

RIIO-ED2 Team

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**Octopus Energy's response to Ofgem's Draft Determinations for DNO allowances under the RIIO-ED2 price control**

We welcome the opportunity to respond to Ofgem's Draft Determinations for DNO allowances under the RIIO-ED2 price control. We are pleased to be a member of Ofgem's RIIO-ED2 Challenge Group and to have been asked to participate in a number of Ofgem led workshops on DSO Incentives in particular. We appreciate the opportunity to provide written feedback before final determinations are made by Ofgem this winter.

As Ofgem have rightly recognised it is crucial that during the ED2 period the building blocks for a smart, digitally enabled energy system are put in place. Without significant progress towards this aim over the next five years, aspirations for a net zero electricity system by 2035 will be severely undermined. We are not currently confident that the detail within the Draft Determinations provides strong enough incentives for DNOs to make substantial progress towards this goal. In particular, there are insufficient incentives on DNOs to: increase liquidity in local flexibility markets; improve visibility on their Low Voltage networks; and ensure new EVs and heat pumps can connect to DNO networks within acceptable timeframes.

There is still time, ahead of the next regulatory period, to ensure the groundwork is laid to effectively encourage DNOs to start adopting the right behaviours. Therefore our key recommendations for changes that Ofgem should focus on before final determinations are to:

- Update the secondary reinforcement volume driver to include the cost of procuring flexibility, as well as the cost of traditional reinforcement to meet unanticipated demand. This is essential to ensure DNOs are incentivised to consider flexibility first before traditional reinforcement
- Increase the relative value of the DSO incentive to at least +/- 1% of RoRE so that it is more reflective of the potential upside benefits that DSO delivery could unlock for consumers in the RIIO-ED2 period
- Review and update the performance metrics within the DSO incentive to ensure they drive the right behaviours to pave the way for a smart, digitally enabled energy system of the future

Our detailed response to the ED2 draft determinations is set out below. Given our expertise and business interests we have focussed our response on the questions which

relate to the progression of DSO responsibilities and emerging local flexibility markets in the RIIO-ED2 period.

We would be happy to meet or lend our support in any other way so Ofgem can strengthen the ED2 determination within the remaining timelines. Please email [madelaine.brooks@octoenergy.com](mailto:madelaine.brooks@octoenergy.com) or [kieron.stopforth@octoenergy.com](mailto:kieron.stopforth@octoenergy.com) in the first instance if you wish to discuss our response or any additional areas in the Draft Determinations further.

Thanks,

### **Questions in the Core Methodology Document**

#### **Core-Q4. Do you agree with our proposed secondary reinforcement volume driver and LV services volume driver and the associated controls?**

Whilst we agree with the proposed automatic secondary reinforcement volume driver, we are disappointed that there is no volume driver to cover the cost of the DNO procuring additional flexibility to manage this unanticipated volume. This serious omission means there is a very low incentive on DNOs to explore the use of flexibility for anything outside of the growth anticipated in their business plans.

Some DNOs did not commit to procure any Low Voltage flexibility services in the RIIO-ED2 period, and as currently designed, the uncertainty mechanism provides no way for them to unlock additional allowances for this purpose, incentivising traditional reinforcement rather than testing first for flexible solutions to defer the need to reinforce. This removes all optionality value that Ofgem has been so keen to create to ensure lowest costs for consumers. We therefore urge Ofgem to reconsider a volume driver with a unit cost allowance for flexibility in order to ensure a flex first approach is truly embedded within DNO's strategies in the RIIO-ED2 period.

It is vital that the secondary reinforcement volume driver has an associated monitoring framework to justify the needs case for the investment and to check that DNOs only use the volume driver when the needs case is justified and other approaches to defer investment have been exhausted. We understand that Ofgem intend for the metrics to be reported annually - with justification that this frequency allows proportionate monitoring of the volume driver. Whilst we do not think it should be necessary to report all metrics whenever the additional allowances are requested through the volume driver, we believe it should be a requirement to report the utilisation banding to justify the need for investment. Only when the utilisation banding is projected to be high should the investment be permitted. If the utilisation threshold is medium or low, then reinforcement should not be allowed as this does not indicate an urgent need for additional reinforcement. We understood that the intent of the volume driver was that it should be used for additional network needs due to unanticipated demand, therefore any strategic investment should already be ring fenced in DNO's business plans, and additional

allowances for this purpose should not be allowed through the volume driver. There is too much uncertainty as to where and when LCTs will connect, and any anticipatory reinforcement may prove to be an inefficient use of funds once LCT demand materialises and is not in the best interest of consumers. Projected or real utilisation information should be known by DNOs in order to forecast the need to upgrade and should therefore be quick and easy to report. This would only deviate from the current proposed process slightly and therefore we do not expect it to delay the volume drive allocation process significantly but would ensure the DNOs do not overinvest prematurely and there will be efficiency savings if this check is done ex ante rather than ex post.

We do not support there being a cap on the LV services volume driver. If all investment passes the utilisation band test, and the additional monitoring metrics proposed by Ofgem, then there should not be a further cap which would limit particular DNOs from moving faster to upgrade the network where there is a greater need in their network areas than other DNOs. As currently designed, the cap could impede certain DNOs from connecting LCTs quickly and this would work against the net zero targets and frustrate customers looking to decarbonise their heat or transport.

We support the LV services volume driver being used to fund proactive or reactive load related LV service reinforcement. In this instance, there is no way to use networks more smartly to enable customers to connect new LCTs and therefore unlooping of LV service cables is necessary, and should be supported whether proactive or reactive. We are supportive of DNOs proposals to use a more proactive approach for LV service unlooping, such as a street-by-street basis as in the future we expect most consumers to own LCTs and there is no alternative way to enable them to connect, meaning in this instance proactive approaches should be encouraged.

#### **Core-Q5. Do you agree with our proposed LRE re-opener?**

We support the proposal for a LRE re-opener to fund investment at higher voltage levels. This is appropriate for the requirements here as there is more variance in costs for works, making it difficult to arrive at a given revenue volume driver for unanticipated investment.

#### **Core-Q6. Do you agree with our proposed approach to the Net Zero re-opener?**

We support a Net Zero re-opener in the RIIO-ED2 period which can be used by Ofgem at any time throughout the period due to changes in government policy or the uptake in LCTs. It is essential that bodies other than Ofgem, can inform the circumstances to trigger a Net Zero re-opener.

#### **Core-Q7. Do you agree with our proposed approach to the value of the SIF?**

We agree to keeping the SIF at the same level. However, the way that the SIF is delivered needs several material improvements.

First, there are almost two years between applying for Discovery and the award of Beta for successful projects. While SIF attempts to be agile, the length of this process risks locking participants into designs that have become obsolete through changes on the system. More money should be directed towards tests rather than feasibility studies and there should be an accelerated pathway directly to beta for projects that are ready.

Second, operating businesses should have a greater role - they should be able to propose SIF ideas and lead consortia. This would enable solutions to be grounded in practically deliverable solutions and ensure value for money as well as financial discipline.

Third, significant portions of innovation spending goes to professional services firms. It would be better value for money for the customer for this to be spent on operating companies that can deliver real solutions and real value.

**Core-Q17. Do you agree with our proposal for implementing a Digitalisation Licence Obligation?**

We agree with the proposal to implement a Digitalisation Licence Obligation which will ensure DNOs publish Digitalisation Strategy and Action Plans, and comply with Data Best Practice. It is important that DNOs plans and the progress they are making in digitalising their networks are transparent and accessible to all their stakeholders. As we move towards more actions needing to be taken closer to real time to manage DNO networks and customer requirements, digitalisation is a fundamental enabler to ensure this becomes reality.

In the final determinations for ED2, Ofgem must explain what action it will take to ensure that DNOs actually deliver on their digitisation commitments within the planned timeframes. As a minimum, we would like to see Regulatory Reporting capture information about DNO data publication and operational data sharing throughout the ED2 period, and that there is the ability to add in new RREs relating to digitisation when needed.

**Core-Q19. Do you agree with our proposed Digitalisation re-opener?**

Yes we agree with the proposal for a Digitalisation re-opener as there are a number of uncertainties about emerging policy topics which could result in a shift in requirements on DNOs from a data and digitalisation perspective. We support Ofgem being able to determine the re-opener window at any point during RIIO-ED2.

**Core-Q22. Do you agree with our intention to modernise the regulatory reporting process?**

We fully support Ofgem's proposal to modernise the regulatory reporting process, and think that this will result in real benefits for all stakeholders.

**Core-Q23. Do you agree with the proposed timeline for implementation of this modernisation?**

Yes, we agree with the proposed timeline.

**Core-Q24. Do you agree with our proposed design of the DSO incentive?**

The introduction of a DSO incentive is a positive development, but the incentive value is too small to drive real change and Ofgem risks missing a vital opportunity to drive substantial moves to the flexible, smart energy system needed if we are to achieve net zero in the most cost effective and speedy way. The savings that DNOs have projected that use of flexibility and other smart solutions to defer the need to reinforce their networks are substantial. Therefore we recommend that Ofgem increases the DSO Incentive value from 0.2% of RoRE to 1% of RoRE, so that the potential benefit is more proportionate to the customer benefits. Equally we believe the value should be split evenly across metrics, performance panel and stakeholder survey with 33% each so that there is a greater weighting towards mechanistic measures to monitor performance, and the weighting for the more subjective stakeholder survey element is reduced.

Transparency and the ability to objectively judge each DNO's effectiveness in DSO activities is key. DNOs should have to provide information in a concise and uniform manner to ensure accountability and full transparency. The stakeholder survey should be concise and easy to complete by stakeholders to ensure maximum participation across the industry. Both stakeholder survey and the performance panel should have a high level of ambition in line with measures required to meet climate objectives.

DNO performance on each of the incentive levers should be easily available through an annual leaderboard or short summary that is easily digestible by the public. Metrics should be published. This would ensure that reputational risks and benefits help to drive executive focus and real change.

**Core-Q25. What are your views on the outturn performance metrics and RRE we are proposing to include in the DSO incentive? If you do not support their inclusion, please outline which alternative outturn performance metric(s) or RRE you think should be included in the framework instead.**Outturn performance metrics

We support the principle that the flexibility market testing metric is trying to achieve in that this should validate DNO's commitments to considering flexibility first before other solutions to run efficient and safe distribution networks. Whilst we agree that a penalty only metric makes sense for the primary network where DNOs are already extensively procuring flexibility and have good levels of visibility of this network, we are less certain that a penalty is most suitable way to drive the right behaviours on the secondary network. Only very few DNOs are currently procuring flexibility services from assets on their secondary networks, and whilst we see this as an important direction to head in, it

may instead drive better progress if this part of the metric was incentivised rather than penalised - given the lower level of visibility of this network at present and the varying degrees of competency across DNOs in procuring these services. The proposed measurement process also seems particularly onerous when applied to the secondary network and we encourage Ofgem to explore whether a simplified measurement process could be used. It is important that market testing for flexibility on the secondary network remains a part of the metric, but we question whether there could be more effective ways to drive progress and to simplify the measurement process.

The network visibility metric is an input measure and we are not confident it will drive the right behaviours from DNOs as a result. Whilst it is important that DNOs better understand their secondary networks and make data more available to users, we remain agnostic about the method by which this is done. The value of improved monitoring is the additional insight and understanding about the network that this will unlock, enabling stakeholders to have more information to determine where to site assets and DNOs to make more informed decisions about how and when the secondary network needs to be upgraded, thereby saving consumers money from more timely investment. In principle we think a metric measuring the accuracy of load forecasts vs actual load profiles would be a better measure which drives DNOs to behave in ways which are beneficial to system users.

We support the metric on curtailment efficiency and expect it to work well. We are happy that this is proposed to be applied to both existing and new non-firm connections, as DNOs should be encouraged to reduce curtailment for all connectees regardless of the specifics of the contractual arrangements. It is important that this applies to existing connections in particular as otherwise there may be a risk that DNOs prioritise curtailing older connections with less well defined curtailment obligations than generators under new connection agreements. Whilst we understand that this may be the reality, there should be a way to reward DNOs who outperform expected curtailment profiles for these older connections too to ensure the incentives are consistent regardless of the connection agreement terms.

If Ofgem does not decide to use utilisation to assess whether the additional allowances can be granted through the secondary volume driver, then there needs to be a metric on utilisation. There are huge variations in the point at which different DNOs reinforce their networks and this needs to be standardised in order to ensure that all reinforcement is done in the best interests of consumers. This utilisation metric should be penalty only. It could involve DNOs having to report utilisation bands in which proposed reinforcements fall under and where reinforcement is proposed and utilisation is below a percentage defined to be acceptable then they must pay a penalty.

#### Regularly Reported Evidence (RRE)

We are largely happy with the information proposed to be included in the regularly reported evidence as this covers all of the expected DSO functions. However, it is important that there is the opportunity to add additional items to measure in the RRE as

new requirements emerge throughout the period. Whilst some of the RREs may indicate the performance of DNOs in certain areas, it is important that the performance panel assessment report allows DNOs to provide evidence to back up some of the RRE scores. For instance, allowing DNOs to demonstrate how they've tried to incentivise flexibility participation in their area, such as hosting events for industry participants or other measures. This will ensure the performance panel has the information available to score DNOs based on their actual performance rather than any external factors which may impact the RREs beyond DNOs control.

We note that the lists of datasets for DNOs to publish are still to be defined but we'd like to highlight the importance that congestion data is published as close to real time as possible down to secondary networks (where possible to do so) in the RIIO-ED2 period. Some DNOs indicated that they expect congestion to be more of a problem on their secondary networks than their primary networks in the near future, and it is therefore important that users can validate this assumption and use this information for investment decisions in storage assets and other technologies able to help reduce congestion in particular areas as soon as possible.

We have included some specific comments on each of the proposed RREs below:

No	RRE	Comments
1	Capacity released through flexibility	Agree that this will be useful to track, but could Ofgem separate the requirements so that capacity released is reported on separately for primary and secondary levels.
2	Distribution flexibility trading	Support inclusion, no comments on detail.
3	Forecasting accuracy	Very important measure - see comments on outturn performance metrics, but we believe this would be a better metric to drive DNOs to improve secondary network monitoring capabilities. However, it should still be measured on the primary network too.
4	Transformer utilisation	This is very important to validate that DNOs have exhausted all other options before choosing to reinforce. We suggest that this forms part of the original Secondary Reinforcement Volume Driver check, rather than an ex post.
5	Data publication	Support inclusion, although it is difficult to comment on when the dataset requirements are still to be defined. Should ensure that further metrics can be added throughout the ED2 period.
6	Operational data sharing	Support inclusion, although it is difficult to comment on when the dataset requirements are still to be defined. Should ensure that further metrics can be added



		throughout the ED2 period.
7	Flexibility procurement	Support inclusion, but urge that the requirement is to separate contracted vs tendered by service and voltage level.
8	Flexibility tendering bid acceptance rate	As above.
9	Flexibility dispatch	As above.
10	Registration time	Support inclusion, no comments on detail.
11	Flexibility market participation	Support inclusion, no comments on detail.
12	Diversity of technologies in distribution flexibility services	Support inclusion, but urge that the requirement is to separate contracted vs tendered by service and voltage level.
13	DNOA decision outcomes	Support inclusion, no comments on detail.
14	Investment decisions review	Support inclusion, no comments on detail.
15	Error corrections issued for dispatch	Support inclusion, no comments on detail.
16	Late issuance of dispatch data	Support inclusion, no comments on detail.

### **Core-Q26. Do you agree with our proposal for the DSO re-opener?**

In light of the recent Ofgem Call for Input on local institutions and governance arrangements, it is sensible that there is a DSO re-opener to account for any future changes to the roles and responsibilities that may come about once this review is concluded. It is important that the review of local governance arrangements stays on track and publishes early conclusions in 2023 as has been outlined. If this work is delayed then DNOs will not have clarity on the future of local governance arrangements until the end of the RIIO-ED2 period, and this could have serious implications on their ability to successfully carry out the DSO roles expected of them. We ask that Ofgem provides further clarity on how DNOs should continue to operate in the meantime until this review is concluded, as there is a large degree of disparity in their business plans on separation of DSO and DNO governance.

### **Core-Q27. Do you agree with our proposal to introduce a new whole system strategic planning Licence Obligation?**



We agree with Ofgem's proposal to introduce a new whole system strategic planning Licence Obligation. As the core methodology document states more co-ordination with other local actors will be needed in the next decade as we embark on economy wide decarbonisation. We support that the plan should be live and digital, as this will improve accessibility for stakeholders and make the plans as useful as possible. Alongside the plan, it is also important that all other local stakeholders we expect DNOs will need to engage with are included in the stakeholder survey as part of the DSO incentive. Whilst publishing strategic plans should help set the direction for DNOs, the effectiveness of the plans and ability of DNOs to deliver on ambitions will best be verified by the stakeholders that DNOs must coordinate with.