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Date: 31 July 2019

Dear Colleague,

Authority determination to adjust black start costs incurred in 2018/19

This letter sets out the Authority's¹ decision to direct an adjustment of £0 to the term $BSTA_t$ of National Grid Electricity System Operator Ltd's ("NGESO") licence for Relevant Year 2018/19 in accordance with Special Condition 4G.21. This decision means that NGESO, as the Electricity System Operator ("ESO"), can recover £48,951,292.85 of costs incurred to procure black start services in 2018/19. We have considered all of the costs submitted to us against the criteria in Special Condition 4G of the ESO's licence, and we have no concerns on their accuracy or compliance with the Approved Methodologies.²

However, in our assessment of feasibility study costs for 2017/18, we found that invoices for one contract were dated before 1 April 2018. Given that the ESO made the choice not to include the cost of this contract prior to our clarifying guidance³ last year, we believe that it is appropriate for the ESO to recover these costs this year. Therefore, we have decided to direct the value for the term $BSTA_t$ to be £0.

This letter sets out the reasons for the Authority's decision to direct an adjustment of £0 to the costs specified in the ESO's annual report prepared pursuant to Special Condition 4G.13, dated 30 April 2019 ("Report").

Background

Black start is the process used to recover from an event which results in the full or partial shutdown of the transmission system. Isolated power stations are started individually without an external power supply, and gradually reconnected in order to re-energise the system. NGESO, in its role as the ESO in Great Britain ("GB"), has an obligation under the Grid Code⁴ to ensure black start capability is available. NGESO also sets local joint restoration plans with relevant parties including transmission owners and distribution network operators.

¹ The terms "we", "us", "our", "Ofgem" and "the Authority" are used interchangeably in this document and refer to the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.

² The 2018/19 methodologies consist of the black start strategy document and the black start procurement methodology documents which can be found at the following address:
<https://www.nationalgrideso.com/balancing-services/system-security-services/black-start>

³ The guidance was provided as part of our decision to direct an adjustment of £0 to the term $BSTA_t$. The decision can be found at the following address: <https://www.ofgem.gov.uk/publications-and-updates/authority-determination-adjust-black-start-costs-incurred-201718>

⁴ As set out in Grid Code CC6.3.5 and OC9.4.7.12.

On 1 April 2017, we introduced a regulatory framework for determining the allowed revenue derived from black start that NGENSO may recover each year.⁵ In addition to the submission of the methodologies, NGENSO is required by Part E of Special Condition 4G to submit the total costs associated with the provision of black start provision to the Authority for an *ex post* assessment at the end of each Relevant Year. We then determine whether the total costs were incurred in accordance with the Approved Methodologies.

The regulatory framework relies on efficiency checks at the end of each year against the Approved Methodologies to ensure that costs incurred are economical and efficient and in the interest of consumers. Therefore, it is vital that all costs incurred in any Relevant Year are reported.

The different costs incurred by NGENSO are to pay for black start service providers to be available to provide the service, to warm service providers that would have otherwise been unavailable, to test and provide capital to ensure capability to service providers, as well as to assess the feasibility of new service providers to provide this service.

NGESO's Submissions

On 30 April 2019, the ESO submitted its Report to the Authority on the total black start costs incurred totalling £48,951,292.85 in 2018/19, pursuant to Special Condition 4G.13. The Report was accompanied by a statement from an independent auditor, which is required pursuant to Special Condition 4G.15.

The Authority's decision

Having considered the Report, auditor's statement and additional information submitted to us by the ESO, in accordance with its obligations under Special Condition 4G, as well as our principal objective and statutory duties, we have decided to:

- Direct the value for the term $BSTA_t$ to be £0 for Relevant Year 2018/19 pursuant to Special Condition 4G.21.

Our assessment described below explains the process that was followed in accordance to Special Condition 4G.20 to determine whether the costs incurred were compliant with the Approved Methodologies for the 2018/19 year. It is important to note that all figures exclude value added tax.

Assessment of cost accuracy and compliance with the Approved Methodology

To assess the accuracy of, and compliance with the Approved Methodologies informing, the total costs submitted, we have performed the following checks:

- Review of the methodology applied on warming;
- Review of the processes for procuring new providers that were subject to costs in 2018/19;
- Review of the availability payments made in 2018/19;
- Recalculation of availability payments based on contract values; and
- Assessment of feasibility studies, testing and invoices submitted to the Authority.

These checks were in addition to those undertaken by the independent auditor, who indicated that to the best of their knowledge, the costs reported were accurate and the costs were aligned with the Approved Methodologies. Our assessment likewise concluded that these costs were accurate and were incurred in accordance with the Approved Methodologies.

⁵ <https://www.ofgem.gov.uk/publications-and-updates/decision-electricity-system-operator-incentives-april-2017-modification-standard-and-special-licence-conditions-transmission-licence>

Costs incurred for Feasibility Studies

Special Condition 4G.13 requires NGENSO to submit total costs incurred in the Relevant Year. In the case of the Report, the Relevant Year is 2018/19. Availability and warming costs can be directly attributed to a particular financial year given their association with a particular 30-minute settlement period. However, feasibility studies can span multiple financial years and are not directly associated with a 30-minute settlement period. In our decision to direct an adjustment of £0 to the term $BSTA_t$ on 20th August 2018,⁶ we clarified that the date that invoices are submitted to the ESO is deemed to be when the costs are incurred.

In our assessment of feasibility study costs for 2018/19, we found that invoices for one contract were dated before 1 April 2018. In accordance with standard accounting practices, and in line with guidance we provided in our previous decision, we have concluded that the cost of this invoice (£90,895.47) was incurred outside of the Relevant Year.

BSTA_t adjustment

Following our assessment, we have determined that the appropriate value for the term $BSTA_t$ to be applied in 2018/19 to be £0 for the following reasons:

- a) While £90,895.47 of the feasibility study costs were incurred outside the Relevant Year, they were incurred in accordance with the spirit of the Approved Methodologies.
- b) Finding new black start providers is in the interest of consumers, by promoting competition and ensuring adequate service provision. As a result, conducting this feasibility study in an economic and efficient manner was in the interest of consumers.
- c) Last year, we took the decision not to deduct these costs, which were deemed to be economic and efficient, and instead provided further guidance on the expectations under the licence due to the fact that it was the first year of the new scheme.
- d) The ESO's deadline for the submission of last year's allowed revenue report was 30 April 2018, and the guidance mentioned above was provided in our decision on 20 August 2018. Given that the ESO took the decision not to include these costs prior to our guidance on 20 August, we believe that the reasons for not deducting costs in 2018 still apply to this invoice.

Therefore, we do not believe that it is appropriate to deduct these costs given they were economic and efficient and the ESO's choice not to include them last year pre-dated our guidance on this issue. However, it should be noted that we do not expect to see any further instances of these errors in the future.

Next Steps

Following this decision, we will continue to engage with the ESO to clarify our expectations on the level of detail we expect to be included in both the ESO's allowed revenue report and future independent auditor's statements that the ESO is required to provide. Published alongside this letter is a copy of the Direction. This letter constitutes notice for the purposes of section 49A of the Electricity Act 1989 in relation to the Direction.

Yours faithfully,

Eleanor Warburton
Deputy Director - ESO and Gas Systems - Duly authorised on behalf of the Authority
Dated: 31/07/2019

⁶ <https://www.ofgem.gov.uk/publications-and-updates/authority-determination-adjust-black-start-costs-incurred-201718>