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Sent by email to: flexibility@ofgem.gov.uk

Dear Mike,

Distribution System Operation Incentive Governance Document

Thank you for the opportunity to provide feedback on the draft guidance. This is a non-confidential response on behalf of the Centrica Group.

It is necessary that the Distribution System Operation (DSO) Incentive is carefully designed and calibrated given it will be one of the main ways of encouraging the distribution network operators (DNOs) to adopt the right behaviours during the RIIO-ED2 price control, ahead of the review of local energy system operation¹ being concluded and the recommendations being implemented. We recognise the difficulties in setting sufficiently challenging targets for the Outturn Performance Metrics. We, therefore, agree that the financial incentive value associated with the Outturn Performance Metrics should be set to zero for the first year of RIIO-ED2. This will allow more time for these elements of the DSO Incentive to be appropriately calibrated.

We comment on some aspects of the draft guidance below and recommend ways in which it can be strengthened.

Stakeholder survey questions:

We previously highlighted that the differences in the DNOs' approaches to and schedules for delivering DSO functions will cause operational inefficiencies for market participants operating in multiple regions². The DNOs were not subsequently required to standardise their approaches and schedules despite stakeholders' concerns about the differences³.

We consider that the lack of standardisation, particularly in the ways in which flexibility markets are operated and the actions required from market participants, is an unnecessary barrier to

¹ See: <https://www.ofgem.gov.uk/publications/call-input-future-local-energy-institutions-and-governance>.

² In our responses to the Call for Evidence on the DNOs' RIIO-ED2 business plans and to the Draft Determinations.

³ Other stakeholders also raised concerns about the lack of standardisation for the delivery of DSO functions.

market entry. We think it would be beneficial for the Performance Panel to assess the DNOs' voluntary efforts to increase standardisation, thereby reducing operational inefficiencies. We recommend that a question be included in the stakeholder survey which allows stakeholders to explicitly comment on the DNOs' efforts to increase standardisation.

Flexibility Market Testing Outturn Performance Metric:

We support this performance metric being included, to quantify the extent to which the DNOs consider flexibility as an alternative when reinforcement is required. We disagree with the metric being applied only to the primary network, as it excludes measuring performance in relation to the secondary network.

Standard condition 31E of the Electricity Distribution Licence requires DNOs to, among other things, procure and use Distribution Flexibility Services where it is economic and efficient to do so. No distinction is made between primary and secondary networks in this standard licence condition. Extending the scope of the Flexibility Market Testing Outturn Performance Metric to include the secondary network does not place additional requirements on the DNOs above and beyond what they are required to do to comply with standard condition 31E; it would merely quantify what the DNOs have done in order to comply with this standard licence condition.

Secondary Network Visibility Outturn Performance Metric:

We also welcome Ofgem reconsidering the metric that should be used to represent network visibility and to which a financial incentive is attached. Ofgem now proposes to use a measure of the network that is 'monitored' instead of the accuracy of year-ahead demand forecasts for the secondary network. In principle, incentives should be focussed on outputs and outcomes (e.g. year-ahead forecasting accuracy) rather than on inputs (e.g. volume of monitoring devices) where appropriate. However, it has not yet been demonstrated that a strong relationship between the volume of monitoring devices installed and forecasting accuracy exists or that increasing the volume of monitoring devices installed is the only means by which forecasting accuracy can be improved.

More importantly, increasing the coverage of monitoring devices across distribution networks increases the DNOs' capability to operate their networks in real time. The enhanced capability in real-time operation is critical for the efficient dispatch of flexibility and other distributed resources. It also facilitates DNOs making more capacity available on the system, when lack of network capacity remains a barrier to the uptake of renewable and other low carbon technologies. Improved forecasting performance will not automatically be accompanied by an enhanced capability in the real-time operation and, therefore, using forecasting accuracy as a metric to represent network visibility is sub-optimal.

The accuracy of year-ahead demand forecasts for the secondary network is still a useful measure of performance. We recommend this metric is added to the suite of Regularly Reported Evidence (RRE) to complement the primary network forecasting accuracy performance measure (RRE 2) and to encourage the DNOs to provide accurate forecasts at both the higher and lower network voltages.

Annual call for evidence:

The draft guidance that has been published is an improvement on the version that was previously shared with the DSO Incentive working group. Particularly, we welcome that stakeholders will be invited to provide feedback on the DNOs' performance⁴. We agree that stakeholder feedback will reduce the information asymmetry between the DNOs and the DSO Performance Panel and, therefore, will mitigate against the systematic bias in assessing performance that would otherwise arise if only the DNOs were permitted to provide evidence. The call for evidence will also allow stakeholders to provide detailed feedback that cannot be provided via the stakeholder surveys and will make it easier for new market participants with new business models to provide feedback.

Performance comparisons:

A key issue to be resolved is how the performance of those DNOs that proposed ambitious plans and the performance of those DNOs that proposed less ambitious plans can be measured in an equitable way. It is also necessary to consider performance against set criteria as well as performance relative to the commitments DNOs made in their DSO strategies. We recommend this issue is addressed in the guidance that Ofgem will develop for the DSO Performance Panel.

We hope you find these comments helpful. Please contact me if you have any questions.

Yours sincerely,

Gregory Edwards
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Centrica Regulatory Affairs & Policy

⁴ Draft guidance paragraph 4.11.
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