

## Electricity System Operator RIIIO-2 Stakeholder Group (ERSG)

Meeting 8 – 7<sup>th</sup> November 2019

Royal Horseguards Hotel, London

### Minutes

#### Attendees

##### ERSG members

Angelita Bradney	ESO- Company Rep
Stuart Cotten	Drax
Toby Ferenczi	Ovo
Sophie Hind	Technical Secretary
Alan Kelly	Scottish power Transmission
Andy Manning	Centrica
Nick Molho	Aldersgate Group
Charlotte Morgan	Chairperson
Kayte O'Neill	ESO – Company rep
Nina Skorupska	Renewable Energy Association
Fintan Slye	ESO – Company rep
Chris Veal	Transmission Investment
Matthew Wright	Orsted

##### ESO Support

Louise Clark	ESO- Observer
Alice Etheridge	ESO- Presenter
Craig Dyke	ESO- Presenter
Nikki Jamieson	ESO- Presenter
Gavin Lochead	ESO-Presenter
Jason Mann	TFI Consulting
Sally Thatcher	ESO-Presenter

#### 1. Conflicts of Interest (all)

No new conflicts of interest were raised

#### 2. Introduction, Minutes and Actions (Sophie Hind)

Open actions were reviewed and updates were given.

#### 3. Regulatory Framework– Ofgem (Closed session)

*Notes in separate document*

#### 4. Regulatory Framework (ESO and Ofgem)

The ESO re-joined the group and the chair gave an overview of things that required discussion in the wider forum. Ofgem were asked to give their view on where things lie with the shared services model.

Ofgem want to ensure that there is complete transparency over costs and where they are allocated to. This was also feedback from the Challenge group.

The chair explained that there are obviously benefits around the shared services model in terms of economies of scale, and asked whether it is a case of benchmarking and transparency of costs.

Ofgem think there are efficiencies to be gained from shared services. But benchmarking is crucial in order to understand the justification of these, as well as transparency. The ESO might look to explore how these services are procured.

The ESO asked how this differs to the current model. Shared Services arrangements were agreed through legal separation, and the price control does not provide an opportunity to unpick this. ESO are not aware that re-visiting how shared services were procured was an option.

Ofgem replied that the license does not specify what is included in shared services one of the areas they had questions around is IT, as this can cover such a large range of activities; from day to day support to the development of new systems.

The ESO explained their understanding that the documentation around legal separation specifically states how these things should be organised and that they don't interpret it as something that could be changed. Therefore, it is not an option to explore how the ESO might do things differently.

The ERSG asked if costs for information on how costs for Shared Services were allocated. The ESO explained that there are different arrangements for each service based on what is most appropriate. These arrangements are approved by Ofgem. There is a financial model which shows how this is allocated and the business plan has an annex which explains how this works. The group asked Ofgem if there was anything additional that they were looking for.

Ofgem's opinion was that the model was created for a different world, and they have questions around where projects, systems and assets are predominantly ESO assets and how appropriate it is to still have the shared services model. The chair added that the concern from the Challenge Group was around the IT.

One group member raised concern if these arrangements were to be revisited annually, as this is not consistent with the price control setting.

The ESO summarised that there is potentially a serious difference in opinion on the shared services model. If there is potential to re-visit this model, then there could be implications for the ESO business plan and also other business plans in the NG Group.

*Ofgem left the meeting*

The ERSG summarised the key issues discussed with Ofgem for the ESO. The majority of the discussion was around risk in the company and how the finance and funding worked, and whether that gives enough flexibility for innovation. In terms of risk and risk structure, Ofgem explained that discussions were ongoing, and that they have asked for further justification on this from the ESO.

There was also an open conversation on cost disallowance. Ofgem see this as a small, unusual risk. The ERSG advised Ofgem that they give further guidance on disallowance. IT projects were discussed, and the group expressed the view that that the funding structure could make the company risk averse. The idea of a risk contingency pot was discussed, which Ofgem seemed relatively open to on the basis that they understood the point that the group were making. Ofgem are going to take this away.

Incentives were then discussed and where upsides might be. Ofgem want to ensure that they are rewarding out-performance as opposed to BAU performance. Ofgem questioned whether there was enough specificity in the business plan to allow for assessment of this. Existing incentives were also discussed, and how they may be made to work.

ERSG explained that Ofgem seem more concerned with over-recovery than they are with closing the risks. Attempts to deal with the risk by allowing bigger profit seem to go nowhere. It may be more productive to work on how the risk can be mitigated. If the ESO were to divorce this from the reward, then discussions may progress further. Ofgem were questioning whether the ESO wanted to see the risks removed or whether they wanted the potential to earn a higher reward.

The ESO replied that this captures the difference in opinion between the two parties. The ESO feel that they are being pushed towards charity / not for profit by Ofgem. They are not looking for a large reward to cater for risk / disallowance. They want a framework which reflects the business and activities that they undertake. There is a significant amount of activity performed by the company which is not remunerated

While the ERSG felt that Ofgem accepted the decisions and outcomes of the SONI CMA case, the ESO felt that this was the opposite of what they had previously heard from Ofgem. Ofgem have created the potential for additional remuneration, but they still believe that this should be set at 0. This was different to what the ERSG felt they had heard, as they felt Ofgem were open to the company presenting more evidence on what the risks were. They had accepted that there is risk in dealing with other people's money.

The ESO pointed out that they have asked the ESO to quantify the risk, but even in the SONI CMO case they were unable to quantify this risk.

ERSG continued to summarise that they had conveyed very strongly the desire for the ESO to be able to take risk and be allowed to do so. Ofgem's requirement for proof of risk is understandable but they need to accept that risk is inherent and difficult to quantify. The question is how to meet them in the middle. The group advised that the ESO need to avoid spurious accuracy, and that the benchmark should be a range.

The ESO asked if there was any appetite from the group to send a note to Ofgem which summarises what was discussed and what was suggested.

## **5. Business Plan- Summary of changes since October (Angelita Bradney)**

The presenter gave an overview of what had been updated in the business plan in the previous meeting. They also went through the feedback letter from the Challenge group which was shared with all ERSG members during the meeting. The group asked for some clarification on why the RAG status on Stakeholder Engagement was amber/red. The company explained that there is some concern on who has been engaged and how widely stakeholders have been engaged. Also, uncertainty on how engagement relates to buy-in. The ESO plan to provide more evidence on this around the Design Authority in the next version. Further Challenge group feedback was that the content in the plan focuses on stakeholder engagement around the plan itself, rather than wider engagement. The ESO are also looking to address this.

The ERSG asked the company to expand on the IT strategy. There's a large up-skilling planned but also a reliance on framework providers. How the split work across in house vs external? The ESO are trying to use a flexible model. ERSG feedback was that the end goal in this area still wasn't clear. The ESO agreed that they would work to clarify this further.

In the Challenge Group feedback on theme 2 they question whether the ESO is the right organisation to deliver the new IT system. The group asked if any more detail was given on this feedback. The ESO weren't aware of any information and don't believe that this had been discussed at any of the meetings.

Further feedback stated that interdependencies on delivery with other market parties still need to be addressed in the business plan, and the ERSG agreed with this feedback. The ESO explained that the Design Authority is the main way that they will address interdependencies and they also understand that they need to further demonstrate their connections with DNOs and other network companies. The chair asked if there were any views in the room on the ESO's relationship with network companies. It was acknowledged that DNOs are a challenging relationship. The ESO is a new organisation and so there is tension between how far they go and how restricted they become. For this reason, they can be perceived as stepping on toes and crossing their boundaries of roles and responsibilities. If the ESO help the industry to recognise that this is the case, then it might help with these relationships.

**ESO confirmed that they would send an updated digitalisation strategy document to the group in the following week.**

## **6. Metrics (Gavin Lothead)**

The presenter gave an overview of the metrics proposed by the ESO.

## Theme 1

Ofgem proposed the idea of having core metrics, and the ESO would consider metrics in this sections to be core.

The ERSG asked how the metrics in this theme interplayed with the ambition for net zero. It is such a large aspect of the transition that you would expect to see it here. It was also questioned whether having a satisfaction survey on the Design Authority was the right way to understand whether it was working or not. The innovation is also not represented as part of these metrics. There needs to be focus on how the company are getting to the future and this will be done by measuring innovation. The ESO remarked that this was useful feedback and they will give it some consideration.

The group asked whether the intention of the metrics was for performance or reporting, or both. The ESO see them as reporting metrics, although recognise that they will probably need to link into incentives in some way. They are also a way of measuring ESO investments. They would assess what each investment is trying to do and have a metric linked to them so that each investment would have a metric linked to them. There is a real possibility that some of them would end up in the incentives framework. The issue today is that delivery against a metric does not ultimately result in a reward. A question to Ofgem is if the ESO are going to have metrics then what purpose will they be for?

With regard to metrics, the group asked how the company would deal with the fact that investment would be upfront and benefits may not be until further down the line. The ESO explained that this has been built into the current incentive scheme. However, the outcome of the first year of the scheme suggests that this has not worked well. Suggests that stakeholders' mindsets is not clear on the idea of future rewards.

The company were asked about proposed metrics on system reliability. The idea would be to measure unplanned outages on CNI systems. There was some confusion whether system reliability referred to IT systems or the network. The ESO confirmed that this was referring to IT systems and that they would make this clearer in the metrics. The company also agreed that they would also include a metric on security of supply which does not overlap with TO responsibilities/

One member raised a frustration that their company had repeatedly raised feedback around the Demand Forecasting metrics which has not been addressed. They believe that accuracy should be measured as a percentage rather than an absolute value. The ESO agreed to arrange a call with relevant people to make sure that this feedback was addressed.

**ESO to arrange a call with Demand forecasting team to address the above feedback.**

Further feedback in this theme was that the ESO could include a measure of diversity of ancillary service providers which would also be a good indication of progress in innovation. Ofgem and BEIS are looking at the BlackStart standard. If there is something like this that the ES) are able to

attach a hard metric to then they will but they need to wait for information on this standard to be released. The ESO will also consider if there is a way to include a specific innovation metric.

## **Theme 2**

The group referred to the metric which states “Proportion of balancing services procured competitively”. What is the proportion currently? The ESO agreed to take this question away.

**ESO to confirm current proportion of balancing services that is procured competitively.**

There was discussion around the “EMR decision quality” and whether this was appropriate. The group suggested that it would be good to have more pragmatism brought into the prequalification process. Equally the metric which proposes “consumer value savings from code modifications” was discussed, and the extent to which the ESO have control over this. It was concluded that this was more to ensure that value is being delivered by the process, and that its more of an industry measure than a measure on the ESO.

## **Theme 3**

The presenter gave an overview of the metrics proposed for theme 3, which were all related to the NOA process. The group asked for clarification on the “NOA participant mix” metric. It was clarified that this refers to non-network solutions, and measuring the move away from solutions being provided purely by the three TO companies. Clarification was also required on whether these metrics were intended to measure end of life assets, which links back to the question of what is an ESO role and what is a TO role. The ESO agreed to clarify this. They were also asked whether the NOA is purely forward looking, as an important metric may be to look back and see how decisions have out-turned. This is unlikely to be included as a metric but the ESO will look at including this in the NOA process. It could perhaps fit into theme 1 as an aspect of regular reporting and could be helpful in engagement with Ofgem.

**ESO to clarify theme 3 metrics and state whether they apply to end of life assets.**

**ESO to look at possibility of expanding NOA process to look back at previous year and determines if outturns were in line with assumptions.**

## **Theme 4**

For theme 4, the ESO were asked if something could be included on timelines and speediness of response. They confirmed that they were currently looking at a second metric on connections which would be more process based, and suggested that they may also need a “right first time” metric. This has been looked at previously but there were concerns over the extent of control that the ESO had on this. They agreed to take it away and have another look.

**ESO to consider whether a “right first metric” could be included relating to the connection process.**

A member of a TO company mentioned that they were also planning to survey customers that they provide network access to, and that it may be appropriate to have a common metric between ESO and TO.

**ESO and TOs to explore the possibility for a common metric around stakeholder satisfaction with connections.**

The ESO had also been looking at the possibility of having a network compliance metric and the group were asked for their thoughts on this. It was suggested that this may be more of a question on for the customer.

The group felt that there was a gap in the metrics on this theme, as there are currently none which relate directly to the title of the theme. It may be helpful to have a metric around frequency that policy and energy solutions are being provided. It may also be a good place for the ESO to include some metrics which references progress made in achieving the overall business plan, for example achieving net zero. The ESO confirmed that they had discussed including metrics along these lines in theme 1. The issue is how they ensured that they do not overstep their responsibilities with a metrics such as this. The group felt that it was more about demonstrating progress in the ability to operate a zero-carbon system. Having something which measures contribution to decisions seems central to theme 4, and the ESO are in the unique position to be able to do this kind of work. The ESO suggested that they will look at a simple critical path with a RAG status as a metric. The ERSG agreed that this would be helpful.

**ESO to consider a critical path of major milestones with a RAG status as a metric.**

The group remarked that there is a clear and positive aspiration to increase access and flow onto network with the network access metrics. They questioned whether there's a risk that this isn't balanced by a metric which allows network access to be taken. The ESO agreed to consider this in coordination with TOs.

**ESO to consider balance between aspiration to increase capacity of network and allowing access for outages in coordination with TOs.**

**Cross ESO Metrics**

The ERSG warned that the metrics should ensure that they differentiate what is beyond the control of the ESO. The company confirmed that they need to avoid a set of rigid incentives which are set 3 years out when they are proposing an agile delivery model. The performance structure needs to support agile delivery. Regarding the proposed metric on data shared, it was asked whether this is regular data or whether it also includes outcomes of studies, findings etc. The ESO intend to create a prioritised list of data so that they can transform it in a way that is more useable for the industry. The group asked that this is more explicit in the metric.

The ERSG reiterated the need for a metric on zero carbon. The ESO wouldn't necessarily need to be assessed against this, but it would indicate progress against the ambition. It is something that

needs to be visible whether the company are judged on it or not. The ESO agreed that this is important, as it is the ambition which holds the business plan together. It's what consumers will care about and will be high profile politically.

**ESO to include metric which measures progress against zero carbon ambition.**

**7. CATO Early Competition plan update (Craig Dyke and Sally Thatcher)**

The presenters gave an update on ESO plans for the CATO early competition plan, given that there was concern around how this has been approached to date. They explained that Ofgem have now made a decision that this piece of work should be progressed independently from the business plan. The first delivery output is required by the end of December this year, and the final plan is due February 2021. The ERSG asked what the output will look like at the end of Feb 2021; how mature will the proposals be and what further will need to be done in order to launch the model? Once the output is delivered by the ESO, it will then be handed back over to Ofgem and it isn't clear how they will manage it from there. Expectations for Feb 2021 will also clearly be set out in December this year. Legislative and license changes will most likely be required. It is expected that the final output will be beyond the conceptual level, and will be specific in what needs to be done. This will include a rulebook and a blueprint for implementation. It is unlikely that there will be specific drafting for license changes at this point but there will be detail of the changes required.

The group asked whether the ESO will be exploring models other than the early model, or whether they will be continuing from where Ofgem have left off. It was highlighted that one of the ways which this could be implemented was by the ESO being the procurer rather than Ofgem. In other industries utilities are the procurer rather than the regulator. Ofgem have little experience of procurement which could be problematic. Work that the ESO will undertake includes looking at who is best placed to run the model and Ofgem have specifically asked what it would look like if the ESO were to take this role.

ERSG also asked if the scope of the work will include competition for non-network solutions. The ESO confirmed that this will be built into the plan, and that there are some challenges around how you compare network with non-network solutions. This has been achieved elsewhere and the ESO will be considering these instances. There were also questions around the ESO's involvement in DSO level competition and how they see this working. Ofgem have asked this as an open question and the ESO are considering a range of options from running the competition to doing an audit of the competition, these considerations are still early in the process. The group felt that it's important to be clear that it is more about coordination than taking over the running of other people's networks, linking in to ESO's overarching role of efficient system operation. The group drew comparisons to the proposals around a connection hub, and that this is presented in a way which suggests that the ESO is looking to take over Distribution networks.

When asked whether the ESO are doing any work on the late model they explained that their focus is currently on the early mode as instructed by Ofgem. They would be exploring this if Ofgem went in this direction. The group asked where the push was coming from to explore



a design only competition format. The ESO weren't sure and thought perhaps the pool for competition was less limited because it's essentially a competition for ideas and could drive innovation. It would be a challenge to enforce credibility in this instance. It is possible that design could be extended to include consenting, which parties would not need a license for. The company clarified that the scope included onshore only, but that they are wary of making decisions which would close doors to an offshore rollout.

There is stakeholder frustration with the start stop nature of the process so far. Given that this is likely to involve license changes, the group urged the ESO to set out timelines for when updates will be given, to keep the momentum and pressure going.

#### **8. Roundup by Fintan, including delivery confidence (Fintan Slye)**

The presenter thanked group members for their ongoing input and explained that it was ERSG feedback which led to the decision to make the ambition of zero carbon operation by 2025 a central theme to the business plan. Two areas were highlighted:

- CATO model: The ESO hope it is now evident that they are actively progressing this work, and how they are doing so
- Shared Services model: The ESO have tried in the next iteration of plans to better articulate how this will work

The ERSG are very appreciative of how the company has responded to the multiple requests. They have been able to feedback positively on this to the Challenge Group and Ofgem. On the IT and Shared Service piece, the group asked who would own the IT relating to these projects. If consumers ultimately pay for these it is important that they also get any benefit arising from the IP. The ESO said that they would confirm this, but they think that it would sit with the ESO.

#### **ESG to clarify who will own Intellectual property of IT projects in the business plan**

The chair highlighted that IT projects do not have a good reputation or running smoothly, and asked to what extent the company learn from past projects, and take lessons learned into account in new proposals. The ESO explained that they do this, and that the way that the delivery model has changed is a result of reaction to lessons learned.

The company were asked how they see the split between staff and contractors. The ESO explained that there are targets set and in one area this will be 95% of NGENSO employees across teams. There is a lot of work to be done to reach this. The ESO are building their own capability internally and will go to providers once the development capability is designed and fully understood. There are plans for a big recruitment drive over the next 18 months in order to recruit approximately 300 people.

The group fed back that they felt the progress made on CATO has been good. Previous points of concern from the group have been covered off well. Time will tell as to how progress is made in this area and there was some support for an ongoing role for the ERSG in monitoring these plans. It would be good to see the ESO be more proactive than reactive in this area, it still seems that actions are in response to Ofgem's direction rather than the ESO taking initiative.

## **9. Future for ERSG (Alice Etheridge)**

The presenter summarised the proposals to continue with the ERSG group and asked some questions to the group on whether they think it is appropriate. The ERSG responded that they will consider the questions in the closed session and come back to the ESO with some thoughts. The ESO also committed to sending a note around about the Open Hearings and what to expect.

Again, the group thanked the ESO for the information and the huge amount of work that has gone into the business plan. The test for the ERSG will be whether the business plan is different to what the result would have been without input of the group. It feels like a great amount of change has been achieved and therefore the group has been a success.

## **10. ERSG Report Preparation (Closed Session)**

*Notes in separate document*