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National Grid ESO response to RIIO-ED2 DSO Incentive Governance Document Consultation

Dear Mike,

Thank you for the opportunity to respond to the RIIO-ED2 DSO Incentive Governance Document Consultation.

As the Electricity System Operator (ESO) for Great Britain, we are in a privileged position at the heart of the energy system, balancing electricity supply and demand second by second. As the UK moves towards its 2050 net zero target, our mission is to drive the transformation to a fully decarbonised electricity system by 2035, which is reliable, affordable and fair for all.

We play a central role in driving Great Britain's path to net zero and use our unique perspective and independent position to facilitate market-based solutions to the trilemma of affordability, sustainability and security. We welcome Ofgem's publication of the Incentive Governance Document to support the transition to Distribution System Operation (DSO). The transition will also impact the ESO, and we need to ensure that our roles and responsibilities develop in co-ordination with DSO. We strongly believe that the implementation of consistent and fair frameworks under the network price controls is crucial to deliver efficient, whole system outcomes for the benefit of consumers. Therefore, alignment of DSO activities across the network organisations is key in supporting the delivery of a low carbon energy system. This is not only critical for the success of DSO, but also in allowing effective ESO/DSO coordination.

General points

We understand that formal DSO arrangements begin from the start of ED2 and therefore this is the first time a DSO incentive scheme has been developed. We welcome Ofgem's intention in this space to incentivise best practice for DSOs and emphasise the need for continued focus, as RIIO-ED2 progresses, on promoting consistency and alignment of DSO activities. This will ensure that the ESO can effectively co-ordinate with all six DNOs as their DSO functions develop and is particularly important in areas such as service coordination and DER visibility. We believe these are not just a priority for the ESO but also for wider industry stakeholders.

Furthermore, we welcome that our RIIO-ED2 feedback to date - encouraging effective DSO/ESO coordination - has been recognised in part via the proposed stakeholder satisfaction survey question centred on DSO coordination. We also welcome the management of actual or perceived DNO/DSO conflicts of interest under the stakeholder satisfaction question themes. We look forward to further clarity on this alongside Ofgem's final decision on Customer Load Active System Services (CLASS).

We would welcome the opportunity for ESO to be part of the Performance Panel.

Incentive scheme framework

We recognise that the framework broadly mirrors the ESO incentive scheme and welcome this. We also recognise that ED-2 is the first time that DSO activities are recognised as a separable element of DNO activity. Therefore, this is the first time an incentive has been put in place to drive performance, and as such the

incentive scheme is likely to develop further as we move into DSO implementation. We set out some further considerations on the areas where there are differences to the ESO scheme:

Penalty/reward mechanisms

ESO have transparent penalty and reward mechanisms tied to the incentive scheme. We would welcome clarity and rationale for proposed penalties/rewards for the DSO schemes and whether these are similar in terms of materiality.

Clarity on how DSOs achieve high performance

It is not currently set out what is expected for DSOs to “exceed” expectations across the role activities, noting this may be more challenging when performance is assessed qualitatively. It is important that DSOs are incentivised to achieve high levels of performance. We recognise that this may be something that comes later due to the stage in development of DSO, but we would welcome Ofgem providing further guidance in due course on this to provide the right steer to DSOs.

Scoring mechanisms

The proposed scoring criteria for performance is more granular to the ESO scheme (1-10 for DSO vs 1-5 for ESO). It would be helpful to understand the rationale for this including the allocation of below, meeting and exceeding expectations by score. For example, we would question whether a score of 7 should be classed as exceeding expectations.

DSO Performance Panel assessment criteria

One of the evaluation criteria set out in the ESO incentives scheme is Plan Delivery which enables the Performance Panel to consider whether the ESO delivery schedule has been successfully delivered on time and/or whether the ESO has delivered additional outputs in line with the expectations in our Roles Guidance. In the absence of a plan delivery criteria in the DSO incentives process, we would like to understand where Ofgem has confidence that a DNO has undertaken activities that are in line with the purpose of the DSO incentive.

Similar to the above, within ESO’s incentive scheme the cost of delivering planned outputs is considered under the value for money evaluation criteria. For ESO, cost benchmarks are set to enable the Performance Panel to assess whether ESO are below, meeting or exceeding expectations. In the absence of a value for money criteria and associated cost benchmarks in the DSO incentives process, we would welcome guidance around how Ofgem will assess whether a DNO is delivering value for money in what is being spent in relation to DSO activities.

Finally, we recognise that both DSO and ESO incentive schemes may evolve over the coming months due to regulatory cycles. Ofgem should ensure that these schemes remain consistent where appropriate in approach, noting that there are multiple DNOs carrying out DSO activities in different regions of the country. The framework should be designed to take account of these regional differences, without introducing unnecessary complexity and whilst maintaining standardisation.

We welcome the opportunity to discuss any of the points raised within this response. Should you require further information or clarity please contact Adelle Wainwright in the first instance. Our response is not confidential.

Yours sincerely

Matthew Wright

Head of Strategy and Regulation