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Call for Input: 18-21 ESO Incentives Scheme

Dear Louise,

We welcome the opportunity to respond on behalf of the National Grid Electricity System Operator (ESO) to Ofgem's Call for Input on the new ESO regulatory and incentives framework from April 2019. We are proposing some changes to make the framework even more effective in consumers' interests.

From April 2019, the ESO will be a new standalone business within National Grid, legally separate from all other parts of the National Grid Group. The ESO will have its own Board, and staff will be physically separate from all other parts of National Grid. This will provide the right environment to deliver a balanced and impartial ESO that can realise real benefits for consumers as we transition to a more decentralised, decarbonised electricity system.

Our Input:

1. We see the **ESO Roles and Principles framework** as sufficiently flexible to capture our current and any new / future roles and business activities; we therefore do not recommend any changes at this point. We welcome a discussion with Ofgem about the weighting of the Principles in the scoring framework and whether the current model of equal weighting appropriately focuses the efforts of the ESO on areas where it can create greatest consumer value.

We are also considering how this framework may evolve over the longer term for RIIO-2, when the ESO will have its own separate price control. We will include our thinking on this in our response to Ofgem's upcoming RIIO-2 Sector Strategy consultation.

2. We are generally supportive of the **Forward Plan process** and support early engagement with stakeholders on a draft version. In developing our Forward Plan FY19-21 we are keen to ensure an active and constructive dialogue with our stakeholders and to provide transparency on how we are responding to feedback. Our 28th September ESO 2030 Ambition event marked a first step in early engagement with stakeholders and we look forward to continued engagement via the forthcoming publication of our draft plan.

A lesson from this year is the importance of a clear baseline, agreement between Ofgem and ESO on what constitutes 'exceeding' performance, and the associated level of reward for delivering at that level. A clearer link between performance and reward would make the scheme even more effective. Ongoing dialogue between Ofgem and ESO throughout development of the 19/21 Forward Plan, along with clarity in the Formal Opinion can address this.

We understand that from April 2019 the Performance Panel will have a key role in reviewing and providing feedback on our Forward Plan, which we welcome. Our preference is for the "Formal Opinion" to represent a joint position by Ofgem and the Performance Panel. This will ensure that the ESO receives consistent

actionable feedback on its plan, metrics and deliverables which is necessary for the ESO to better understand how to prioritise improvement activities in line with consumers' interests.

3. Regarding **the Reporting Process**, we recognise that there are concerns from stakeholders that a more evaluative incentive scheme could make it more difficult to track our performance including compare current and past performance vs. a quantitative scheme where data can be easily compared. We would welcome the opportunity to discuss this feedback and consideration of any changes with Ofgem.
4. We found the **Performance Panel day** on the 20th of November to be a good opportunity to meet and engage with the Performance Panel and stakeholders on our Mid-Year evidence, answer questions and receive direct feedback that we can use and implement for our next Forward Plan and reporting. The morning session involved whole group presentations by the ESO Leadership Team on all the Principles, each followed by a whole group Q&A. We anticipate a refined approach at the End of Year Panel session to ensure a constructive and detailed feedback and discussion opportunity for stakeholders, as well as to encourage more stakeholders to actively participate.

It is our strong view that in principle all Panel members should attend both the Mid-Year and End of Year Panel day. This to ensure all Panel members have full sight of all information presented, and to afford an opportunity for the ESO leadership team to demonstrate how it is showing up differently in an external environment (under the new scheme and as a consequence of the ESO legal separation process). This is important additional information to consider in addition to the written evidence / reporting as part of the qualitative 18-21 scheme. In the event that a Panel Member cannot be present for good reasons then we suggest a fully briefed delegate of equal seniority.

We would like to emphasize the importance of a robust and comprehensive decision making process by the Panel regarding the penalty/reward for the ESO. This is a significant decision (-£30m /+£30m) for both consumers and the ESO and we would like to explore with Ofgem whether the current process is adequate to ensure this. Potential refinements to the process could include the opportunity to engage with the panel more fully on complex Forward Plan & Performance items, for example through a hosted session in Wokingham to allow time to deep dive with the ESO leadership team and others and have a detailed Q&A session. Such an approach would allow the Panel be fully briefed ahead of the "formal" Panel Days and determine where further information and challenge is needed the most.

Given the timing of this Call for Input we cannot yet comment on the outcome of the Mid-Year Panel day or the End of Year Panel day, the ESO performance scoring by the Panel or the financial outcome. We would welcome the opportunity to provide additional feedback after the completion of the first full year of the scheme.

5. On the **Incentive payment/penalty reconciliation licence change**, we welcome Ofgem's initial view that introducing this change to the Licence would benefit consumers. Through the ongoing customer interactions that we have as ESO, the feedback received supports this view that BSUoS customers find challenge in uncertainty around the reconciliation value driven by ESO incentive performance. We welcome Ofgem's proposed timeline to implement this change, subject to consultation, to ensure it applies to 2018/19 performance year and therefore realises benefit as soon as possible.

Yours sincerely

Kayte O'Neill
Head of Strategy and Regulation