

## RIIO-ED2 LRE Volume Drivers Governance Document

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<b>Contact</b>	Joe Slater
<b>Team:</b>	RIIO-ED2
<b>Telephone</b>	020 7301 7263
<b>Email:</b>	Joe.Slater@ofgem.gov.uk

This document is version 1.1 of the RIIO-ED2 LRE Volume Drivers Governance Document referred to under Special Condition 3.9 of the Electricity Distribution Licence.

This document covers the arrangements for the Load Related Expenditure (LRE) Volume Drivers in RIIO-ED2. The purpose of the Load Related Expenditure Volume Drivers is to allow Distribution Network Operators (DNOs) to invest in their secondary network (ie high voltage (HV) and low voltage (LV) networks) if demand increases beyond the baseline against which allowances were set at the start of RIIO-ED2.

This document is aimed at DNOs and other stakeholders with a general interest in the LRE Volume Drivers. It covers the guidance and administration of the LRE Volume Drivers, including the metrics that delivery under the volume drivers will be assessed against, how the cap will be set, and the process that will be undertaken to review these parameters during the price control.

## Related Documents

- RIIO-ED2 Draft Determinations, Core Methodology Document, Chapter 3
- RIIO-ED2 Final Determinations, Core Methodology Document, Chapter 3
- Special Condition 3.9 (LRE Volume Drivers) of the Electricity Distribution Licence

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## Context

Ofgem is the Office of Gas and Electricity Markets which regulates the electricity and gas industries in Great Britain. Our principal duty is to protect the interests of existing and future gas and electricity consumers. Consumers' interests are taken as a whole, including their interests in the reduction of greenhouse gases and in the security of the supply, and in the fulfilment of relevant statutory objectives when we are carrying out our functions as the gas and electricity regulator of Great Britain.

We work in various ways to protect the interests of current and future consumers. One way we do this is by regulating the network companies through the RIIO price controls. We set price controls to specify the services and level of performance that the network operators must provide for users and consumers and to restrict the amount of money that the network companies can recover through network charges over the length of a price control period.

In [November/December] 2022 we published our RIIO-ED2 Final Determinations for the electricity Distribution Network Operators (DNOs). This set out the key elements of the price control from 1 April 2023 to 31 March 2028. This included the Secondary Reinforcement Volume Driver and the Low Voltage Services Volume Drivers for Load Related Expenditure (LRE) in RIIO-ED2. These newly introduced arrangements are given effect to in the Electricity Distribution Licences.

The purpose of this document is to outline the function of the LRE volume drivers and the requirements the DNOs need to satisfy to comply with the licence.

It is the responsibility of each DNO to understand the provisions of this Governance Document and how those provisions apply to it. This Governance Document comes into effect on 1 April 2023.

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## 1. Introduction

1.1. This Load Related Expenditure (LRE) Volume Drivers Governance Document ("the Governance Document") sets out further information to Special Condition 3.9 of the RIIO-ED2 licence in relation to the reporting requirements and methodologies for the Secondary Reinforcement Volume Driver (SRVD) and the Low Voltage Services Volume Driver (LVSVD).

1.2. This Governance Document is intended to help the licensees fulfil requirements to receive funding from the LRE Volume Drivers (the Volume Drivers are set out in Special Condition 3.9 of the Licence). The Governance Document provides further information on the accompanying monitoring and reporting framework and assists the licensees in reporting their use of the LRE volume drivers alongside the Regulatory Instructions and Guidance (RIGs) and Regulatory Report Packs (RRPs) processes.

1.3. The SRVD and the LVSVD will enable relevant LRE allowances to be adjusted during RIIO-ED2.

1.4. We have also established the LRE Re-opener, which does not fall within the scope of Special Condition 3.9. The LRE Re-opener will allow DNOs to bring forward requests for additional allowances for work on their primary (ie extra high voltage) networks as well as other categories of LRE expenditure which are not covered by the SRVD and LVSVD. Guidance on the LRE Re-opener is provided in Appendix [x] of the RIIO2 Reopener Guidance and Application Requirements.

### Compliance

1.5. DNOs are required by Special Condition 3.9 to comply with this document.

1.6. For the avoidance of doubt, this document is subordinate to the licence. This document does not change any definition or obligations contained within the licence and in the event of any ambiguity over the Governance Document, the licence will take precedence.

1.7. This document in no way relieves affected parties, including DNOs, from their responsibility to ensure ongoing compliance with legislation including competition, data protection, environment, and consumer protection laws.

### Review

1.8. The Authority may amend this Governance Document by direction in accordance with the common procedure laid out in Special Condition 1.3.

## 2. Secondary Reinforcement Volume Driver

### Overview

2.1. The Secondary Reinforcement Volume Driver (SVRD) is relevant to investment on the DNOs' secondary networks (ie HV and LV networks). DNOs have been provided with a baseline allowance for this investment, as set in the RIIO-ED2 Final Determinations.

2.2. We expect that the dominant driver of secondary network reinforcement for RIIO-ED2 will be the uptake of Low Carbon Technologies (LCTs), specifically Electric Vehicles (EVs) and Heat Pumps (HPs). The pace, location and local network impact of these technologies is challenging to predict. This creates uncertainty over the volumes of network interventions which will be needed to ensure that connections of LCTs can be supported without compromising network reliability. The SVRD is designed to manage this uncertainty.

2.3. The core parameters of the volume driver are provided in the box below.

**Table 1: Secondary Reinforcement Volume Driver overview**

UM Parameter	Position
Scope	The Secondary Reinforcement Volume driver funds work related to capacity constraints affecting substations and circuits on the secondary network (LV and HV).
Volume measure	<p>The mechanism is used to vary allowances based on set unit costs for the following volume measures:</p> <ul style="list-style-type: none"> <li>Substations: £/MVA gross additions for pole mounted transformers (PMTs) and ground mounted transformers (GMTs).</li> <li>Circuits: £/km additions with separate unit costs by voltage level.</li> </ul>
Adjustment mechanism	<p>DNOs received a baseline allowance for the whole of RIIO-ED2, set at the start of the price control. The volume driver will adjust allowances (up or down) as the sum of the volume metrics multiplied by the relevant unit rates as set out in Special Condition 3.9.</p> <p>Five metrics are included in the monitoring and reporting package for the SVRD, to help guard against sub-optimal investment.</p> <ul style="list-style-type: none"> <li>Metric 1: Transformer utilisation</li> <li>Metric 2: Transformer capacity released ratio</li> </ul>

	<ul style="list-style-type: none"> <li>• Metric 3a: Circuits length added ratio</li> <li>• Metric 3b: circuits transformer ratio</li> <li>• Metric 4: Load growth index</li> <li>• Metric 5: LCT forecast</li> </ul>
Totex Incentive Mechanism (TIM)	The TIM will be applied to any outperformance or underperformance against the unit rates provided by the volume driver.
Allowance cap	The total expenditure that can be accessed from the SRVD will be subject to a cap. The cap is set on an aggregate basis, limiting the total costs that are available from the volume driver. The cap is individual to each DNO and applies for the whole of RIIO-ED2.

## SRVD reporting and monitoring framework

2.4. DNOs are required to report their performance in relation to the SRVD in accordance with the RIIO-ED2 RIGs. This includes submission by the deadline stated in the RIGs and in the format prescribed by the RIIO-ED2 RRP.

2.5. The sections below include further detail on what is to be reported for each volume driver, including each metric within the reporting framework for the SRVD.

2.6. In line with the RRP's 'CV2 – Secondary Reinforcement' datasheet DNOs must submit both costs and volumes annually for the following conventional reinforcement asset types:

- PMT Transformer gross (capacity) additions (HV+LV, MVA)
- GMT Transformer gross (capacity) additions (HV+LV, MVA)
- OHL Circuit (length) additions (LV, km)
- OHL Circuit (length) additions (HV, km)
- Cable Circuit (length) additions (LV, km)
- Cable Circuit (length) additions (HV, km)

2.7. Figure 1 below sets out the high-level process that DNOs will follow in using the SRVD.

*Figure 1: SRVD monitoring process*

[Will insert screenshot of flowchart when finalised]

## SRVD monitoring indicators

2.8. DNOs are required to provide information which will be used to track DNOs' LRE investment against five SRVD metrics included in the RRP [sheet name TBC]. DNOs are required to submit this information and it will be monitored in each year of the price control. The metrics are designed to protect customers against unjustified costs arising from sub-optimal investment in the network that was not supported by robust information on network requirement. This is achieved by each metric identifying whether DNOs are exhibiting unexpected behaviour, for example increasing investment when LCT demand is less than expected, or reinforcing a high proportion of low utilised assets.

2.9. If any of the checks produce a red flag and the DNO has exceeded their baseline allowance, then the Authority will request and review costs, volumes, and additional information submitted by the DNOs as outlined in this chapter. This review could lead to claw-back of allowances, if the DNO has already exceeded their baseline allowance and if the review highlights sub-optimal expenditure. More detail of this process is highlighted in the 'Annual SRVD metric review process' section of this chapter.

### **Metric 1: Transformer utilisation**

2.10. The transformer utilisation metric is designed to control against sub-optimal reinforcement of transformers. The metric checks that works are occurring within 'high' utilisation bands or areas of projected high utilisation. The threshold for high utilisation is set as:

- For Pole Mounted Transformers (PMTs) this will be based on a forecast of the asset's utilisation for a year ahead, ie to the March 31<sup>st</sup> immediately after the RRP submission. This reflects the fact that PMTs can rapidly progress from 100% utilisation to a level that would be beyond safe operation.
- For Ground Mounted Transformers (GMTs) it will be based on utilisation as at the March 31<sup>st</sup> immediately prior to the RRP submission. This reflects the fact that GMTs typically progress from 100% utilisation to a level that would be beyond safe operation over a period longer than one year.

2.11. A tolerance of 10% of capacity additions in 'low' utilisation bands (ie below 100%) will be permitted under the metric, to account for situations where it is justified to invest in transformers with a utilisation below 100%.

2.12. On an annual basis, DNOs are required to report:



- PMT gross capacity additions (HV + LV combined, MVA) within the respective 20% **forecast** utilisation bands.<sup>1</sup>
- GMT gross capacity additions (HV + LV combined, MVA) within the respective 20% utilisation bands.

2.13. DNOs are also required to provide a method statement that ensures utilisation is measured consistently across DNOs. The method statement will be an independently validated audit of the methodology used to calculate utilisation and will include validation of:

- The source data used
- Modelling and calculations being based on the source data correctly
- Final outputs being correctly recorded
- Final outputs fulfilling any requirements required by the Authority.

2.14. The method statement will need to be independently validated before the start of the RIIO-ED2 price control and during year 3 of the RIIO-ED2 price control.

2.15. The figure below shows how the utilisation metric works in the RRP.

*Figure 2: Transformer utilisation metric in RRP*

[Placeholder for annotated screenshot of the model]

## **Metric 2: Transformer capacity released ratio**

2.16. The transformer capacity released ratio checks that transformer capacity additions are proportional to changes in LCT demand, by measuring the ratio of GMT and PMT gross capacity additions to the increase in peak load capacity caused by new LCT demand.<sup>2</sup> Each DNO is compared to an industry benchmark, as used in the disag model, which is fixed at the beginning of RIIO-ED2. A tolerance of 10% above the industry benchmark is permitted, with any deviation above that causing a red flag to be produced. The formula for the ratio is presented below:

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<sup>1</sup> The 20% bands are those outlined in the RRP: 0 – 20%, 20% – 40%, 40% – 60%, 60% – 80%, 80% – 100%, 100% – 120%, and >120%

<sup>2</sup> LCT demand peak load contribution are calculated for two technologies: [0.6 kW for EVs; and 0.8 kW for heat pumps.]

$$\frac{\sum_i \text{Additional LCT connected}_{t,i} \cdot \text{Peak load contribution}_i}{\text{Peak load capacity}}_{t,i}$$

$i = \text{LCT technology type}$

2.17. DNOs are required to report on an annual basis:

- HPs installed on the DNOs' network during the year, using the MCS database as a data source (#)
- EVs registered in the DNOs' region(s) during the year using the DVLA registration database as a data source (#)
- GMT & PMT gross capacity additions (HV + LV combined, MVA)

2.18. The figure below shows how the transformer capacity released metric works in the RRP.

*Figure 3: Transformer capacity released metric in the RRP*

[Placeholder for annotated screenshot of the model].

### **Metric 3a: Circuits length added ratio**

2.19. The circuits length added ratio checks that the addition of circuits (length) is proportional to changes in LCT demand, by measuring the ratio of overhead pole line (OHL) and cable length additions to the increase in peak load capacity caused by new LCT demand.<sup>3</sup> Each DNO is compared to an industry benchmark, as used in the disagg model, which is fixed at the beginning of RIIIO-ED2. A tolerance of 10% above the industry benchmark is permitted, with any deviation above that causing the check to produce a red flag. The formula for the ratio is presented below:

$$\frac{\text{Circuits length added (OHL + Cable)}_t}{\sum_i \text{Additional LCT connected}_{t,i} \cdot \text{Peak load contribution}_i}$$

$i = \text{LCT technology type}$

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<sup>3</sup> LCT demand peak load contribution are calculated for two technologies: [0.6 kW for EVs; and 0.8 kW for heat pumps.]

2.20. DNOs are required to report on an annual basis:

- Outturn heat pumps installed on the DNOs' network during the year, using the MCS database as a data source (#)
- Outturn EVs registered in the DNOs' region(s) during the year using the DVLA registration database as a data source (#)
- OHL & cable length additions (HV + LV combined, Km)

2.21. The figure below shows how the circuits length added metric works in the RRP.

*Figure 4: Circuits length added ratio in RRP*

[Placeholder for annotated screenshot of the model].

**Metric 3b: circuits transformer ratio (to note – included for if this approach progressed, in which case 3a is removed)**

2.22. The circuits transformer ratio compares outturn circuit reinforcement volumes against expected circuit reinforcement volumes. Expected volumes are based on the historic relationship between transformer and circuit reinforcement for each DNO. The historic relationship is calculated as the number of transformers reinforced per km of circuit reinforced. Therefore, the expected total length of circuit reinforcement each year is the number of transformers reinforced in a given year multiplied by the DNO's historic ratio. A tolerance of 10% above or below the expected total length is permitted, with any deviation outside of this causing the check to produce a red flag.

2.23. DNOs are required to report on an annual basis:

- GMT & PMT transformers reinforced (HV + LV combined, #)
- OHL Circuit (length) additions (LV, km)
- OHL Circuit (length) additions (HV, km)
- Cable Circuit (length) additions (LV, km)
- Cable Circuit (length) additions (HV, km)

2.24. The figure below shows how the circuits transformer ratio metric works in the RRP.

*Figure 4: Circuits transformer ratio metric in the RRP*

[Placeholder for annotated screenshot of the model].

**Metric 4: Load growth index**

2.25. The load growth index is a measure of annual load growth from a baseline derived in the first year of the price control using a representative sample of installed LV monitors[...]

2.26. DNOs are required to [xx].

2.27. The figure below shows how the load growth index metric works in the RRP.

*Figure 5: Load growth index in RRP*

[Placeholder for annotated screenshot of the model].

### **Metric 5: LCT forecast**

2.28. The LCT forecast metric compares ex-ante LCT volume forecasts with outturn volumes to determine how outturn has differed from expectations. Changes in LCT outturn vs forecasts are compared to changes in ex-ante asset reinforcement outturn volumes vs forecast reinforcement. If asset reinforcement is above / below forecast levels then the metric should demonstrate a link to LCT outturn that is above / below forecast levels (respectively). If a link is not established (i.e. the direction of change for asset reinforcement differs to the direction of change for LCT demand) then the check produces a red flag. A red flag can be produced for either circuit reinforcement, transformer reinforcement, or both.

2.29. DNOs are required to submit:

- Ex-ante forecast estimated number of LCTs installed (HPs and EVs);
- Outturn number of LCTs installed (HPs and EVs);
- Ex-ante BPDT forecast estimated volumes of gross capacity additions for transformers (MVA);
- Ex-ante BPDT forecast estimated volumes of gross length additions for circuits (km)
- Outturn volumes of gross capacity additions for transformers (MVA);
- Outturn volumes of gross length additions for circuits (km);

2.30. The figure below shows how the LCT forecast metric works in the RRP:

*Figure 6: LCT forecast in RRP*

[Placeholder for annotated screenshot of the model].

## **Annual SRVD metric review process**

2.31. DNOs will report on the five metrics as part of the annual RRP process. Ofgem will then review the information between July and November. The Authority will check the submitted data for the monitoring metrics along with any supporting commentary provided by the DNOs.

2.32. If all checks produce green flags then costs and volumes will be rewarded (if the cap has not been reached, see below) with the TIM applied to over / under spend against ex-ante unit costs.

2.33. If any checks produce red flags, the supporting commentary doesn't justify why, and DNOs have exceeded the baseline LRE allowances set at the start of RIIO-ED2, then they will be required to submit additional information.

2.34. Listed below are examples of the type of information that we would expect to review if one or more of the metrics produces a red flag, though the Authority may request such additional information as it considers necessary in the circumstances. The specific additional information requested will depend on which of the five metrics have produced a red flag. DNOs may also provide additional information for the Authority's consideration.

- Forecast and outturn LCT volume uptake;
- Engineering justification papers (EJPs) for any interventions on low (ie below 100%) utilisation assets;
- Circuits (km and MVA) reinforced (broken down by new circuits and replacement of old circuits);
- Local engagement that has informed the DNO investments subject to the review;
- Data on HV and LV network existing and forecast constraints in the areas where reinforcement has been undertaken, both before and after the interventions; and
- Age and condition of assets replaced.

## **SRVD Cap**

2.35. The total expenditure that can be accessed from the SRVD will be subject to a DNO specific cap, set out in Special Condition 3.9. The cap is set on an aggregate basis, limiting the total costs that are available from the volume driver, ie individual caps will not be set per asset type. The cap applies for the whole of RIIO-ED2, allowing an uneven profile of spend across years if necessary.

2.36. The cap has been calibrated using an independent high-case forecast scenario of LCT uptake for each DNO.<sup>4</sup> Taking a scenario from an independent source ensures an even treatment across DNOs. Using a scenario with ambitious forecasts for LCT take-up reduces the risk of blocking net zero whilst mitigated the risk that DNOs are provided with too much funding that will increase costs for customers.

2.37. If a DNO reaches the cap, it will no longer be able to incur allowances against the SRVD. As set out in Chapter 4, the level of the cap will be reviewed in Year 3 of RIIO-ED2, with provision to review the cap earlier should it be necessary.

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<sup>4</sup> This is based on the EV and heat pump forecasts contained in the [xxxx xxxx] scenario.

### 3. Low Voltage Services Volume Driver

#### Overview

3.1. The Low Voltage Services Volume Driver (LVSVD) is designed to fund proactive and reactive load related LV service reinforcement, particularly 'unlooping' of LV service cables.

3.2. Historically, there are hundreds of thousands of properties (with the scale varying by DNO) where low cost, shared services have been provided. Put simply, shared services, split the LV service cable running into a property into two or more parts, which reduces the capacity available to consumers. This reduced capacity can present a barrier to customers installing an LCT.

3.3. The core parameters of the volume driver are provided in the box below.

*Table 2: Low Voltage Services Volume overview*

UM Parameter	Position
Scope	<p>A volume driver to fund proactive and reactive load related LV service reinforcement. This covers:</p> <ul style="list-style-type: none"> <li>• Overhead Pole Line – LV Service (OHL)</li> <li>• Cable – LV Service (UG)</li> <li>• Switchgear – Cut Out (metered)</li> <li>• Fuse upgrades</li> </ul>
Volume measure	The volume measure is on a £/assets reinforced basis with separate unit costs for each activity, albeit the same unit cost will apply whether the works are proactively or reactively driven.
Adjustment mechanism	DNOs received a baseline allowance for the whole of RIIO-ED2, set at the start of the price control. The volume driver will adjust allowances (up or down) as the sum of the volume metrics multiplied by the relevant unit rates as set out in Special Condition 3.9.
Totex Incentive Mechanism (TIM)	The TIM will be applied to any outperformance or underperformance against the unit rates provided by the volume driver.
Allowance cap	The total expenditure that can be accessed from the LVSVD will be subject to a cap. The cap is set on an aggregate basis, limiting the total costs that are available from the volume driver. The cap is individual to each DNO and applies for the whole of RIIO-ED2.

## **LVSVD reporting and monitoring framework**

3.4. The DNOs are required to report their individual performance in relation to the LVSVD in accordance with the RIIO-ED2 Regulatory Instructions and Guidance (RIGs). This includes submission by the stated deadline and in the format prescribed by the RIIO-ED2 Regulatory Reporting Pack.

3.5. DNOs are required to submit both costs and volumes annually in the RRP 'CV2 – Secondary Reinforcement' datasheet for the following proactive and reactive service reinforcement asset additions:

- OHL LV service reinforcement asset additions (LV Service (OHL), LV, #)
- Cable LV Service reinforcement asset additions (LV Service (UG), LV, #)
- Switchgear reinforcement asset additions (Cut out (metered), LV, #)
- [Fuse upgrades]

## **LVSVD Cap**

3.6. The total expenditure that can be accessed from the LVSVD will be subject to a cap, set out in Special Condition 3.9. The cap is set on an aggregate basis limiting the total costs that are available from the volume driver, ie individual caps will not be set per asset type. The cap applies for the whole of RIIO-ED2, which allows an uneven profile of spend across years, if necessary.

3.7. The cap has been calibrated using an independent high-case forecast scenario of LCT uptake.<sup>5</sup> Taking a scenario from an independent source will provide an even treatment across DNOs. Using a scenario with some of the most ambitious forecasts for LCT take-up reduces the risk of blocking net zero whilst mitigated the risk that DNOs are provided with too much funding that will increase costs for customers.

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<sup>5</sup> This is based on the EV and heat pump forecasts contained in the [xxxx xxxx] scenario.



3.8. If a DNO reaches the cap, it will no longer be able to incur allowances against the LVSVD. As set out in Chapter 4, the level of the cap will be reviewed in Year 3 of RIIO-ED2, with provision to review the cap earlier should it be necessary.

## 4. Review of LRE volume drivers

### Scope

4.1. There will be a review of the LRE volume drivers during Year 3 of RIIO-ED2. The review is designed to ensure that the volume drivers are functioning as intended, ie that DNOs are able to invest in the network to meet net zero without consumers paying for work that isn't necessary.

4.2. The Authority may, if it considers it necessary to do so, initiate the LRE volume drivers review earlier than Year 3 of RIIO-ED2, at a time agreed ad-hoc with the DNOs via Energy Networks Association.

4.3. The scope of this review will include, but may not be limited to:

- The efficacy of the unit costs set out in the volume drivers;
- A review of whether the volume driver caps are set at the right level, including through consideration of revised forecasts for LCT uptake, outturn LCT uptake figures and additional commentary provided by DNOs. For the cap to be increased, DNOs must prove that investment was justified and that demand is increasing;
- Re-validation of the method statements required under SRVD metric 1;
- Consideration of whether the SRVD metrics are functioning effectively, ie whether they are identifying unjustified investment and not incorrectly identifying justified investment; and
- An assessment of progress against the expectations of granular utilisation data to be available for RIIO-ED3.

### Process

4.4. The review of the LRE volume drivers will begin in January 2026, following conclusion of the RIIO-ED2 Year 2 RIGs and RRP processes. the Authority will aim to conclude its review by June 2026, ahead of the RIIO-ED2 Year 3 RIGs and RRP processes.

4.5. By Monday 12<sup>th</sup> January 2026, DNOs should provide the Authority with any information that it considers relevant to inform the scope of the review described at paragraph 4.3 above. As part of this, DNOs must provide the Authority with updated versions of the method statements required under SRVD metric 1.

4.6. The Authority will then begin its review, which will include a supplementary question process with the DNOs, the detailed arrangements of which will be agreed between the Authority and the DNOs in December 2025.

4.7. If, as a result of this review, the Authority intends to update any of the key parameters of the LRE volume drivers contained within either Special Condition 3.9, the Governance Document, or the RIGs and RRP, it will do so in line with the relevant process set out in Special Condition 3.9 or Special Licence Condition 46.