- To improve the Role 2 score by the end of the year, the Panel would like to see the ESO identify the lessons learnt from the balancing market performance this year and prioritise the timely implementation of the reforms that will deliver most consumer benefit and, where possible, use approaches that ensure co-creation alongside market participants.

Roles 3: System insight, planning and network development

- Principle 3.1: Coordinate across system boundaries to deliver efficient network planning and development;
- Principle 3.2: 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 other parties across network boundaries when undertaking network planning and development. The ESO should also facilitate competition to ensure value for consumers and to drive innovation.

Role 3 score	3 (low)
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The Panel agreed on a score of a 3. The Panel reflected that given the information available the ESO's performance was within the lower range of this score and marginally below baseline expectations. The panel deliberations focussed mostly on plan delivery, stakeholder views and evidence of benefits.

- On plan delivery, the Panel's assessment was hampered by a lack of specificity in what the ESO planned to deliver during this period. The Panel noted that the lack of clear interim milestones or well-defined outputs within the deliverables meant there was comparatively less evidence of tangible progress during the first six months of 2020-21. The Panel considered that the pathfinders were still making tangible progress against the longer-term outcomes but they could not see a clear line

from the existing deliverables into a long term strategy in this area. As noted in Role 2, the Panel was not clear how the ESO expects the pathfinders to impact / interact with the market reforms in Role 2. The lack of clarity on long term strategy made it harder to conclude that the ESO's plan for this year had the highest priority deliverables and was making the necessary progress and delivering the necessary consumer value.

- The slow progress of the loss of mains work was also a noted concern for the Panel. Given the large consumer benefits associated with this work the Panel expects the ESO to treat this as a high priority and sees it as a critical deliverable for the end of year incentives outcome. The Panel understood that COVID-19 had impacted this work due to the need for on-site verification but expects to see the ESO step up its leadership of this work to make progress in engaging harder-to-reach generators.
- The Panel also noted that the constraints pathfinder appeared to be focused on bringing forward specific solutions rather than creating level playing fields for all solutions to compete to solve network needs. As the pathfinders are based on 'learning by doing', the Panel also expects to see evidence that learning gained so far is shaping the future direction in order to maximise benefit.
- The Panel recognised that stakeholder feedback was positive on the loss of mains project and in engaging/working with DNOs. However, feedback from TOs, particularly on the pathfinders and early competition, was poor. The Panel recognised that the TOs are involved in putting forward projects for consideration in these processes, but as licenced network operators, TOs also have a role to play in working with the ESO to ensure these processes are well designed and run effectively.
- On evidence of benefits, the Panel was unable to conclude that the ESO is prioritising clearly the most high value activities. For example, the descope of the constraints management pathfinder raised questions about whether the ESO was focused on the areas that could deliver most value. In general, the Panel felt that there is more for the ESO to do to comprehensively evaluate and communicate the cost benefit of its Role 3 initiatives and to use this evaluation to prioritise its areas of focus.

- To improve upon the mid-year score the Panel suggested that by the end of 2020-21 (or, if possible, in advance of this) the ESO should rearticulate what Role 3 outcomes the ESO is trying to achieve, how specifically the ESO deliverables will achieve these outcomes, and how these outcomes interact with market developments in Role 2. This would allow the Panel to clearly see whether the ESO is driving forward excellent developments in network planning. To support this, the ESO should also clearly show how it is learning lessons from the delivered pathfinders and improving engagement with TOs on other existing/future pathfinders.
- To improve their score the Panel also expects the ESO to deliver clear, tangible delivery of key intermediate milestones, in particular material progress on the loss of mains work.

Annex 1: Panel Membership for the Mid-Year Review 2020-21

The members of the Panel include:

- Ian Tait (independent Panel member)
- Jo Butlin (independent Panel member)
- John Carnwath (independent Panel member)
- Robert Hull (independent Panel member)
- Energy UK (represented by Jack Presley Abbott)
- Association of Decentralised Energy (represented by Chris Kimmet)
- Energy Networks (represented by Lynne Bryceland)
- Citizens Advice (represented by Richard Hall)
- Ofgem Chair/facilitator (represented by Eleanor Warburton on behalf of Cathryn Scott)

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