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Dear Charlotte,

## **Ofgem response to National Grid Electricity Transmission plc's Electricity System Operator's Consultation on the Electricity System Operator Forward Plan 2018-19**

### **Introduction**

Ofgem's principal aim is to protect the interests of current and future energy consumers. We regulate National Grid Electricity Transmission, as the Electricity System Operator (ESO)<sup>1</sup>, to help ensure the actions it takes align with the interests of consumers. We welcome the opportunity to respond to the ESO's [consultation on the Electricity System Operator Forward Plan 2018-19](#).

### **The ESO regulatory and incentives framework from April 2018**

We recently published our [decision](#) on changes to the ESO regulatory and incentives framework from 1 April 2018. Our new arrangements represent a material change from the previous approach. They aim to encourage the ESO to identify proactively how it can maximise consumer benefits across the full spectrum of its roles. Our decision includes a final set of Principles for the ESO; a requirement to develop a Forward Plan with stakeholders; a requirement to publish regular performance metrics and reports; the introduction of a new Performance Panel; and a move towards a broader, more evaluative financial incentive.

We expect this framework to remain in place for the next three years. However, we intend to keep it under review during the first year, and make any necessary refinements alongside the legal separation of the ESO in April 2019.

### **The ESO Forward Plan – our expectations**

A key objective for our future framework is to make the ESO more clearly accountable to its customers and wider stakeholders. We want the ESO to place its customers and stakeholders at the centre of its decision-making. We expect it to be continuously engaging with both existing and potential future stakeholders in order to identify how it can best meet its Principles and deliver additional benefits for consumers. This is why we are introducing a requirement on the ESO to engage with its stakeholders to produce a Forward Plan before the start of each regulatory year. This plan should set out the ESO's longer-term vision for how it intends to drive consumer benefits under its different Roles and Principles. It should also set out the specific steps the ESO intends to take in the year ahead to meet these aims. The final Plan should contain an unambiguous set of deliverables with clear dates and milestones.

As part of this process, the ESO should also propose a set of performance metrics linked to each of the Principles. These metrics will create transparency around the ESO's performance by helping stakeholders to track the ESO's progress against its Forward Plan. Each performance metric should be supported by performance benchmarks. These should set out and clearly justify what outcomes would

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<sup>1</sup> The ESO role is currently carried out by National Grid Electricity Transmission plc (NGET), which is also the owner of the transmission network in England and Wales. NGET is part of the wider National Grid plc group of companies. The ESO is due to become a legally separate function within National Grid plc from April 2019.

constitute performance that is: under expectations; in line with expectations; and exceeding expectations (with reference to the baseline behaviours and outcomes defined by the ESO Principles).

The Forward Plan will be a key input into the end of year incentive<sup>2</sup> decision, therefore it is important that the ESO develops a comprehensive and stretching set of deliverables and metrics. Overall, the plan should be ambitious. By that we mean:

- 1) A comprehensive breadth/coverage of tangible steps/activities/deliverables covering all the ESO Principles and;
- 2) A sufficient level of stretch in what constitutes expected performance levels.

We want to be as clear as possible to the ESO about the extent to which the deliverables and metrics in the ESO Forward Plan go beyond or fall below baseline expectations. Therefore, we have committed to providing a Formal Opinion. In reaching our Formal Opinion, we need to assess the final Forward Plan and be comfortable that the ESO has extensively engaged and responded to stakeholder feedback in order to validate the deliverables and performance metrics. The ESO also needs to evidence clearly how its Forward Plan meets and/or exceeds baseline expectations for each principle and the extent of additional consumer benefits its actions will create.

We have provided further [draft guidance](#) on the reporting and incentive arrangements, including the ESO Forward Plan.

### General comments on ESO Forward Plan

We have reviewed the Forward Plan, Delivery Schedule and Technical Annexe and have provided some overall comments for the ESO to consider alongside stakeholder responses as part of its consultation to develop the final version of the Forward Plan. **Please note that the views expressed on the draft ESO Forward Plan are indicative and not comprehensive. Our Final Opinion will be informed by our analysis of the ESO's final Forward Plan and a review of the stakeholder feedback received as part of the consultation process on the plan undertaken by the ESO.**

Overall, we appreciate the ESO's effort in engaging with the new reporting and incentive arrangements. As this is the first year of the new framework, we expect there to be a few iterations and discussions in order for the Forward Plan to meet our expectations and stakeholder expectations. We are pleased to see the ESO engaging proactively with the new framework and seeking stakeholder views through this consultation process and the ESO Forward Plan stakeholder events. Generally, we think the draft ESO Forward Plan looks promising in areas, but **the current metrics and level of explanation is not enough for us to determine whether the plan is ambitious overall**. We require more information (in the areas described below) in order to make a robust assessment of ambition.

### Our expectations

Our baseline expectations around each principle are defined in the [ESO Roles and Principles guidance](#).<sup>3</sup> The ESO Roles and Principles underpin the entire framework. So far, we are pleased to see that the ESO Forward Plan, Delivery Schedule and Technical Annexe have all been structured clearly to relate back to these Roles and Principles. In particular, the improvements and deliverables proposed under Principle 3 and Principle 7 appear broadly positive and link back to the expectations described in the guidance. We encourage the ESO to ensure the proposals in the Forward Plan across each principle meet the expectations set out in our guidance.

### Deliverables and improvements – Delivery Schedule

The structure of the Forward plan (in particular the Delivery Schedule) looks helpful and clear: setting out the key activities the ESO delivers today to meet the Principles; its ambition to improve; the benefits this will have; the metrics to measure performance and the outputs we will see in 2018/19. We encourage the ESO to provide as much **information and detail** as possible in each of these areas in order for us to assess and comment on the level of ambition for each principle. For instance, we think more detail is required on some areas, including:

- Current performance (under the 'key activities' section) – this would help to measure performance over time and to see how the ESO has improved from previous years.

<sup>2</sup> The ESO Performance Panel will use five key inputs to evaluate the ESO's performance: ESO evidence of delivered benefits; ESO evidence of future benefits / progress against longer term initiatives; stakeholder views; plan delivery and outturn performance metrics and justifications.

<sup>3</sup> We have recently published an updated version of the ESO Roles and Principles guidance which will come into effect from 1 April 2018.

- The 'improvements' sections of the Delivery Schedule – we would like to see the ESO explicitly justifying how the improvements proposed either meet or go beyond the expectations set out in the ESO Roles and Principles guidance. We would also like more justification for why the ESO has chosen to focus on these areas for improvement. The ESO will only be financially rewarded for carrying out its activities in a way that goes above and beyond the baseline expectations of a competent system operator, so as to drive additional benefits for consumers.
- The 'benefits and outputs' section:
  - Wherever outputs are included, we would like to see dates or milestones associated in order to measure the ESO's progress.
  - We would like to see more explicit information on the benefits (currently the Delivery Schedule refers to the performance metrics in the Technical Annex). Wherever possible, the ESO should be justifying why deliverables are chosen, by calculating or estimating, direct or indirect consumer benefits.

#### Performance metrics – Technical Annex:

We have not provided individual comments on each performance metric proposed at this stage, but our first impression is that it would be helpful for the ESO to include **more information relating to the metrics**. For instance, where stakeholder surveys are incorporated, we would like to see the Forward Plan specifying the detailed questions that will be asked as part of their consultation.

Generally, the metrics proposed should be **reflective** of the areas of 'improvements' and 'benefits and outputs' identified in the Delivery Schedule in order to demonstrate sufficient coverage. For instance, the metrics proposed to measure performance under Principle 3 reflect the areas of improvement and the outputs the ESO is working toward, therefore we consider these metrics to have sufficient coverage. Whereas under Principle 1, the ESO proposes a number of improvements in the areas of information provision, accuracy, transparency and engagement in its Delivery Schedule. However, the proposed performance metrics focus on publishing on time and accuracy, which does not cover all of the areas of improvement identified by the ESO.

The metrics proposed should also be **more outcomes focussed** as opposed to process/output focussed. We understand the quality of performance can be difficult to capture in ex-ante metrics, but we would still like to see the ESO drawing on stakeholder surveys and incorporating these into their metrics wherever possible as opposed to just including metrics that measure the timeliness of publications. We think that this is important to truly assess the value created for customers and consumers in that area. Wherever narrower process/output focussed metrics are used, we would expect this to be justified to stakeholders in the Forward Plan. We also note that where narrower metrics are used, this may result in more weight being placed on the supporting evidence collected throughout the year.

#### Overlap

The Roles and Principles have a large degree of overlap and interaction. Therefore we expect the ESO to identify and clearly articulate in the Forward Plan where improvements and/or deliverables are relevant for more than one principle. For instance, we think more work needs to be done to highlight the cross-cutting element of the whole system coordination work (Principles 5 and 6). The ESO should consider how coordinating across network boundaries and the optimal use of resources will have benefits across their other sections/principles and this should be articulated more clearly in the Forward Plan (at least at a high level). And ideally this should have corresponding metrics across these areas.

Furthermore, the outputs and metrics proposed under Principle 5 and Principle 7 appear to overlap with those proposed under Principle 7 – we would encourage the ESO to provide further detail and justification for this. In particular, metric 13 (whole system optionality) and metric 18 (NOA consumer benefit) appear to be similar as they are both described as measuring the number of non-transmission solutions identified through an extended NOA. Where metrics drive outcomes against more than one Principle it may be appropriate for these to be used to inform the assessment against each of these Principles. The ESO would need to articulate clearly this in the ESO Forward Plan.

#### Performance benchmarks for performance metrics

Without further detail it is difficult to comment on the level of ambition of the metrics but our initial thoughts (based on the information provided in the ESO Forward Plan) is that a number of the metrics could be **more stretching** (through setting more challenging performance benchmarks). For example,

we question whether looking at the number of consultation responses under metric 19 is an effective measurement of the quality of NOA engagement.

As mentioned previously, we would like more narrative / explanation on why certain performance benchmarks are set. This could be through providing evidence of existing performance (in order to give an indication of whether the suggested performance benchmark is stretching or not) and/or through evidence of consumer benefits (either calculated or estimated, direct or indirect consumer benefits).

We expect the ESO to meet its legal obligations as part of our baseline expectations. Outperformance of metrics (especially the 'exceeding expectations' benchmark) should not be set at meeting those baseline requirements. We also expect that improvements made during previous years should be "banked" as baseline for subsequent years.

**Overall we think the information described above will provide greater clarity on the level of ambition in the ESO Forward Plan as a whole.** We think this information is required across the principles in order for us to be more comfortable with the ESO proposals for 2018-19 in the Forward Plan.

### **Next steps**

We look forward to continuing to work with the ESO and stakeholders to refine the Forward Plan to ensure it is fit for purpose for the regulatory year 2018/19.

Once the ESO Forward Plan consultation closes, we expect the ESO to consider stakeholder responses, review and update its Forward Plan accordingly and publish the final version of the Forward Plan for 2018-19 before 1 April 2018.

We want to be as clear as possible to the ESO about the extent to which the deliverables and metrics go beyond or fall below baseline expectations. We have therefore committed to providing a Formal Opinion on this plan by 1 May at the latest.

Should you wish to get in touch with us in the meantime, please do so by emailing [electricitySoreform@ofgem.gov.uk](mailto:electricitySoreform@ofgem.gov.uk).

Yours sincerely,

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