Electricity System Operator RIIO-2 Stakeholder Group (ERSG)

Meeting 5 – 4ᵗʰ June 2019

Amba hotel, Marble Arch, London

Minutes

Attendees

ERSG members

Angelita Bradney	ESO – Company rep
Peter Emery	Electricity North West
Sophie Hind	Technical Secretary
Jo-jo Hubbard	Electron
Alan Kelly	SP Energy Networks
Andy Manning	Centrica
Catherine Mitchell	Exeter University
Charlotte Morgan	Chairperson
Kayte O'Neill	ESO – Company rep
Eddie Proffitt	Major Energy Users Council (MUEC)
Simon Roberts	Centre for Sustainable Energy
Fintan Slye	ESO - Company rep
Jamie Stewart	Citizens Advice Scotland
Chris Veal	Transmission Investment
Barbara Vest	Energy UK
Matthew Wright	Orsted

ESO Support

Kashia Anderson	ESO- Observer
Pirvinder Bansel	ESO – Presenter
Alice Etheridge	ESO- Presenter
Nikki Jamieson	ESO-Presenter
Emily Leadbetter	ESO- Observer
Julian Leslie	ESO - Presenter
Cecile Marion	ESO- Presenter
Cathy McClay	ESO- Presenter
Richard Smith	ESO- Presenter
Carolina Tortora	ESO- Presenter
Gary White	ESO - Presenter

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

   The Chair invited feedback on whether members had identified potential Conflicts of Interest relating to the proposed agenda. It was confirmed that Stew Horne was not attending the meeting due to potential conflicts of interest as a member of the Challenge Group.

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

Open actions were reviewed and updates were given. The majority of open actions were met by the content of the meeting.

3. Stakeholder and Consumer engagement – Alice Etheridge

The presenter outlined the enhancements which had been made to the stakeholder strategy since the January meeting following internal and external reviews (slides 8-12). ERSG were asked for their views on whether the company have stepped up sufficiently in this area, as well as for opinions on the proposals.

Some members felt there was evidence of a culture change, which needs to continue to be built on. Continuing with themes of increased transparency and inclusivity. The ideas and aspirations presented are heading in the right direction, but they need to become the norm. All stakeholders need to be included at key points rather than as an exception. This will help to build trust.

Other members felt that the evidence was all anecdotal, and that the Marketing Pod report was weak in terms of highlighting what is best practice. It was highlighted that slide 12 says that NGESO will be "Championing the priorities of the consumer internally through our Customer and Stakeholder team". It was questioned whether stakeholders have been asked about this and whether they want the company to do this? There is still a lack of structure and ongoing strategy. These things would provide greater ability to push back on what Ofgem are saying, as they don't appear to be listening and their changes don't seem to reflect stakeholder feedback.

It was noted that while all monopolies in the industry were being encouraged to increase stakeholder engagement, there is a limit to how responsive you should be to this. The company should have a clear sense of what needs to be achieved, and in some cases this may mean pushing back on stakeholder feedback. Its important to be clear on what you are taking from stakeholders in the strategy that is set out. The example of promoting competition was used to demonstrate that not all stakeholders are going to be supportive of everything. The key is how you demonstrate the balance. Having different voices in the conversation is where you will get support for competition.

From a consumer perspective, there is quite a lot of evidence already available, such as academic work. Consumers don't necessarily need to be asked if they like the Business Plan because they won't care, but this information should be used to inform the wider public and cultural setting within which the business is operating.

Some felt that the "light-touch" approach for consumer engagement is the right one. It was questioned whether the role of consumer champion is Ofgem's role rather than the ESO's. It was suggested that ESO should not be a champion for consumers as such, but evidently responding to consumers' needs.

The fact that consideration of stakeholder views is very present throughout the plan. But where stakeholder feedback is mentioned it would be better to provide more detail. For example, was the feedback from one stakeholder or a group? Was it a survey?

Some specific examples of recent stakeholder engagement were discussed. Despite best efforts the webinar on competition through transmission was not well attended and very limited feedback was given. Power Responsive was mentioned as an example of great stakeholder engagement, although it had become more dominated by storage which has meant consumer providers are less engaged.

The example of Anglian Water's stakeholder engagement approach was discussed, and the importance of control that was demonstrated throughout their strategy (plan, do, check, act), as well as the multiple channels that they used. The ESOs Future Energy Scenarios (FES) document was used as a good example of where agreements and disagreements are clearly represented.

Summary

The chair summarised that the ESO have taken positive steps to address feedback from stakeholders and consumers. But that greater clarity is needed on the source of feedback in the main body of the report. More evidence of where academic work has been consulted and incorporated into the plan and how it has informed your understanding. It would also be good to have further clarity what feedback you are and aren't taking on board, and being clear when feedback is not agreed with.

The ESO responded that for the October version of the Business Plan they will be taking a further look at academic reports and how they can engage with academics. From reports they have already referenced such as the Green Alliance consumer energy report, they will be aiming to pick out key stakeholder groups mentioned and engaging with them directly. The company also confirmed that further detail on the stakeholder engagement strategy could be found in the annex to the main document, which aims to provide further robustness to the overall strategy, but that it was perhaps still lacking the context of some of the options that were discussed with stakeholders throughout the process.

The chair suggested that groups of stakeholders could be referenced more specifically in the main body of the report. set out an action for the ERSG to read the Stakeholder Engagement annex and then take a view on whether some of the feedback is still relevant.

Action for ERSG to read the stakeholder engagement annex and provide a view on whether feedback given during this session still stands.

Action for the ESO to provide more detail in the Annex about options presented to stakeholders at the different events and provide a better breakdown of stakeholders that attended/provided feedback.

4. Ofgem's sector specific strategy decision (Angelita Bradney)

The presenter gave an overview of Ofgem's decision for the ESO, as well as the funding model options that they have proposed (slides 13- 18). ERSG were asked to give their views on these options as the ESO prepares their consultation response.

Ofgem are consulting on two models, neither of which provide a layered model with a risk based margin that has been discussed previously. The first model is a return to RAV / WCC like in T1, and the other is based on 100% cost pass through which will be reimbursed throughout the year.

One member asked if it was still possible to disagree with both models that Ofgem had set out, or whether these were now finalised as the only possible options. The ESO confirmed that their response will set out that neither models are appropriate. Ofgem believe that a cost pass through means zero risk for the ESO so no margin will be allowed. They don't recognise a risk associated with running the business. The ESO fundamentally disagree and believe that Ofgem are taking an overly simplified view.

Some members of ERSG agreed that this seemed like an oversimplification and that a margin for risk should be allowed. One member commented that by looking at the difference in prices of IT projects that have a fixed price vs variable price, it would be clear why it's better to hold margin.

It was questioned whether Ofgem were trying to push the ESO towards something other than what has been set out in the business plan. At a senior level Ofgem have suggested to the ESO that they are in line with our ambitions, but on other levels they seem more concerned with minimising costs and risks. In the ESO's opinion these don't fit together.

The group discussed what behaviours this would result in. The key question is from a consumer perspective, does the model of cost pass through drive a better result?

If the company does not have any risk margin then how would it absorb a shock? It was discussed that if the company doesn't have equity or "skin in the game" its very difficult to drive down the cost of delivery. The Crossrail project was given as an example, where the company spends more to ensure that risk doesn't happen and this doesn't push prices down.

Without certainty on the funding model its difficult to judge the finance-ability of the business plan. The ESO raised a concern that there will not be clarity on this before the October business plan.

The chair asked why Ofgem felt it was appropriate to move away from a layered model, and the ESO confirmed that Ofgem felt that there was no risk left in the business due to legal separation and that they could not justify margins. The Chair raised her concerns about a lack of clear communication on this point between the company and Ofgem.

The group questioned the ESO, about how a funding model like this would impact the business plan. If the outcome was one of the options set out by Ofgem, what would you need to pull back on, or if there's a way to achieve these things with this structure.

ESO to set out what the two options mean for the business plan, and what impacts they have for consumers for the July meeting.

The group discussed that the proposals are more like a not for profit structure. The ESO would need assurance / approval from Ofgem on each project if this was the structure. It was questioned whether Ofgem have the authority to convert a commercial business into a not for profit.

5. **Business Plan Overview – Kayte O'Neil.**

The presenter gave an overview of the Business Plan (slides 19-25). An overview of the type of company that ESO are trying to become, with an emphasis that the Business Plan is not a "shopping list", but a coherent plan which will deliver the ambition and key outcomes.

One member commented that one thing missing from business plan was the ESO interaction with National Grid Group. Interconnectors seemed to be highlighted as a special group throughout the plan.

Slides 23 and 24 summarised overall costs and benefits. The group commented that it was quite difficult to see what the overall value is, and that it would be helpful to have a summary table bringing all of this together. The ESO confirmed they are working on articulation of the CBA and diving down into the detail of how the plan will be delivered. Further work will be done on ensuring that costs are easier to understand. It was questioned how useful this information was in the context of a 100% pass through model, and that it would be better to focus on risks. It was also noted that it isn't clear how the incurring of new costs would impact existing costs (and whether these should go down as a result).

ESO to include summary table of costs and benefits in October Business plan, and to provide a demonstration of impacts to existing costs.

Some of the group felt that the benefits were subjective and fluffy, and more info was needed on how these figures were arrived at. If the regulators decide on a cost pass-through model, then it would be more appropriate to focus more on the benefits in the plan. The ESO noted that more detail on the Cost Benefit Analysis could be found in the annex of the business plan.

6. **Ensure reliable, secure system operation to deliver energy when consumers need it – Richard Smith**

The presenter summarised to theme 1 of the Business Plan (slides 26-33).

There were some questions from the group about the Digital Twin concept included in this section of the plan. The ESO confirmed that the twin would look like a test and simulation environment. It will allow the proposal of changes that can be sandboxed in a more open environment, and allow the exploration of market rules. This would be more interactive and allow market participants to try things out. It is a more modular approach currently being trialled by the Platform for Ancillary Services (PAS) project.

The Chair asked if this proposal was the most cost effective solution. The ESO confirmed that this option comes out around 5% more expensive, but carries less risk as doing things in the current way will not deliver what is needed.

A member of the group highlighted the challenge that market participants are going to have different ways in which they wish to interact, how can the ESO strive to ensure that what's being delivered is fit for purpose for as many people as possible, which may entail more traditional providers needing to change their ways. The importance of including elements such as secondments

to other companies was highlighted as mitigating this issue. The ESO added that establishing a Design Authority should also help with this. It was also noted that a better understanding of how the ESO and DSOs will work together in this area would be useful.

The ESO took an action to arrange a follow up session with Alan Kelly to discuss the finer details of the Digital twin proposal.

There was general consensus from the group that this seemed like the right solution given the small additional cost vs large potential consumer and security benefit. Although, some needed further clarity on what the digital twin solution involves, including to what level will be twinned (every asset etc?)

The presenter asked for some further feedback on the People and Capability aspect of this section. Scarce engineering resource will be a key challenge and additional skills will be needed such as economic and data science combined with power system engineering. The group were asked about the best way to pursue this.

The importance of work life balance was noted. Some of the group felt that this is the biggest delivery challenge facing the ESO. It will be necessary to partner with universities, the ENA, and campaigning is needed to ensure that it's seen as an attractive career path. People with relevant skills are being attracted to industries such as gaming. Work will also need to be done with younger people to influence their choices.

The ESO has proposed the creation of an academy, and the group asked how much this would cost to establish. This will depend on exactly what form it takes. It seems that universities are already doing things in this space so it would be most efficient to work with what's already there, and the ESO don't have to be the sole driving force.

7. **IT Strategy and Cyber – Nikki Jamieson, Gary White & Pirvinder Bansel**

The presenters gave an overview of the IT strategy section of the business plan, along with how feedback from previous meetings had been incorporated.

The presenters were asked where the Design Authority would sit – would it be a senior, budget level group or more detailed? The ESO responded that it would most likely be a combination of the two – a group empowered to make decisions plus people with a more detailed knowledge. It will most likely be an overarching steering group with smaller groups per project. ESO would have overall decision making authority.

A concern was raised about the resource implications that this could put on market participants. The kind of resources needed by these groups is very expensive, and small businesses may not be able to spare this. The ESO confirmed that they would need to find a balance to ensure that it isn't just larger parties participating.

At the previous ERSG meeting the presenters were asked about the capability at board level to deliver this scale of change and expertise; they were asked to provide a further update on this. The ESO confirmed that a Chief Information and Digital Officer had been appointed, and agreed that more information could be added on the cultural shift and the people that are being brought in to

allow this. It was noted that the culture change needs to be across the company and not just the IT department, so that the entire company is focussed more on IT.

The chair summarised that there had been a major step forward in this area since previous discussions, but more depth is needed in terms of demonstrating understanding of the cultural and operational change required.

8. Transforming participation in smart and sustainable markets – Cathy McClay

The presenter gave an overview of Theme 2 in the business plan (slides 46 – 56).

One member commented that they didn't get the sense that much would be changed through the Ofgem codes review, more just a case of digitising the codes. The ESO confirmed that they believe more needs to be done, and the content needs to be reviewed too. The company are currently working on an example of what this might look like. It was questioned whether this approach needs to be more industry led and whether its in the ESO's gift to transform the codes. The presenter confirmed it would require collaborative working with other parties such as distribution companies.

The costs and benefits relating to this section were discussed. The group felt that the accuracy in the figures was not helpful and that it would better to have a range. The ESO were asked whether there are other places where markets are close to real time where an idea of the value can be drawn from. The presenter explained that other markets are looking to us for market design.

There is a real opportunity in this area to demonstrate the benefit, and so it needs to be well supported and move Ofgem's focus from the cost to the magnitude of benefits that can be achieved. If this is not achieved, then it limits the benefits that can be realised throughout the market. The presenter agreed that markets are a key enabler to unlock the value because it is what attracts new participants, and agreed that this could be emphasised much more here. The ESO were asked whether they could take this further and create closer to real-time markets. The ESO are focussing on getting the day ahead market working first, and intraday will be further down the line. The ESO agreed that they could to change the wording in relation to this so that it says "at least day ahead".

Another member was pleased about the information on long term markets, because this is important for new businesses that need investment to have some longer-term certainty. The ESO agreed with this, but added that there is an important balance between long term and short term markets. If you lock flexible assets into long term contracts, you remove the value of the flexibility, and if we only had long term contracts then consumers would overpay. However, it may also be that for long term contracts you can get a better price. Anyone investing will need a balance of long-term, they can't handle everything short term. It was agreed by the group that these kinds of issues need to be set out against the five-year control period.

The ESO were asked if this change was realistic in two years. The presenter explained that it is doable in the timescales, and all the thinking and direction of travel is already happening now.

9. **Open Data and unlocking zero-carbon system operation and markets – Richard Smith**

The presenter gave an overview of ESO proposals to make our data open and accessible and provide a clear route to services. Overall principles of share quick and share simply.

The group asked who will have access to the data and whether this approach would cause any security issues. The ESO are thinking about providing open access to data where possible. Its important to really understand the categorisation of data in terms of commercial confidentiality and CNI. There is plenty that could be shared and not misused. The point is that you don't try to pre-empt what people will do with the data but ask people to let you know what uses they find for it. It's a very different way for the ESO to think about data but could bring lots of value, by letting the industry go ahead and use it.

The chair asked what kind of data the ESO will need to hold back. Anything categorised as CNI, for example details around black start capability which is important for national security infrastructure.

The ESO are hoping to start sharing some of this data before 2021 and will be prioritising by what's most likely to be most useful.

10. **Unlocking consumer value through competition in networks- Julian Leslie**

The presenter gave an overview of theme 3 of the business plan.

In reviewing the costs and benefits for this section, the ESO were asked where the capex cost comes from. They confirmed that it related to additional computing power required. The estimated benefit is derived from a combination of investments and when they need to happen and finding lower cost ways to achieve solutions, for example an intertrip scheme vs asset build can be a large saving. The calculation of benefit includes the scenario where a solution may be put in place by someone other than the ESO.

The ESO explained that the NOA is an annual process which flows through to TOs and can trigger them to make a request. It needs to be considered how it will work if the most cost effective solution changes from one year and the next, and how this will feed into funding models for the ESO and TOs. One member noted that the base case for these assessments will be just as important as the model.

The chair summarised that the group are broadly in favour of the proposals, although there are details to be worked out around how the funding works when plans change. There are impacts on the business plans of other entities that need to be considered here. Concerning the CATO regime, it was noted that the ESO have moved from reluctant to active participant in the proposals. The group are broadly in favour of the expansion of the NOA.

11. **Driving towards a sustainable whole energy future – Julian Leslie**

The presenter gave an overview of theme 4 in the business plan (slides 62 – 66). Proposals involve ensuring that decisions taken will optimise outcomes for consumers across transmission and

distribution, and taking Future Energy Scenarios (FES) work a step further to develop policy recommendations.

The group asked for some further clarity on what the company is proposing to do here, particularly around the connections portal which was discussed at the previous meeting. The presenter explained the Network Access Policy, where they work with TOs to see if they can shorten expensive outages to reduce cost. The ESO believe there is significant value to be unlocked by rolling this approach out across GB and working with DNOs.

One member asked if legal separation had any impact on costs, revenue and benefits from a whole system perspective. The ESO explained that they still operate a "one SO" model in order to maintain benefits of thinking across two fuels. FES is an example where employees are able to work across two fuel types, although there are a limited number of people in the business that can do this.

The group felt that the Capex cost figure in this section (£70m) was quite high compared to what is being proposed. The presenter explained that this cost was due to the system development required to facilitate model sharing, which is currently only done annually but will move to a monthly process and this will require a huge amount of data transfer and tool development to better understand the performance of the system. The savings in this area are being driven by the whole system solution and enabling distributed energy to contribute to the solution. Interfacing with DNOs in real-time will create new opportunities for connection, therefore creating additional capacity based on data without needing to invest in physical assets.

The group commented that they would like to see more clarity between the BAU and the transformational activities in the report. The BAU should not be exactly what is done now because there is no future world which allow operating like this. The ESO confirmed that the BAU in the paper involved what would need to be done to continue to operate in the same way as today. It was suggested that a new phrase be used to summarise this, similar to "the new normal".

It was also mentioned that TOs are putting very similar proposals in their business plan, so it is important to ensure that it all fits together correctly, and that the regulators incentivise it as a whole. Collaboration needs to be brought out as a key theme in this section.

Some of the group still felt uncomfortable about the figures in this section and felt that the cost was very high. It was also discussed that from the information given it was difficult to judge if the proposed solution was good value or not. It needs to be clear where spend is enabling benefit through other areas and that in some cases the spend will not automatically lead to benefit, other action needs to be taken off the back of this. The danger of double counting benefits is significant and needs to be highlighted to Ofgem.

In summary, the group felt that the proposed costs feel too high, and need to be revisited or further justification needs to be provided.

12. Innovation: Carolina Tortora

The presenter built the innovation presentation from the previous meeting (slides 67 – 74), including the development of the ESO innovation strategy and the prioritisation of issues. An example of a recent innovation project was discussed which enabled the correction of a generation forecasting

error. The presenter clarified that the £100m impact came from the fact that the policy on how much reserve needs to be held could be adjusted and less reserve was procured as a result. This saving flowed through to consumers. The presenter confirmed that information on the ESO innovation projects can be found on online [here.](#)

There was a conversation around at what point does an innovation project become business as usual. The presenter explained that innovation does not deliver the final product. A project will be handed over to business as usual once it has been successfully tested.

The chair clarified that the NIA allowance is currently a percentage of overall revenue, and asked whether this will continue to be the right model for the ESO now that it's a legally separate company. The ESO do not believe that this will be an appropriate model going forward, and that Ofgem will be consulting on this. Ofgem have previously proposed the figure being a percentage of BSUoS but stakeholders did not agree with this.

One member felt that innovation is presented in the Business Plan as a standalone element, and it needs to be demonstrated that it is integrated into the culture of the business. The presenter confirmed that the innovation team do not run the projects, and that this is built into the core teams. Another member suggested that innovation should be paid according to success of projects, but the presenter highlighted that if this was the case the innovation strategy would need to be much more risk averse. In some cases it can be difficult to track progress of day to day innovation. The group thought that the fact that the innovation team don't deliver the projects was positive in demonstrating that innovation is being built into the business. Most other companies have a different structure where the innovation team do deliver the change, and its harder to embed as BAU in this way.

13. Building our capability for the future: Cecile Marion

The presenter gave an overview of the ESO's strategy for resourcing effectively across the 4 themes in the Business plan (slides 79- 84). The people and capabilities that the ESO have today can not deliver the full ambition. The ESO are currently working on detailed quantitative analysis looking at the number of FTEs required and cross checking with supply, identifying gaps and exploring how to deal with this. Current estimates suggest that the ESO will be looking to recruit a further 200 people and this is not as a result of legal separation. The ESO are exploring partnerships with universities as well as how to pitch recruitment campaigns. The group asked whether there's potential for competition for resource between the ESO and DNOs who will be looking for similar people. The ESO can see that this may be an issue and thinking about how they can collaborate with the other companies to tackle the problem. The group highlighted the importance of flexible working and other benefits in attracting a good workforce. They also highlighted a moral responsibility of how you behave in this space, in attracting people from other countries etc.

14. July Meeting plan: Alice Etheridge

The presenter proposed that the next meeting is used to have a more detailed discussion on the regulatory framework. The remainder of the meeting can then be used by the ERSG to focus on production of the group report. The group agreed.

The ESO confirmed that they were immediately working on an updated version of the plan based on the feedback. One member highlighted that Ofgem are still consulting on the funding model, and asked how the business plan would reflect this. Will the plan be changed to reflect the two year plan rather than 5 for example. The ESO will still need to develop 5 years of costs but it will only be approved two years at a time. The Business Plan submission to Ofgem in July will respect the decisions that have already been made. Where things are still open, the plan will be based on assumptions that are within the envelope of the options.

The group discussed the option of submitting a group response to Ofgem's consultation. It was concluded that responses should be submitted on an individual basis. Instead it was suggested that the chair have a meeting with Ofgem to discuss their concerns about the proposals.

The Chair to arrange a meeting with Ofgem to discuss the ERSG concerns on funding model proposals, and seek clarification on the intention.

ESO representatives left the room for a closed discussion.