
RIIO-ED2 Distribution System Operation Incentive metrics decision

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This document describes our decision for the three outturn performance metrics proposed as part of the Distribution System Operation (DSO) incentive in our RIIO-ED2 Final Determinations.

Despite recognising the value of the metrics, we do not think it is feasible to set performance targets for RIIO-ED2 due to concerns with data quality, a lack of historical data and methodological issues.

As a result, we have decided to implement our alternative approach where Distribution Network Operators (DNOs) will be required to report on performance in these areas by gathering data to improve future target setting. Furthermore, we have decided to reallocate the weighting of the incentive originally intended for the outturn performance metrics from Year 2 of RIIO-ED2 to the DSO performance panel assessment and stakeholder satisfaction survey equally.

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1. Introduction

Section summary

This section sets out an overview of our decisions on the three outturn performance metrics considered as part of the RIIO-ED2 DSO incentive. Our high level decisions are described below:

- 1) We have decided to maintain our consultation position and not switch on the performance metrics during RIIO-ED2.
- 2) We have decided to maintain our consultation position and continue with the metrics as a reporting requirement during RIIO-ED2.
- 3) We have decided to change our consultation position and reallocate the 20% weighting, originally designed for the outturn performance metrics, equally to the DSO performance panel assessment and stakeholder satisfaction survey.

Overview of our decision

- 1.1 This document sets out our decision on the three outturn performance metrics that were proposed as part of the Distribution System Operation (DSO) incentive in our RIIO-ED2 Final Determinations.¹
- 1.2 As described in our RIIO-ED2 Final Determinations, the DSO incentive is a new output delivery incentive mechanism that has been introduced as part of RIIO-ED2. The DSO incentive was to be made up of three evaluation criteria – a stakeholder survey, a performance panel assessment, and three outturn performance metrics. We decided not to implement targets for the three outturn performance metrics in Year 1 of RIIO-ED2. Instead, we stated that we would require Distribution Network Operators (DNOs) to gather performance data on the metrics with the aim to set targets from Year 2 onwards.
- 1.3 Following six months of thorough and in depth work with the DNOs our consultation position was to not switch on the outturn performance metrics during the RIIO-ED2 price control period. While we acknowledged the value of the metrics, various concerns arose during the group discussions and following our analysis of detailed information collected from the DNOs (through Request for Information (RFI) responses). These concerns included: data quality, insufficient historical data, methodological challenges, and the risk of unintended

¹ [RIIO-ED2 Final Determinations | Ofgem](#)

consequences. This led us to a conclusion that setting appropriate metric targets was not feasible at this point in time.

- 1.4 We have reviewed all DSO stakeholder views provided to us as part of our consultation document.² We acknowledge and share the disappointment in not activating the outturn performance metrics as planned at Final Determinations. However, we maintain our consultation view that due to the aforementioned issues it is not appropriate to switch the outturn performance metrics on during RIIO-ED2.
- 1.5 As a result, we have decided to maintain our proposed approach to continue with the metrics as a reporting requirement (subject to resolving the outstanding methodological issues which prevented this part of the incentive being switched on). We maintain our view that this is the most appropriate solution that will allow us to build on the evidence base to enable financially incentivised performance in these areas in RIIO-ED3.
- 1.6 Finally, we have decided to reallocate the 20% weighting of the incentive, (originally designed for the outturn performance metrics from Year 2 of RIIO-ED2) equally to the DSO performance panel assessment and stakeholder satisfaction survey. This means the value of the remaining components of the incentive will be split equally from Year 2 of RIIO-ED2. This will give DNOs the opportunity to include the data in the evaluation of their performance as a DSO, while also capturing the views of a wide range of stakeholders as part of the survey. In addition, this preserves the intended value of the incentive for Years 2-5 of RIIO-ED2, as per our RIIO-ED2 Final Determinations (ie, increasing from 0.32/-0.16% in Year 1 to +0.4/-0.2% from Year 2 of RIIO-ED2).

Context and related publications

- 1.7 The key publications related to this consultation are:
- RIIO-ED2 Final Determinations – Core Methodology Document, Chapter 4, Regulating Distribution System Operation functions: [RIIO-ED2 Final Determinations | Ofgem](#)
 - Electricity Distribution Licence – Special Condition 4.8 (Distribution System Operation output delivery incentive): [Decision on the proposed modifications to the RIIO-2 Electricity Distribution licences | Ofgem](#)

² [RIIO-ED2 DSO Incentive - Outturn Performance Metrics | Ofgem](#)

Decision – RIIO-ED2 Distribution System Operation Incentive metrics decision

- RIIO-ED2 DSO Incentive Governance Document: [Decision on the proposed modifications to the RIIO-2 Electricity Distribution licences | Ofgem](#) (located in “Subsidiary Documents – 17 February 2023 publication of Associated Documents and relevant issue logs.zip”)

Our decision-making process

- 1.8 Table 1 outlines the key stages of our decision-making process.
- 1.9 Our consultation informing the decision-making process and the non-confidential responses received can be found on our website via the following link - RIIO-ED2 DSO Incentive – Outturn Performance Metrics Consultation: [RIIO-ED2 DSO Incentive - Outturn Performance Metrics | Ofgem](#)

Decision-making stages

Table 1 - Decision-making stages

Date	Stage description
16/02/2024	Stage 1: Consultation opens
15/03/2024	Stage 2: Consultation closes (awaiting decision), deadline for responses
26/04/2024	Stage 3: Responses reviewed and published
26/04/2024	Stage 4: Consultation decision/policy statement
End of May 2024	Stage 5: Statutory consultation on proposed modifications to the Electricity Distribution licence

General feedback

We believe that consultation is at the heart of good policy development. We are keen to receive your comments about this report. We would also like to get your answers to these questions:

1. Do you have any comments about the overall quality of this document?
2. Do you have any comments about its tone and content?
3. Was it easy to read and understand? Or could it have been better written?
4. Are its conclusions balanced?
5. Did it make reasoned recommendations?
6. Any further comments?

Please send any general feedback comments to stakeholders@ofgem.gov.uk.

2. Background

Section summary

This section covers the background to the DSO outturn performance incentive and describes the development of the DSO outturn performance metrics.

Overview

- 2.1 In line with our objective for DNOs to support a smarter, more flexible energy system, we implemented a new financial DSO incentive as part of our RIIO-ED2 Final Determinations. The DSO incentive drives licensees to more efficiently develop and use their network, taking into account flexible and smart alternatives to network reinforcement and ultimately reduce customer bills, based on DNOs' delivery of their DSO activities.
- 2.2 A hybrid approach was developed for the DSO incentive to balance mechanistic and evaluative approaches. The three criteria consisted of a stakeholder survey, a performance panel assessment, and three outturn performance metrics.
- 2.3 Our RIIO-ED2 Final Determinations confirmed that we would seek to implement the following three outturn performance metrics:
- **Flexibility reinforcement deferral (FDt)**, to drive DNOs to use flexibility to address network constraints when it is the most economic solution.
 - **Secondary network visibility (NVt)³**, to promote visibility and accuracy of utilisation of Pole Mounted Transformers (PMTs) and Ground Mounted Transformers (GMTs).
 - **Curtailement efficiency (CEt)**, to incentivise DNOs to limit curtailement of users on Curtailement Connections resulting from actions taken to restrict the conditions of a connection (import and/or export capacity) in response to a constraint on the distribution system.
- 2.4 We decided not to implement targets for the outturn performance metrics in Year 1 of the price control, such that performance against them is not subject to any financial incentive in the first year. Given the novelty and complexity of this domain, we said that we would work with the DNOs to gather performance data

³ This metric was originally described as Secondary Network Visibility (NVt) in our RIIO-ED2 Final Determinations but subsequently changed to better reflect the intent of the metric.

on the metrics before applying financial rewards or penalties for performance in Year 2 onwards (subject to targets being set).

- 2.5 Following six months of extensive discussion and analysis including several working groups and two detailed Requests for Information (RFI), we published our informal consultation proposing not to activate the outturn performance metrics during the RIIO-ED2 price control. Despite recognising the value in establishing a robust set of performance metrics, we did not have sufficient confidence in setting realistic targets against these three metrics due to data quality concerns and unresolved methodological issues. Further, we still had concerns about the clarity of the outputs delivered by Secondary Forecasting (SFt)⁴ and CEt due to the ongoing concerns with the SFt methodology and the overarching difficulty in precisely defining the criteria for what constitutes a “good” outcome for CEt. Therefore, our consultation position was to not switch on the metrics during RIIO-ED2.
- 2.6 Instead, we stated that our proposed approach was for DNOs to report on performance in these areas by gathering data to enable the design of a similar incentive in future, including increased confidence in being able to set stretched targets. Furthermore, we recommend that the 20% weighting of the incentive, (originally designed for the outturn performance metrics) should form part of the DSO performance panel assessment. This would result in a 60/40 split between the performance panel and stakeholder survey. This would allow the DNOs the opportunity to include the relevant data related to the DSO incentive in the evaluation of their performance as a DSO.

⁴ NVt was changed to Secondary Forecasting (SFt) to better reflect the intent of the metric.

3. Decision on DSO outturn performance metrics

Section summary

This section encompasses the feedback received during the consultation and outlines our decision for each performance metric, including our future approach.

Introduction

3.1 The DSO incentive performance metrics consultation closed on 15 March 2024. We received ten responses from six DNOs and four industry stakeholders. We have reviewed all responses provided to us as part of our published consultation. This chapter offers a summary of these views and our corresponding decision for each metric.

Flexibility Reinforcement Deferral (FDt)

Background

- 3.2 As described in our informal consultation, there were several challenges that impacted the feasibility of progressing the FDt metric. Persistent inconsistencies were observed within certain aspects of the methodology and our analysis revealed a number of anomalies which raised concerns about the accuracy of the data provided and the integrity of the overall data set.
- 3.3 From the second Request for Information (RFI2) responses submitted, four licensees lacked historical flexibility services data and three showed an output significantly greater than 100%. Although some variations in the FDt profiles were expected given the geographical disparities in the availability of flexibility services and known licensee variations in existing DSO activity, we were concerned by the significant disparities in the data presented to us.
- 3.4 Overall, despite significant working group discussions, clear discrepancies in the methodologies and a lack of historical flexibility services data did not provide the necessary confidence that realistic and meaningful targets could be set.

Q1. Do you agree with our recommendation not to switch on the FDt outturn performance metric during RIIO-ED2?

Consultation responses to question 1

- 3.5 We received ten responses to this question. All respondents agreed that, given the challenges presented in the consultation, it is not appropriate to implement

- the FDt metric in Year 2 of RIIO-ED2 as per the original intent described in our RIIO-ED2 Final Determinations.
- 3.6 The consensus among eight respondents was that, whilst disappointing that the FDt outturn performance metric could not be developed sufficiently, the activation of the metric during RIIO-ED2 should be deferred until RIIO-ED3 to allow for resolution of remaining consistency issues in the methodology and the accumulation of historical flexibility data.
- 3.7 Whilst agreeing with the consultation position, UKPN advocated for its implementation in Year 3 of RIIO-ED2 within the price control period. In addition, an industry stakeholder encouraged the outturn performance metrics to be switched on during RIIO-ED2 if the target setting issues could be resolved. We have carefully considered the responses and decided that it is not in consumers interest to switch on the metric(s) during RIIO-ED2. Further time would need to be spent developing targets and making the necessary licence modifications (as per the prescribed timeline for metric implementation within the RIIO-ED2 framework). Our view is that such a proposal would mean that any metrics would only be in place during the final year of RIIO-ED2. This would be too late for the results to inform the design of RIIO-ED3. Our proposed approach also provides certainty to DNOs and stakeholders on the design of the incentive for the remainder of RIIO-ED2.
- 3.8 There was disagreement amongst DNO respondents regarding the progress of the FDt metric development. ENWL viewed FDt as a metric that requires less fundamental work to function as robust Regularly Reported Evidence (RRE). UKPN believed the right principles are in place but recommended more work is needed on the reporting template and associated guidance. SPEN set out further recommendations around target setting and calibration and highlighted terms within the methodologies that are at risk of inconsistent interpretation amongst DNOs. Conversely, SSEN considered there are fundamental issues with the metric design that question the value it can provide in its current form. Their view was that it would be inappropriate for networks to report against it in its current form. Furthermore, NPg had concerns that performance is sensitive and volatile to externalities such as flexibility market growth, tender success and location of flexible assets and that it would be difficult to set targets that adequately addressed individual licensee circumstances, whilst effectively driving performance.
- 3.9 We agree with UKPN that the right principles are in place for the FDt metric, however we acknowledge that a material amount of additional work is needed to

refine the metric to a level where there is a clear robust methodology that can be consistently reported upon and drive incentive allowances. We acknowledge SPEN, SSEN and NPG's concerns and think these should be addressed as part of any future work that will take place.

Our decision

- 3.10 We have decided to not switch on the Fd_t metric during RIIO-ED2 for the reasons set out in our consultation. There is general agreement amongst the consultation respondents regarding our proposal, with no new evidence presented indicating that it would be in consumers' interest to switch on the metric at this time.

Secondary Forecasting (Sf_t)

Background

- 3.11 As outlined in our consultation, concerns were raised by some DNOs that their ability to forecast utilisation on the secondary network at a granular level was affected by factors outside of their control. Therefore, an updated Secondary Forecasting (Sf_t) methodology was established with the working group to reduce the effects of the variations to ensure the metric was less sensitive to factors outside of the DNOs' control.
- 3.12 After reviewing DNOs' RF12 data submissions, we identified several issues with the profiles. All licensees had a starting Sf_t position above 95%, with several profiles rising to over 98%. Although the very high figures could be interpreted as the effectiveness of the licensee's forecasting capabilities, we think that the observed figures were tied to the methodology used. Setting a common target based on the average performance would mean that 11 licensees would start ahead of the target, potentially resulting in a reward for their current performance, rather than exceeding it.
- 3.13 The data submitted raised doubts over the effectiveness of the metric in its present form and for its intended purpose. Additionally, we were concerned with the possibility of licensees earning rewards for minimal effort rather than genuine excellent performance. This prompted further scrutiny regarding the potential for improvement given the already elevated starting position.
- 3.14 Even though this metric had evolved to manage the concerns with earlier versions, we considered it was not appropriate to implement as an incentive in its current form.

Q2. Do you agree with our recommendation not to switch on the Sft outturn performance metric during RIIO-ED2?

Consultation responses to question 2

- 3.15 We received ten responses to this question. All respondents agreed that, given the challenges presented in the DSO consultation, it is not appropriate to implement the Sft metric in Year 2 of RIIO-ED2 as per the original intent described in our RIIO-ED2 Final Determinations. Although most respondents agreed with not switching on Fdt during RIIO-ED2, there was some disagreement from two respondents (UKPN and an industry stakeholder) who were keen for the outturn performance metrics to be switched on during RIIO-ED2 if the target setting issues could be resolved.
- 3.16 The overwhelming agreement among the DNO respondents was that the Sft metric is unsuitable and does not adequately serve its intended purpose. Therefore, implementing the Sft metric should be postponed, allowing for additional work and effort to bring it to a standard where it can effectively serve as a reporting requirement for RIIO-ED2 and support an incentive for RIIO-ED3.
- 3.17 There was consensus amongst DNO respondents regarding the progress of the Sft metric development. ENWL and SSEN considered that the Sft metric needs significant work before it is fit for purpose, with SSEN highlighting it is still not entirely clear what 'good' looks like for this metric. SPEN had significant concerns with this metric and believe changes to the methodology are required to avoid unintended consequences. UKPN described the Sft metric as inappropriate and oversimplistic and are keen to expand on their alternative version of the metric that was discussed as part of the working groups. NPg did not believe the developed Sft metric is aligned with the original primary output and was concerned that this may lead to an incentive that may drive perverse behaviours.
- 3.18 One industry stakeholder said that Ofgem should drive progress on secondary network visibility using minimum standards on the installation of monitoring equipment on LV assets, and should consider using a target-based approach implemented through licence conditions, similar to the roll out of smart meters mandated via suppliers.
- 3.19 We agree that the Sft metric requires significant work to get it to a level where there is a robust methodology that can be consistently reported upon. We acknowledge all DNOs' concerns and think these should be addressed as part of any future work that will take place, including UKPN's alternative version of the metric. We acknowledge therefore that, in its current form, this metric does not

drive behaviours in line with customer interest. We are not proposing minimum standards on the installation of monitoring equipment on LV assets at this time. We will monitor progress through Regulatory Reporting Pack (RRPs) and may consider minimum standards in the future if we think there is a sufficient case to do so.

Our decision

- 3.20 We have decided to not switch on the Sft metric during RIIO-ED2 for the reasons set out in our consultation. The consensus among the DSO respondents agreed with this; the Sft outturn performance metric is deemed unsuitable in its current form and fails to fulfil its intended purpose. No new evidence presented indicates that it would be in consumers' interest to switch on the metric at this time.

Curtailed Efficiency (CEt)

Background

- 3.21 As per the consultation document, our major concern regarding the Curtailed Efficiency outturn performance metric (CEt) is a lack of data available to inform target setting. Only seven out of 14 licensees were able to provide a historic baseline dataset. Of those seven licensees, five currently have a small amount of Curtailed Connections/MW capacity in scope. These data limitations reduce insight and limit our ability to set robust targets, risking the potential value of the metric.
- 3.22 After RFI1, the DNOs raised doubts about their ability to accurately forecast Curtailed Connection capacity across RIIO-ED2. This reduced our confidence in the data we were able to collect in RFI1 and resulted in us changing our approach for RFI2, asking for a reduced amount of forecast data in combination with historic data. Furthermore, DNOs provided evidence demonstrating that as curtable capacity increases (as all DNOs predicted would happen over RIIO-ED2 to varying degrees) so will the need to curtail. This further challenged target setting, with the risk that poorly reasoned targets could unintentionally reward DNOs for limiting Curtailed Connection growth to more easily achieving better efficiency scores. A 'Target Adjuster' mechanism was developed in attempt to tackle this issue but was also limited by a lack of data.
- 3.23 Overall, historic and forecasting data limitations increased the challenge of determining what "good" performance looked like for CEt and reduced the potential value of implementation in RIIO-ED2.

Q3. Do you agree with our recommendation not to switch on the CEt outturn performance metric during RIIO-ED2?

Consultation responses to question 3

- 3.24 All respondents agreed that, given the issues presented in the consultation, the CEt metric should not be switched on in Year 2 of RIIO-ED2 as originally intended. Furthermore, all respondents except UKPN and one industry stakeholder agreed that CEt should not be switched on during RIIO-ED2 at all, with the need to work through remaining methodological consistency issues and collect more data to identify what good or bad performance under this metric would be. As with the other metrics, UKPN and an industry stakeholder proposed to delay switching on CEt, yet still aim for implementation in RIIO-ED2 if possible. This option was considered in our consultation position and is addressed in paragraph 3.7; it would not be realistic to implement the metrics before Year 5 of the price control and there is value in having certainty for the remainder of RIIO-ED2.
- 3.25 There was disagreement amongst DNO respondents regarding the progress of CEt development. UKPN suggested CEt is the closest of all metrics to implementation. However, ENWL stated CEt will need significant work before it is fit for purpose, while NPg suggested it requires a more fundamental reconsideration, arguing that the metric incentivises behaviours which are not aligned with Ofgem’s Access and Forward-Looking Charges Significant Code Review (“Access SCR”) decision⁵. NPg further stated the incentive will require funding for data collection and it has difficulty in determining what “good” performance looks like. Although we agree that there is inherent challenge in determining what exactly CEt targets should be (worsened by current data issues), we believe that the core objective of the metric – to limit Curtailment of users on Curtailable Connections in response to constraint on the Distribution System – is important and desirable.
- 3.26 In all stakeholder consultation responses, concern regarding the experiences of non-firm connection customers was referenced in response to this question, with disappointment regarding the loss of the benefits relating to curtailment levels and transparency that CEt might be able to provide. One stakeholder respondent stated that they believe alternative options to the metrics would be less effective at tackling the above issues. Two respondents suggested alternative approaches to the recommendation in our consultation (Question 5) in order to better

⁵ [Access SCR - Final Decision \(ofgem.gov.uk\)](https://www.ofgem.gov.uk)

replicate the aims of this metric. We acknowledge the importance of non-firm connection customer experiences and agree that any alternative approach must consider them. We discuss how these issues are considered in our decision-making behind the alternative approach later in this chapter.

Our decision

3.27 We have decided not to switch on the CEt metric during RIIO-ED2 for the reasons set out in our consultation. There is general agreement amongst the consultation respondents regarding the decision-making, with no new evidence presented indicating that it would be in consumers' interest to switch on the metric earlier.

Alternative approach

Background

3.28 As per our consultation position, our alternative proposal is to work with DNOs to develop robust reporting requirements from Year 2 of RIIO-ED2 that allow us to build the evidence base to enable financially incentivised performance in these areas in RIIO-ED3.

3.29 In addition, our consultation position stated our preferred approach was to reassign the full 20% weighting of the outturn performance metrics' allowance to the performance panel. We were also minded to allow DNOs who reported robust data with clear methodological approaches to use this data in the DSO Performance Panel assessment.

3.30 We stated in our consultation document that we would look to adapt the evaluation criteria in RIIO-ED2 Year 2 to include more specific references to aspects of the metrics not already included in the evaluation criteria. We also advised there may be a need for changes to the format of the panel (ie, extending the time given to each assessment).

Q4. Do you agree with our alternative approach to continue with the metrics as a reporting requirement?

Consultation responses to question 4

3.31 Eight responses supported our approach to continue with the metrics as a reporting requirement for RIIO-ED2. Of these, five DNOs believed that more work or further development is necessary to reach that stage.

3.32 ENWL agreed with our alternative proposal for Ofgem to work with DNOs to develop robust reporting requirements, however, and as per SSEN's feedback,

they believed all three metrics need different approaches due to their varying stages of maturity. NGED supported further development of the metrics, in their RRE form, to ensure they deliver a clear performance benchmark that can be used in RIIO-ED3. SPEN supported Ofgem and DNOs working together to agree the approach to target setting and resolve outstanding methodological issues. UKPN were very supportive of Ofgem continuing with the metrics as a reporting requirement, with a view to switching on the financial incentive aspect as soon as is practically possible. In addition, SSEN recommended that Ofgem should use the metric reporting part of the incentive to allow real-life data to be assessed and aid the correct design of the incentive measures.

- 3.33 Furthermore, three industry stakeholders agreed that if the performance metrics are not going to be introduced in RIIO-ED2, then these should continue to be a reporting requirement to achieve what was originally set out in Final Determinations and to set metrics for RIIO-ED3. One industry stakeholder stated that Ofgem should take this opportunity to strengthen minimum standards on data across the breadth of DSO activities, with a focus on building the evidence base needed to set ambitious performance incentives on DSO for RIIO-ED3.
- 3.34 We agree with the five DNOs that further effort is needed to implement metrics as a reporting standard. We may indeed need to go further and introduce additional RREs that supplement those already included in the DSO incentive reporting. Each metric is at a different stage of development and so we acknowledge the necessity of employing different approaches to address their current deficiencies. We acknowledge SSEN's comment on allowing real-life data to be assessed and think this should be addressed as part of any future work that will take place.
- 3.35 NPg disagreed with reporting on the metrics during RIIO-ED2 stating that in the absence of meaningful and objective metric assessments, Ofgem should turn off the whole incentive mechanism and use public-facing reports to hold DNOs to account against a reputational incentive. We disagree with this approach. Disabling the entire incentive poses a significant risk of not realising the substantial customer benefits that DSO can unlock during RIIO-ED2. By turning off the incentive altogether, we would potentially overlook valuable opportunities to achieve key DSO objectives outlined for RIIO-ED2. Therefore, while acknowledging the concerns associated with the current set up, the potential benefits of retaining the incentive outweigh the risks of discontinuing it entirely.

Our decision

- 3.36 Following consideration of the consultation responses, and for the reasons set out in the consultation, we have decided to continue with the metrics as a reporting requirement. We maintain our view that this is the most appropriate outcome that will allow us to build the evidence base to enable a financially incentivised performance in these areas in RIIO-ED3.
- 3.37 We expect all DNOs to work collaboratively to develop robust reporting requirements from Year 3 (2024/25) of RIIO-ED2. Before reporting commences, further work is required from all DNOs to develop the metrics to a level where they can effectively function as a reporting requirement, that generates meaningful data in RIIO-ED2. This includes resolving outstanding methodological issues and expanding the guidance around the metrics to ensure that each DNO has a common interpretation of each methodology.
- 3.38 As part of this process, we anticipate there will be a consultation on updates to the RIIO-ED2 Regulatory Instructions and Guidance (RIGs) ahead of the 2025/26 regulatory year. This will therefore provide an opportunity to finalise the metric reporting templates and their guidance so that consistent metric data can be captured in the remainder of RIIO-ED2.

Q5. Do you agree with our alternative approach to reassign the 20% value of the incentive to the performance panel assessment?

Consultation responses to question 5

- 3.39 We received ten responses to Question 5. There were split views on re-allocating the 20% weighting of the outturn performance metric incentive to the performance panel metric.
- 3.40 Four responses (ie, NGED, SSEN, UKPN and one industry stakeholder) agreed with the 20% weighting being moved to the performance panel. NGED supported further development work on the metrics, in their RRE form, to ensure they provide the performance panel with the clarity they need to make an assessment. SSEN also agreed that the performance panel is well equipped to assess company performance and recommended the panel is broadened to include the respective 'purposes' of the three metrics. UKPN agreed that the performance panel is the best alternative. An industry stakeholder agreed that the additional 20% weighting should be given to the performance panel but stated that a requirement to measure the performance of licensees against the metrics should be required. They did not think there should be additional weighting given the

performance panel without specific details in the evaluation criteria being put in place against the metrics.

- 3.41 In contrast, four responses (ie, ENWL, SPEN and two industry stakeholders) disagreed with our approach and stated that the 20% weighting should be split between the performance panel and stakeholder satisfaction survey. ENWL were concerned that panels can be prone to risk resulting in poor and unintended consequences for consumers. As the weighting is new and untested, they consider an equal weighting between the two remaining components of the incentive would make a balanced outcome. SPEN were concerned that the metrics were in place to demonstrate tangible benefit delivery to stakeholders and believed it is appropriate for the assessment of the incentive to place more views on a wide range of stakeholders with direct experience as users of DSO services. They therefore recommended that the 20% weighting increment should be either fully, or in part, reassigned to the stakeholder satisfaction survey.
- 3.42 In addition, SPEN did not support the panel considering the reported metric performance in their assessment. We disagree with this position. Given the relevance of the reported metric data to the panel assessment criteria, we believe if the issues with the metrics can be resolved so as to enable standardised reporting, the three metrics should be treated in the same way RRE is by the panel – and so allowing DNOs to make reference to the data in their panel submissions.
- 3.43 One industry stakeholder also recommended the 20% weighting of the outturn performance metrics incentive be split equally between the performance panel and stakeholder survey so that stakeholders impacted by connections curtailment can be captured within the stakeholder survey as a proxy for the curtailment efficiency metric that is now not proceeding. A second industry stakeholder reiterated this point, stating that in the absence of quantitative metrics, feedback from customers should be a priority for measurement of performance, specifically for Curtailable Connections. The stakeholder therefore suggested the 20% weighting should be split equally between the performance panel and the stakeholder survey. We agree that splitting the weighting equally and assigning 10% to the stakeholder survey will allow us to gain a better understanding of the current state of connections services, identify areas for improvement, and make more informed decisions.
- 3.44 NPg stated that without a clear objective basis for the incentive the whole mechanism should be removed. NPg do not support the subjective elements of the incentive, such as the performance panel, and had concerns that it will distort

activity towards more visible DSO outcomes and away from other approaches that deliver bigger consumer benefits. They also have concerns that the best submission will be rewarded rather than the most effective DSO. We disagree with this position. We believe that performance panels promote transparency and accountability. If DNOs have performed well against the performance panel criteria, the evidence used to communicate performance should be the primary deciding factor.

- 3.45 A further industry stakeholder did not support any of the 20% weighting being reassigned to another component of the DSO incentive. The stakeholder contended that there could not have been a legitimate expectation that the incentive weightings would have been changed. They also did not believe any stakeholder could have had a legitimate expectation that the DSO incentive weightings would be changed if the metrics were not switched on. They expressed doubts that the performance panel can ensure DNOs will be held accountable for the areas currently covered by the metrics and believe this represents poor value to consumers and network users. They also stated that adapting the performance panel criteria to include references to specific parts of the metrics does not address the loss of accountability for performance in those areas.

Our decision

- 3.46 After considering all options presented to us, we have decided to change our consultation position and reallocate the 20% weighting originally designed for the outturn performance metrics equally between the DSO performance panel assessment and stakeholder satisfaction survey.
- 3.47 Our view is that in the absence of qualitative and tangible metrics, placing additional emphasis on the diverse perspectives of stakeholders directly engaged with DSO services is crucial to supporting the development and implementation of these services. As previously highlighted, this will, as a minimum, allow us to capture views of stakeholders impacted by Curtailable Connections. Assigning an equal weighting between the two remaining components of the incentive will also aim to mitigate uncertainties associated with the new incentive structure, fostering transparency in performance evaluation. We recognise that this incentive is new and untested. Our aim is to ensure that the results are fair and balanced and optimise the potential benefits for consumers.
- 3.48 Our RIIO-ED2 Final Determinations confirmed that we would implement an incentive value of +0.4%/-0.2% of RoRE per year for the DSO incentive. This

would be +0.32%/-0.16% RoRE in the first year, reflecting that the outturn performance metrics (which would make up the remaining RoRE available through the incentive in later years) had not yet been implemented. We therefore believe it has been sufficiently clear that the value of the DSO incentive was always going to be +0.4%/-0.2% of RoRE in Years 2 – 5 of RIIO-ED2. We remain committed to this approach and disagree with the suggestion that, for example, we should not reallocate the additional value to either component. This would result in a less powerful incentive and risks missing out the substantial customer benefits that DSO can unlock during RIIO-ED2. Our RIIO-ED2 Final Determinations said that the weighting of the three components would be 40% to the survey, 40% to the panel and 20% to the metrics (excluding the first year). Our Final Determinations were silent on what would happen if the metrics were not implemented. We disagree that this created any expectation on what would or would not happen if this was the case. Once we concluded that our view was that the metrics were not in a suitable place to be implemented, we consulted on an alternative that sought to maintain the original intended value of the incentive in the latter years of RIIO-ED2. We have carefully considered the responses to this consultation and decided this is still the most appropriate approach. We have however listened to the concerns from respondents and adjusted this as described in the earlier paragraphs. The practical effect of this is that there is no change in the relative importance of the survey and panel between Year 1 and subsequent years.

- 3.49 We will work with DNOs to learn lessons from the performance panel and stakeholder survey in the first year of RIIO-ED2 and apply these to the following years. This could include changes to the survey questions and/or panel criteria to account for specific references to the areas that were considered by the metrics. Changes to the DSO Governance Document will be made in accordance with Part A of Special Condition 1.3 of the Electricity Distribution Licence ensuring that stakeholders have the opportunity to provide their own views.

4. Next steps

Section summary

This section describes the next steps to the DSO incentive following our decision on the outturn performance metrics.

- 4.1 Following the decisions outlined in this document, the following points detail the path forward and serve as a guide for moving from decision-making to implementation:
- **Licence change (Q2 2024)** – a licence change is required to give effect to our decision (ie, to reallocate the 20% weighting evenly to the performance panel and stakeholder survey) and subsequent impact on licence values. We will publish a statutory consultation on the proposed modifications to the Electricity Distribution licence soon.
 - **Further work on reporting requirements (Q2 2024 – Q1 2025)** - further work is required to develop the current methodologies to a level where they can adequately function as a reporting requirement for RIIO-ED2. This includes resolving any methodological issues and expanding the guidance around the metrics to ensure that each DNO has a common interpretation of each methodology. We encourage DNOs to work together to bring forward a set of agreed proposals that can be considered as part of any other changes to the RIGs needed for years 2025/26 onwards.
 - **Reflect on changes that may be needed to the performance panel and stakeholder survey for Year 2 (Q3 – 4 2024)** – consider whether there is a need for any changes to the performance panel and stakeholder survey for Year 2 – including changes to the survey questions and/or panel criteria to account for specific references to aspects of the metrics.
 - **Consult on RIGs and DSO Governance Document changes (Q1 2025)** - we will consult on any changes to the RIGs and DSO Governance Document that are needed to implement new reporting requirements and or improvements to the survey and panel. This will provide all stakeholders an opportunity to provide input to the proposals.