

By e-mail to: ESOperformance@ofgem.gov.uk

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Dear Louise

ELEXON's response to your Call for input on 2019-20 ESO regulatory and incentives framework

We welcome the opportunity to provide thoughts on potential improvements to the Electricity System Operator (ESO) regulatory and incentives framework from April 2019, as requested in your letter to stakeholders dated 16 October 2018.

As you are aware, ELEXON (as 'BSCCo') is the Code Manager for the Balancing and Settlement Code (BSC). We are responsible for managing and delivering the end-to-end services set out in the BSC and systems that support the BSC. ELEXON is also responsible for EMR settlement arrangements.

Under the BSC and EMR arrangements we rely heavily on the ESO:

- for timely and accurate data in order, for example, to calculate imbalance prices
- for support in raising certain BSC Modifications e.g. those required to meet EU legal requirements
- for providing resource and information to enable certain BSC Modifications to be progressed and implemented in a timely and efficient manner.

In turn, ESO relies on both industry's and ELEXON's expertise and input.

Therefore the design of the ESO regulatory and incentives framework is key for us, and important to the electricity industry and ultimately to end consumer, to the extent that this framework fosters or hinders cooperation and collaboration between the ESO and ELEXON.

The views expressed in this letter are those of ELEXON Ltd alone, and do not seek to represent those of the BSC Panel or Parties to the BSC.

I hope you find these thoughts helpful and if you would like to discuss any aspects, please don't hesitate to contact me at steve.wilkin@elexon.co.uk.

Yours sincerely,



Steve Wilkin
European Coordination Manager

ELEXON'S THOUGHTS ON ESO 2019-20 ESO REGULATORY & INCENTIVES FRAMEWORK

1. Introduction

- 1.1 The following sections 2 to 6 inclusive reflect the areas on which Ofgem is seeking stakeholder views (as set out in Annex 1 of your 'Call for input' letter, dated 16 October 2018).

2. The ESO Roles and Principles

- 2.1 In response to Ofgem's question as to whether there are any gaps in the Roles and Principles, we have not identified any to date.
- 2.2 Rather, we wish to re-iterate a view we have previously made that, if the ESO incentives for Principle 4, which are currently partly based on relative performance in comparison with other code administrators, start acting to discourage collaboration and cooperation between ESO and ELEXON (see cover letter), then we would suggest that the incentives should be changed to reward absolute, not relative, ESO performance improvements.

3. The Forward Plan Process

- 3.1 We agree that the Forward Plan should be published earlier in the process each year for stakeholder consultation and Ofgem consideration.
- 3.2 We also suggest that the Ofgem Formal Opinion should come at least two months earlier i.e. by end February, so that it falls ahead of start of the incentive year and gives ESO time to react and, if necessary, revise its plans. In turn, this suggests that the ESO Forward Plan should be submitted to Ofgem by end January, say, each year.
- 3.3 We agree that additional reporting on ESO's internal expenditure would be helpful. This should reveal the strength of the incentives relative to base expenditure and will help decide if the strength of the incentives is appropriate, e.g. the relative size/weighting of the incentive pots; and indeed, in the longer term, whether the size of the overall incentive (currently +/- £30m) remains appropriate.

4. Within-year reporting requirements

- 4.1 In answer to Ofgem's question as to whether the within-year reporting requirements strike the right balance between transparency and resource burden, currently we do not believe that they do.
- 4.2 For us, ESO is publishing too much information too frequently rather than targeted, easier-to-find, key information. The resource burden on stakeholders and Performance Panel is large and may mean that information of key value to particular stakeholders, though public, is not seen by them in a timely manner.
- 4.3 For example, in the first six months of the new incentive scheme ESO has published monthly; then quarterly and Mid-year reports. The Mid-year report was over 200 pages in length.
- 4.4 In total it appears that ESO has published 29 separate monitoring reports and minutes (see link [here](#)) since April 2018 up to end October 2018. Or a total of nearly 520 pages, equivalent to reading three pages per working day in this period for anyone wanting to make sure that they did not miss anything, e.g. Performance Panel members.

- 4.5 It may be appropriate for ESO to publish its expenditure on within-year reporting. As this may test whether the current reporting level is an effective, value for money, use of its resources. This also aligns with the point we made, in section 3 above, supporting additional reporting of ESO's internal expenditure generally.

5. The Mid-Year Review and Panel processes

- 5.1 We agree that it is too early to draw any firm conclusions on this process.
- 5.2 We note that there is a danger that the resource burden will be too much for the ESO Performance Panel. And this may undermine one of Ofgem's stated reasons for its existence, i.e. that the Panel can provide an independent view to address the asymmetry of information between Ofgem and ESO. For example, if the Panel relies too heavily on Ofgem for a summary of the ESO's points or stakeholder views.
- 5.3 However, as the Panel has only just met for the first time, we suggest that this is tested in practice by asking Panel members themselves for their feedback on the process.
- 5.4 We also have some observations on the open, morning, session of the first Panel held on 20 November 2018, which you may find helpful.
- We had expected to be attending as observers at a 'Parliamentary Select Committee' style hearing where ESO presented, followed by an interview of ESO by the Performance Panel.
 - However, the open session was an ESO-led seminar where we had a series of ESO presentations followed by Questions and Answers from the floor (Panel members and general audience mixed).
 - We observed some interesting effects from this format. ESO was not challenged or commended on past performance by Panel members & stakeholders (with some exceptions) as much as expected. Instead the discussion moved more towards future ESO plans, rather than a discussion of the past six months. This may indeed be an appropriate format for the six month review, but we have some alternative suggestions for the annual review when past performance will need to come into sharp focus.
 - For the end of year review, it might be better to adopt the following approach to challenge and test ESO's performance over the review year:
 - ESO presentation on its successes (and failures if any) for Principle 1
 - Stakeholder presentations on Principle 1 for any who wish to do so
 - Questions from the Panel Members to ESO and to Stakeholders on Principle 1
 - Repeat the above elements for each Principle in turn.
 - This could lead to a more effective use of stakeholders' and Panel members' resource, but you will probably wish to test this idea with the Panel members.

6. The evaluation process and financial incentive parameters

- 6.1 Our understanding is that the baseline ESO costs for Principle 4 (which includes code administration and BSUoS billing) is only £5m. This suggests that the incentive lever of +/- £4.29m may be too powerful and that the weighting of Principle 4 should be reduced relative to the other pots. Publication of internal expenditure (section 3 above) by principle pot would support more detailed analysis of this.

END.