

All interested parties,
stakeholders in GB and beyond,
and other regulatory bodies

Email: esoperformance@ofgem.gov.uk

Date: 9 October 2020

Dear colleagues,

Request for amendments on the proposal for defining and using specific products

On 18 June 2019, we¹ received a proposal² for defining and using specific products for balancing energy and balancing capacity (the specific products proposal) in accordance with Article 26(1) of Commission Regulation (EU) 2017/2195³ establishing a guideline on electricity balancing (the EBGL Regulation). The proposal was submitted to us by the Electricity System Operator (ESO) as the relevant Transmission System Operator (TSO) for Great Britain (GB), in line with our decisions on the assignment of obligations.⁴ The ESO is proposing to maintain the use of the existing Short Term Operating Reserve (STOR) and Balancing Mechanism (BM) products for the purpose of energy balancing.

This letter sets out our decision to request amendments to the specific products proposal in accordance with Article 6(1) of the EBGL Regulation and outlines the necessary next steps that must be taken.

¹ The terms “we”, “us”, “our”, “Ofgem” and “the “Authority” are used interchangeably in this document and refer to the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.

² See the ESO proposal for defining and using specific products at the following address:

<https://www.nationalgrideso.com/document/145721/download>

³ Commission Regulation (EU) 2017/2195 of 23 November 2017 establishing a guideline on electricity balancing. The EBGL Regulation came into force on 18 December 2017.

⁴ See Ofgem’s decision of 14 September 2018 on assignment of EBGL obligations at the following address:

<https://www.ofgem.gov.uk/publications-and-updates/decision-assignment-transmission-system-operator-obligations-under-guideline-electricity-balancing-regulation-within-gb>

Background

The EBGL Regulation requires all TSOs performing the reserve replacement⁵ (RR) process to develop a European platform for the exchange of balancing energy from RR. The Trans-European Replacement Reserves Exchange (TERRE) is the project to develop such platform, hence allowing Balancing Service Providers⁶ (BSPs) in GB to provide balancing energy to the ESO and other TSOs in Europe. The ESO will also be able to procure balancing energy from BSPs in other markets.

The ESO has submitted its specific products proposal pursuant to Article 26(1) in order to maintain the use of its existing RR products for the purpose of energy balancing once it begins to use the TERRE platform. In accordance with Article 26(1) of the EBGL Regulation, this proposal must contain the following information:

- (a) a definition of specific products and of the time period in which they will be used;*
- (b) a demonstration that standard products are not sufficient to ensure operational security and to maintain the system balance efficiently or a demonstration that some balancing resources cannot participate in the balancing market through standard products;*
- (c) a description of measures proposed to minimise the use of specific products subject to economic efficiency;*
- (d) where applicable, the rules for converting the balancing energy bids from specific products into balancing energy bids from standard products;*
- (e) where applicable, the information on the process for the conversion of balancing energy bids from specific products into balancing energy bids from standard products and the information on which common merit order list the conversion will take place;*
- (f) a demonstration that the specific products do not create significant inefficiencies and distortions in the balancing market within and outside the scheduling area.*

We note that the ESO does not intend to convert balancing energy bids from specific products into balancing energy bids from standard products. As a result, no information was submitted in line with Article 26(1)(d) and (e).

⁵ 'Replacement Reserves' or 'RR' means the active power reserves available to restore or support the required level of FRR to be prepared for additional system imbalances, including generation reserves.

⁶ In accordance with Article 2(6) of the EBGL Regulation, "Balancing Service Provider" (BSP) means a market participant with reserve-providing units or reserve-providing groups able to provide balancing services to TSOs.

Decision

We have reviewed the proposal submitted to us in line with the requirements of the EBGL Regulation, the wider objectives of the Regulation (EU) 2019/943⁷ (the Electricity Regulation) and our statutory duties and obligations.

We have concluded that the proposal cannot be approved in its current form and that it needs to be amended.

Our principal concerns relate to:

i) Optional Downward Flexibility Management

Since the submission of the specific products proposal, the ESO has introduced a new replacement reserve product, the Optional Downward Flexibility Management (the ODFM)⁸. The ODFM service provides the ESO with additional downward flexibility. While ODFM forms part of the terms and conditions related to balancing (the balancing T&C) pursuant to Article 18 of the EBGL Regulation, it does not form part of the specific products proposal despite being defined by the ESO as a Replacement Reserve product. Considering that the ESO indicated a need to use the ODFM product in its submission of the balancing T&C,⁹ we believe that the ESO should include ODFM in the specific products proposal following our decision to amend the balancing T&C.¹⁰ In our decision we noted that the balancing T&C would have to be amended to comply with the requirements of Article 6 of the Electricity Regulation for standard and specific products, at least for their part related to the ODFM. We therefore expect that the ESO will also propose amendments to the balancing T&C regarding the design of ODFM at the same time as it submit its amended specific products proposal.

ii) Compliance with Article 26(1)(b)

In accordance with Article 26(1)(b), the specific products proposal should demonstrate that standard products are not sufficient to ensure operational security and to maintain the system balance efficiently or should demonstrate that some balancing resources cannot

⁷ Regulation (EU) 2019/943 of the European Parliament and of the Council of 5 June 2019 on the internal market for electricity, available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32019R0943>

⁸ A description of the service is available here: <https://data.nationalgrideso.com/ancillary-services/optional-downward-flexibility-management-odfm1>

⁹ See the ESO's letter dated 23 June 2020 on the Optional Downward Flexibility Management Terms and Conditions, available at the following address: <https://www.nationalgrideso.com/document/172631/download>

¹⁰ See Ofgem's decision dated 03 July 2020 on Optional Downward Flexibility Management in relation to the Terms and Conditions related to Balancing at the following address: https://www.ofgem.gov.uk/system/files/docs/2020/07/decision_on_optional_downward_flexibility_management_in_relation_to_the_terms_and_conditions_related_to_balancing_.pdf

participate in the balancing market through standard products. Even though the specific products proposal relates only to RR balancing products, the ESO has so far not provided sufficient description of why the RR standard products are insufficient and has mainly referred to the FRR process. We believe that the ESO should focus specifically on providing evidence on why and how the use of specific products BM and STOR, as RR specific products, would be necessary and why the RR standard product is not sufficient.

From the information provided by the ESO, it seems that the main benefit of the specific RR products is a shorter full activation time than the standard product as well as the ability to dispatch units at a particular location. However, information is not provided to explain why having a specific RR product with a shorter full activation time than the standard product is necessary and why this is preferable to using more frequency restoration reserve to balance the system. We ask the ESO to provide us with this additional information in its resubmission.

Moreover, the ESO has noted that it will need to be able to use the BM to unwind actions taken on TERRE through BM activations as it had described during Grid Code modification GC0097. However, it is not clear in the proposal whether the ESO would unwind the actions via the BM or would avoid activating a TERRE instruction due to unavailability. The ESO should clarify this in its resubmission.

iii) Compliance with Article 26(1)(c)

In accordance with Article 26(1)(c), the specific products proposal should describe the measures proposed to minimise the use of specific products subject to economic efficiency. We believe that the specific products proposal does not provide a sufficient description of those measures.

In the specific product proposal, the ESO states that the platform for the standard RR product will allow TSOs to put a limit on the price of the standard RR bids. The ESO then notes that it expects to use this feature to procure the volume from the platform when economic to do so. While we understand the flexibility available in the platform to enable TSOs to price their imbalance and the ESO's intention to use that flexibility, it has not provided a detailed description of the process it will use to price imbalance needs in the platform.

Moreover, it is unclear what would be the circumstances that would lead the ESO to use specific or standard products. We would like the ESO to provide details on the processes

and decisions that will be taken to minimise the use of specific products, subject to economic efficiency.

We furthermore note that the specific products proposal states that the ESO will be performing post-event analysis which will allow it to identify how its strategy for balancing will evolve. We would like the ESO to describe what the post event analysis will involve and in what way it will allow the ESO to assess how it has minimised the use of specific products subject to economic efficiency.

iv) Compliance with Article 26(1)(f)

In accordance with Article 26(1)(f), the specific products proposal should demonstrate that the specific products do not create significant inefficiencies and distortions in the balancing market within and outside the scheduling area.

The proposal suggests that the specific products will not create such distortion as it will only be used in instances where the ESO is required to manage voltage, the risk of certain losses and to solve import/export thermal constraints, which are not services provided by the standard product. We would like the ESO to confirm whether specific products will only be used for system needs or whether it could be used to resolve energy needs. We also ask the ESO to include a description of the activation purpose of the specific products in its submission for compliance with Article 26(1)(b).

Moreover, the ESO claims that there would not be a distortion from these specific products by noting the insufficiency of standard products to resolve system needs and how using specific products is more economic and efficient. As noted in the section describing our requests for compliance against Article 26(1)(c) we would like the ESO to describe how the pricing methodology will ensure that specific products are only used in the event that it is more economic and efficient to do so. We would also like the ESO to elaborate on how its decision to only activate specific products when economic and efficient to do so will minimise any distortion to the balancing market. Finally, the specific product proposal does not provide a justification on why using specific products will not create distortions and inefficiencies outside the scheduling area.

Next steps

The ESO must make the necessary amendments to the proposal for specific products to address the points summarised below and re-submit an amended proposal to us within two months of this decision.

For the resubmission, we request the ESO to amend the specific products proposal to:

- 1) include the ODFM. In doing so, the ESO should ensure that ODFM complies with the requirements of the Electricity Regulation;
- 2) provide specific evidence on why the RR standard products are not sufficient to ensure operational security and maintain system balance efficiently;
- 3) provide a justification on why there is a need to use specific products instead of buying more TERRE and explain why this action wouldn't be sufficient to solve the issue and why unwinding balancing actions via the BM is preferable to not activating a TERRE instruction;
- 4) provide a more detailed description of the process that the ESO will use to price imbalance needs in the platform;
- 5) explain what circumstances would lead the ESO to use specific or standard products subject to economic efficiency;
- 6) explain what the post-event analysis on use of specific products will involve. Also explain how such analysis will allow the ESO to assess how it will minimise the use of specific products subject to economic efficiency;
- 7) confirm the activation purpose of the specific products;
- 8) explain how this pricing methodology will minimise distortions by ensuring that specific products are only used in the event that it is more economic and efficient to do so; and
- 9) explain why using specific products will not create distortions and inefficiencies outside the scheduling area.

If you have any queries regarding the information contained within this letter, please contact Alastair Owen at Alastair.Owen@ofgem.gov.uk.

Yours faithfully,

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