

By e-mail to: RIIO2@ofgem.gov.uk

ESO Regulation Team
Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

24 September 2019

Dear ESO Regulation Team,

ELEXON's response to Ofgem's consultation on the ESO RIIO-2 financial methodology and incentives

We welcome the opportunity to provide a response to the above consultation. We have concentrated in this response on the incentives aspects of the consultation.

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.

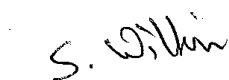
In turn, ESO relies on both industry and ELEXON's expertise and input, e.g. in developing the GB TERRE settlement arrangements and in widening Balancing Mechanism access; in developing harmonised imbalance settlement in Europe; and data for ESO to calculate TNUoS charges.

Therefore, the key ESO performance attribute for us is collaboration and cooperation between ESO and ELEXON on matters where we deliver maximum benefit to the end customer via joint service excellence to the industry. Therefore, in our view, the ESO incentive framework should operate to support this.

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 do not hesitate to contact me at steve.wilkin@elxon.co.uk.

Yours faithfully,



Steve Wilkin
European Coordination Manager

ELEXON'S VIEWS ON THE PROPOSED ESO RIIO-2 FINANCIAL METHODOLOGY; AND INCENTIVES FRAMEWORK

1. Proposed ESO incentives Framework

Key messages

- 1.1 **Our first key message is the same as we noted to you last year, i.e. we would wish that the incentive framework encourages ESO to work jointly and collaboratively with ELEXON for maximum consumer benefit.**
- 1.2 In the second six months of the ESO 2018/19 performance year, we noted to you that we had seen an improvement in National Grid ESO's performance in that ESO had starting to publicly recognise and acknowledge joint collaboration and working between ELEXON and ESO. This is a very welcome development. We will continue to work with ESO on initiatives going forward for the benefit of industry.
- 1.3 **Our second key message is that we wish to be able to compare our own code management performance with that of others, including ESO.** On this aspect we are concerned as to whether ESO incentives will continue to allow us compare our respective services. We are always seeking ways to improve our code management performance, as we expect ESO is and do this, in part, by learning from each other. We would therefore appreciate if the ESO incentive reporting keeps the transparency of code operations to continue to allow us, and others, to compare code services and carry out benchmarking to drive improvements to either the ESO or other Code Managers' services.
- 1.4 Our answers to your specific consultation questions are set out below. We have not answered every question.

2. Our answers to your specific questions on the ESO incentives framework

Q15. Do you have any views on our initial thinking for how the ESO roles framework should evolve?

- 2.1 We believe that the new ESO incentive scheme design has worked well overall in its first year of operation (2018-19), particularly the creation of the Performance Panel, whose expert analysis has provided what we see as valuable input to Ofgem's decisions on how well ESO has met its incentive targets. We agree with Ofgem that adjustments should build on this rather than replace the scheme with something different.
- 2.2 We agree that greater clarity in the evaluation approach and a clearer understanding of what excellent performance looks like will help all involved, including those of us, like ELEXON, who need to work closely with ESO on a daily basis to deliver the best outcomes for the consumer.
- 2.3 While we agree with ensuring that the ESO internal roles do not overlap, we note that in practice it may become increasingly difficult for us to measure our own performance in code management against that of ESO. Clearer comparison could enable us to both adopt and further develop industry best practice for the code management function. For us, transparency across all code managers and administrators is key.

Q16. Do you support the introduction of a defined set of ESO outcomes and impacts? If so, what should these outcomes and impacts be?

- 2.4 In principle yes. However, some of the examples given in the table on page 41 of the consultation seem high-level and non-specific. Perhaps testing the Outcomes against 'SMART' principles for objective setting would help.

- 2.5 It may also be appropriate to add an Outcome based on ESO's ability to adapt to the ever-increasing pace of change in the electricity markets and to be flexible enough to support change and innovation where this can be shown to be in the consumer interest.
- 2.6 And building on our first key message of collaboration, a 'coordinated approach across the whole energy system' must be interpreted more widely than collaboration with DSOs or for a transmission/distribution system view, but must include the electricity markets and other industry facilitators, such as ELEXON.

Q18. Do you agree the incentives scheme should be focussed on encouraging the ESO to provide an exceptional quality of service when delivering its price control funded activities? Do you agree with our initial views on what an exceptional quality of service would include?

- 2.7 We agree with Ofgem's proposals if 'robust stakeholder engagement and a high level of industry trust and respect' encourages ESO to work collaboratively with ELEXON, as one of its many delivery partners.

Q21. Should there be financial incentive implications for the ESO as a consequence of the business plan assessment process?

- 2.8 We agree with the Ofgem view that a robust initial business plan will make later monitoring of ESO's performance and achievements easier for all concerned; and that a financial incentive should help achieve this.

Q22. What if any changes might be needed to the incentives evaluation criteria?

- 2.9 For ELEXON, coordinated delivery of the plan is important, however incentivising ESO to be 'ambitious around its deliverables or timelines' (table row (d) on page 50 of the consultation) could be counterproductive and work against maximising consumer benefit if it does not take this into account.
- 2.10 When ESO and ELEXON need to work closely together, as we need to do to deliver wider Balancing Mechanism access and project TERRE, it is important that we work seamlessly together. Both of these initiatives were widely welcomed by industry as opening up competitive markets. In our view it is more important that ELEXON and ESO work together than, for example, one of us having a financial incentive to diverge from joint plans or to shorten delivery timescales at the expense of the overall project. So we suggest that ESO's role and incentives should be considered in the wider context of delivering consumer benefits together with its delivery partners, such as ELEXON.

Q.26 Do these arrangements [Performance Panel] give stakeholders the right platform to shape ESO activity and hold it to account for its performance?

- 2.11 Yes, we believe the Performance Panel has worked well to date.
- 2.12 We agree with Ofgem that the Panel and its administration could easily become very resource intensive. We particularly note the volume of reports that ESO produced for the last performance year was considerable and think that the Ofgem proposal to scrutinise the business plan ex-ante to enable more streamlined reporting from ESO on its performance could help alleviate this burden in future years. However we would highlight our earlier point about ensuring ESO can and can be benchmarked against other Code Managers.

END.