98 Aketon Road
Castleford
West Yorkshire
WF10 5DS

15 March 2024

David McCrone
Price Control Operations Policy
Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

Dear David,

RIIO-ED2 Distribution System Operation Incentive metrics consultation

We have supported the DSO incentive metrics development process keenly as, since the introduction of the DSO incentive in the ED2 draft determinations, we have held the position that it must contain sound objective measures of performance, alongside the more subjective elements of performance panel score and stakeholder survey.

We acknowledge the reasoning for turning off the metrics that Ofgem sets out in this consultation (data quality concerns, lack of historical data and potential for perverse incentives) and would suggest that this is symptomatic of how nascent the area of DSO is. The lack of clarity on primary outputs to be delivered highlighted in table 2 of your consultation demonstrates that it is not yet clear exactly where the directly identifiable value of DSO is delivered.

We are committed to delivering market leading DSO functions and fully recognise the benefits that this will deliver to our customers on the whole. However, we do not believe that performance panel assessment or stakeholder survey are effective regulatory mechanisms to identify strong performance and this would not lead to a sufficiently justified distribution of customer money. It is harder yet to understand how strong performance will be identified by the panel and stakeholders, when Ofgem and the working groups have not been able to clearly define primary outputs in the form of metrics. These mechanisms could lead licensees to carry out more visible DSO activities, rather than more subtle approaches that may be more cost effective.

The purpose of the DSO incentive (per Ofgem's DSO Incentive Governance document) is to drive licensees to more efficiently develop and use their network, taking into account flexible alternatives to network reinforcement. As we set out in our ED2 methodology response we believe that this purpose is achieved through cost and outcome mechanisms without the need for any discretionary incentives.

As such, our position is, in the absence of any objective element to the DSO incentive it is an overly subjective allocation of customer funds that does not effectively drive the desired outcomes. We therefore do not support the reallocation of the 20% metric incentive onto the performance panel element, and instead advocate for the entire DSO incentive to be switched off.

We have provided a more in-depth analysis of these points in answer to your specific questions in annex 1. We look forward to continuing to engage with you on this topic.

Yours sincerely,

Paul Glendinning
Director of Energy Systems

Appendix 1 – Detailed responses to consultation questions

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

Deferral of reinforcement using flexibility services is one of the central use cases of DSO, and as such should be one of the areas that is easier to define as a metric. As detailed in your consultation, there is clarity on the primary output of FDt and it is considered important.

However, during the ED2 period each licensee will face a different level of network constraints to address and each has a flexibility market available to them of differing maturity[1]. As such the expected performance of each licensee varies greatly.

Further, the number of constraints being solved for many licensees is relatively low and performance is subject to a number of externalities (load growth and constraints arising as expected, flexibility market growth, tender success, location of flexible assets) and as such performance is sensitive to these factors and volatile.

In addition, as work on defining standardised flexibility products is ongoing via the ENA Open Networks group whilst the metrics have been defined, there are no standardised definitions and interpretations to rely on. As such each DNO may take slightly different approaches to capturing the data associated with this metric.

In summary, taking these points into consideration, it will be difficult to set targets for licensees that are based on consistent principles and adequately address individual circumstances, whilst effectively driving performance.

Q2. Do you agree with our recommendation not to switch on the SFt outturn performance metric during RIIO-ED2? Please explain why.
Yes.

The intent behind the SFt metric was to drive licensees to have better secondary network visibility, however defining and measuring this in an annual time bound metric was a challenge. As such this led to the development of SFt as a forecasting accuracy metric, as a proxy for visibility.

As the developed metric is not aligned with the original primary output this leads to an incentive that may drive perverse behaviours and does not drive behaviour in line with customer benefit.

In addition, the metric formulation that was defined in the DSO Incentive Governance Document was subject to significant externalities, such as actual LCT uptake, weather, and socio-economic factors. This meant performance on this metric would be more driven by chance, rather than controllable factors. Further iterations of the formula sought to address this externalities point, however as can be seen from figure 6 this led to a metric performance expected to be mid-to-high 90% for all licensees – making it difficult to differentiate high performance.

[1] Regional Variation in the Uptake of Flexibility Services Report

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

We have previously highlighted issues with this metric in response to your consultation on the DSO incentive governance document:

> *The curtailment efficiency metric is seeking to incentivise behaviours that are not supported by Ofgem's Access and Forward-Looking Charges Significant Code Review ("Access SCR") decision and has practical challenges with any new data collection that would require funding and time to roll out.*

Furthermore, through the working group it became clear that it is difficult to define what good performance looks like and thus what a target should be; zero curtailment is bad, some curtailment is good, but too much curtailment is also bad.

Q4. Do you agree with our alternative approach to continue with the metrics as a reporting requirement? Please explain why.
Not as currently set out.

We advocate a much more simplistic price control in ED3 and believe DSO activity is effectively encouraged through objective 'ED1-type' mechanisms such as cost incentive and outcome delivery incentives. As stated above and in more detail in the question response that follows, in the absence of meaningful and objective metric assessment, Ofgem should turn off the whole incentive mechanism. Ofgem's reporting routines and public facing reports would allow it the necessary mechanisms to hold DNOs to account against a reputational incentive.

Q5. Do you agree with our alternative appro ach to reassign the 20% value of the inventive to the performance panel assessment? Please explain why.
No.

As stated in our response to your consultation on the ED2 methodology, we do not support the subjective elements of the DSO performance panel and DSO stakeholder survey:

> *[The DSO incentive will:]*
> a) *It will distort activity towards visible DSO outcomes, even if these are not cost effective, and away from more subtle approaches that deliver bigger consumer benefits.*
> b) *It will reward the best submissions, not the most effective DSOs.*
> c) *It is unnecessary; Ofgem could instead rely on its cost and outcome incentives, along with comparative competition between DNOs.*

Reassigning the 20% incentive value from the metrics to the performance panel will further exacerbate these points.

Instead, we believe that without a clear objective basis for the incentive the whole mechanism should be removed. If the DSO incentive continues with only the subjective measures, licensees are incentivised to carry out activities that may be more aligned to publicity and recognition rather than action that is rooted in sound cost benefit analysis and development of efficient networks.