



Review of Unit Costs for LV Service Volume Drivers

Ofgem

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FINAL REPORT



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Executive summary

Ofgem is planning to consult in Q1 2026 on its review of Low Voltage Services Volume Driver (LVSVD) for ED2. In the ED2 Final Determinations, Ofgem committed to a mid-period review of the LVSVD at Year 3 of ED2. At ED2 there was limited historical data available to underpin the forecasts used to set unit rates for ED2 and, since then, DNOs have submitted evidence to suggest that Ofgem's current unit rates might not be cost-reflective.

In preparation for this consultation, Ofgem has commissioned CEPA to support its review of ED2 unit cost rates for two service activities under LVSVD: overhead pole line (OHL) and underground cable (UG) additions.

This note sets out our advice on potential methodologies for setting updated unit rates for ED2 years 4-5 (i.e. on a forward-looking basis) and draws out the trade-offs between these alternative approaches. This analysis is informed by responses from 3 of the 6 DNO groups to a Request for Information (RFI) in November 2025, as well as company regulatory reporting packs (RRPs).

We agreed with Ofgem to assess four shortlisted options:

Option	Description
(1) Use current unit rates	Maintain the existing ED2 unit rates for OHL and UG services (i.e. no recalculation or updates).
(2) Use rates based on updated methodology, applied to costs in ED2 business plan	Apply the ED2 methodology on a consistent per-addition basis, by removing the volume-doubling treatment for ENWL and NGED (which was applied at ED2).
(3) Use rates based on updated methodology and ED2 outturn data	As in Option 2, remove the ENWL/NGED volume-doubling treatment; plus update unit rates for ED2 Years 4-5 based on ED2 Years 1-2 outturn costs and volumes as reported by DNOs in the 2025 RRP.

(4) Use DNO forecast rates

As in Option 2, remove the ENWL/NGED volume-doubling treatment; **plus** update unit rates for ED2 Years 4-5 based on DNOs' forecast unit cost data for those years, where available.

We assess these options against four criteria, which reflect Ofgem's objectives for the unit cost drivers at the ED2 Final Determination (FD) stage, align with Ofgem's ED3 documentation to date, and which facilitate differentiation between the options:

1. **Methodological coherence:** Are unit rates calibrated on the same basis as they are applied in the mechanism, i.e., do they reflect efficient costs on a £ per service addition basis (the unit on which the LVSVD pays)?
2. **Cost reflectivity and incentives for cost efficiency:** Do the unit rates reflect efficient delivery costs likely to be incurred, while providing appropriate efficiency pressure (i.e., stretching but achievable)?
3. **Delivery incentives and volume efficiency:** Does the approach encourage delivery of the right activities and volumes (including proactive work), avoiding systematic under-delivery and/or inefficient over-delivery?
4. **Evidence quality and proportionality:** Is the approach evidence-based and replicable using available data, transparent to stakeholders, and proportionate to implement?

Our main findings are as follows:

- The methodology to set unit rates for OHL and UG should be updated for ENWL and NGED to reverse an adjustment made in the FD calculation that created an inconsistency between the unit cost (per property) and unit rate (per addition).
- ED2 outturn costs to date appear to be materially higher than forecast costs. This would support a minded to position of recalculating the unit rate based on actual ED2 outturn costs, if they are believed to be a more reliable predictor of unit costs for Y4-5 than the ED2 forecasts. However, this conclusion is uncertain given low volumes of work to date in ED2.
- Ofgem should use its consultation to gather views on the reliability of ED2 outturn costs as a predictor of unit costs for ED2 Y4-5, and the potential to set the unit rate by triangulating across forecast and outturn costs, noting that both may provide some insight into the efficient unit costs of volumes during ED2 Y4-5.

1. CONTEXT AND BACKGROUND

Ofgem is planning to consult in Q1 2026 on its review of volume drivers for ED2. In preparation for this consultation, Ofgem has commissioned CEPA to support its review of unit cost rates for two service activities under the Low Voltage Services Volume Driver (LVSVD) – overhead pole line (OHL) additions and underground cable (UG) additions.

Ofgem is not considering retrospective changes to the unit rates for these activities ED2 years 1-3 as part of its review. Therefore, this note sets out our advice on potential methodologies for setting updated unit rates for ED2 years 4-5 (i.e. forward-looking), and draws out the trade-offs between these alternative approaches. As Ofgem's analysis suggests that the LVSVD cap is unlikely to bind even if unit rates for these two service activities are increased, we do not assess changes to the cap.

1.1. ED2 FINAL DETERMINATIONS: LVSVD DESIGN AND UNIT-RATE METHODOLOGY

For ED2, Ofgem introduced a set of Load-Related Expenditure (LRE) uncertainty mechanisms to allow DNO funding to adjust as demand for low-carbon technologies (e.g. EVs and heat pumps) evolves. The LVSVD is one of these mechanisms and is intended to fund specified LV service reinforcement activities, particularly unlooping of LV service connections.

The LVSVD provides funding through:

- an ex-ante allowance set at the ED2 determination stage (a combination of the disaggregated benchmarking component (unit rate × forecast volumes) and the totex benchmarking component); and
- an in-period reconciliation that adjusts allowed revenue in line with actual volumes delivered (unit rate × outturn volumes).

Where the funding from this reconciliation materially exceeds the ex-ante allowance, Ofgem may review delivery (using volume driver metrics) and may disallow volumes it considers inefficient. The reconciliation mechanism is also subject to an overall cap that limits the expenditure that can be recovered under the LVSVD volume driver for each licensee throughout the whole ED2 period^{1,2}. This cap is set on an aggregate basis rather than for individual service activities).

The LVSVD covers four categories of service activity: (1) OHL, (2) UG, (3) Switchgear, and (4) Fuse upgrades. For ED2, Ofgem set unit rates for each service activity under the LVSVD using an industry benchmark approach. For LV services, Ofgem combined proactive and reactive³ forecast costs and volumes from ED2 business plans, to derive a common set of ED2 industry median unit costs for each LV service asset category. These were then applied as unit rates for each activity in the LVSVD.

When setting the LVSVD unit rates during ED2 Final Determinations, achieving like-for-like comparability of business plan data for OHL and UG across DNOs was a key challenge. To address this, Ofgem applied a volume adjustment for a subset of DNOs that sought to place the unit cost evidence on a more consistent basis⁴, as described in Box 1.

¹ Ofgem (2023) LRE Volume Drivers Governance Document.

² The LVSVD cap is the sum of the DNO ex-ante submitted costs, and costs subject to the uncertainty mechanism. The cap for ED2 is £680.4m, compared to the LVSVD Final Determinations set allowance of £259.9m.

³ Reactive service reinforcement is prompted by customers, generally for Low Carbon Technology (LCT) installation, whereas proactive reinforcement is initiated by the DNO. Ofgem (2025) ED3 Sector Specific Methodology Consultation.

⁴ Ofgem (2022) RIIO-ED2 Final Determinations Core Methodology, paragraph 7.198.

Box 1: Ofgem's rationale for the volume adjustment

Ofgem judged that LV Services business plan data (OHL and UG) was not directly comparable across DNOs because licence areas assumed different relationships between an LV service addition and the outcome of this activity (the number of properties unlooped). Forecasts from some DNO groups (ENWL and NGED) implied one addition could unloop two properties (a 1:2 relationship), while forecasts from other DNO groups (SPEN, SSEN, UKPN, ENWL) assumed one addition per property unlooped (a 1:1 relationship).

These different assumptions make unit costs expressed as '£ per addition' less comparable across the DNOs, because an addition is not the same-sized unit of work in each case. A DNO assuming 1:2 could unloop the same number of properties with around half the number of additions. This mechanically increases its '£ per addition' even if its underlying cost per property unlooped is similar.

To standardise the denominator for benchmarking, Ofgem doubled the LV Service volumes for ENWL and NGED DNO groups (i.e., 5 DNOs). Ofgem's intention was that, by placing all DNOs on a consistent 1:1 basis for the unit-cost derivation, the £/LV Service unit costs would be comparable across DNOs.

In the ED2 Final Determinations⁵, Ofgem committed to a mid-period review of the LVSVD at Year 3 of ED2. At ED2 there was limited historical data available to underpin the forecasts used to set these unit rates, and Ofgem highlighted some uncertainty as to the level of future volumes. The review is intended to assess whether the mechanism's parameters, including the unit cost rates and the cap, remain appropriate and are operating effectively. In particular, it seeks to ensure unit rates are set at the right level to support efficient delivery, while avoiding perverse outcomes, e.g. where justified investment is discouraged, or where inefficient investment is inadvertently rewarded.

1.2. EMERGING EVIDENCE AND ISSUES DURING ED2

Three DNO groups responded to Ofgem's November 2025 Request for Information (RFI) for LVSVD – SPEN⁶, SSEN and UKPN – covering seven of the fourteen GB DNO licence areas (SPD, SPMW, SSEH, SSES, LPN, SPN and EPN). However, these responses also provided summarised unit cost data across all fourteen DNOs.

In the responses, the DNOs raised concerns around the suitability of the unit rates for OHL and UG in view of outturn cost information. Therefore, the scope of Ofgem's review, and this note, is focused on OHL and UG only, and does not consider switchgear or fuse upgrades.

Across these RFI submissions, the narrative is consistent that the current ED2 unit rates result in material under-recovery of costs under the LVSVD. The shortfall is reported to be most pronounced for LV underground (UG) service installations, reflecting the relatively high volumes of this activity. Analysis by the Energy Networks Association⁷ (ENA) in response to the RFI indicates that, across all DNOs, LV service works in Years 1-2 incurred £104.1m of expenditure, while only £77.3m has been recovered through the LVSVD (i.e. approximately 74% of outturn costs have been funded). This implies under-recovery of around £26.8m, with the majority (85%) of under-recovery attributable to UG.

The DNOs argue that this under-recovery is driven by:

- 1) **Methodological issues:** Ofgem applied a volume adjustment to standardise the ED2 benchmarking dataset onto a common, per-property basis. This adjustment reduced the implied unit costs for ENWL and NGED, and therefore lowered the industry benchmark (median unit cost) used to set allowed rates (see Box 1).

⁵ Ofgem (2022) RIIO-ED2 Final Determinations Core Methodology, paragraphs 3.37 and 3.59. Also see Ofgem (2022) RIIO-ED2 Draft Determinations Core Methodology, paragraph 3.73.

⁶ Although ENWL is now part of the ScottishPower group as SP Electricity North West, it was not included in SPEN's RFI response (which covered only SPD and SPMW).

⁷ Referenced in Ofgem's presentation: Load Related Expenditure Volume Drivers Review, 15th December 2025.

- a) The LVSVD pays £ per service addition, but the volume adjustment effectively calibrates the benchmark on a £ per property unlooped basis. This creates an inconsistency, meaning the adjusted unit rate may be systematically non-cost-reflective when applied on a per-addition basis.
 - b) Even on a per-property basis, costs may not scale proportionately with the number of properties unlooped. For example, LV service jobs include fixed, per-intervention elements (e.g. traffic management, mobilisation, site setup), which do not increase linearly with the number properties unlooped. An intervention which unloops two properties will not necessarily cost twice as much as an intervention which unloops one property. On this basis, halving ENWL and NGED's implied unit costs (by a simple 'doubling' of their volumes) may have reduced their unit costs by more than is justified.
- 2) **Unforeseen additional works in carrying out unlooping:** Across the three RFI responses (SPEN, SSEN and UKPN), there is a consistent narrative that ED2 delivery has highlighted non-optional additional works, which materially increase the cost of delivering LV service upgrades. For example, challenging service locations and meter positions, buried services, concrete driveways, etc. They argue these drivers were not adequately captured in the evidence base available at ED2 Final Determinations, and therefore are not reflected in the current allowed unit rates. More generally, unlooping is a relatively new activity, and there was limited historical evidence at Final Determinations on which to calibrate forecasts.

As outturn LVSVD funding is determined by applying unit rates to outturn volumes, there is a risk that, if unit rates are materially below efficient delivery costs, DNOs may reduce or defer delivery volumes. This may be most marked for proactive programmes, as those are the volumes over which DNOs have greater discretion or control.⁸ This could undermine timely network readiness for electrification of heat and transport (e.g. EV charging and heat pumps).

Delivery to date in ED2 has also been more reactive than Ofgem expected. This matters because proactive programmes can typically be planned and standardised and are therefore often lower cost than reactive interventions. In ED2 Years 1–2, around 46% of UG volumes were delivered reactively, whereas 34% of FD implied volumes for UG were forecast to be delivered reactively. Across UG and OHL combined, delivery to date is around 9 percentage points less proactive than assumed at FDs.⁹

The methodologies we assess are intended to address the issues identified to date, improving cost reflectivity and strengthening delivery incentives.

1.3. ED3 CONTEXT AND IMPLICATIONS

Looking ahead to ED3, Ofgem is consulting on a more proactive, plan-led approach to distribution investment. A greater share of funding is expected to be provided upfront through baseline allowances set at the start of the price control, with less reliance on multiple, in-period funding adjustments. Ofgem is also consulting on a more selective use of reopeners (mechanisms that adjust allowances during the period) and reducing their number, while retaining the ability to respond where new needs emerge.¹⁰

⁸ Whilst reactive interventions are typically more expensive than proactive interventions, companies have less control over these volumes because, where reactive LV services are triggered by a customer request, DNOs are generally obliged to progress the request, subject to standard conditions.

⁹ This calculation is based on outturn volumes reported in the 2025 RRP. We compare against the implied ED2 Final Determinations volumes (ex-ante allowed expenditure divided by the allowed unit rate), i.e. the volumes DNOs were funded for ex ante. Particularly for UG, outturn volumes for FY2024 and FY2025 indicate a lower level of proactive delivery compared to ED2 forecasts.

¹⁰ ED3 Framework Decision, para 3.28; ED3 Sector Specific Methodology Consultation, para 9.17



In this context, Ofgem has indicated that the funding arrangements for the LRE Secondary Reinforcement and LVSVD will change in ED3.¹¹ Ofgem has noted that, although ED2 included mechanisms such as the secondary reinforcement volume driver, most reinforcement allowances are not linked to specific output or volume measures. Therefore, Ofgem considers that stronger delivery accountability is needed in ED3 to reduce the risk of under-delivery or deferral. Taken together, this suggests volume drivers may play a more targeted role within a broader ED3 framework that is funded upfront, monitored through stronger delivery assurance, and supported by a range of adaptability mechanisms where circumstances change.

In view of this direction of travel, Ofgem has advised us that the ED2 mid-period update should:

- be proportionate and targeted;
- improve cost reflectivity and delivery incentives for ED2 Years 4-5 using the best available evidence; and
- maintain a clear audit trail so the analysis can inform ED3 design and future data expectations.

¹¹ ED3 Sector Specific Methodology Consultation, para 7.24

2. OPTIONS APPRAISAL

In light of the emerging evidence and issues set out in Section 1, Ofgem has commissioned CEPA to assess options for updating the LVSVD unit rates for OHL and UG on a forward-looking basis for ED2 Years 4-5. This section sets out our assessment criteria, options discounted from an initial longlist, the shortlisted options, and our full assessment of the shortlisted options.

2.1. ASSESSMENT CRITERIA

Our assessment criteria are as follows:

1. **Methodological coherence:** Are unit rates calibrated on the same basis as they are applied in the mechanism, i.e., do they reflect efficient costs on a £ per service addition basis (the unit on which the LVSVD pays)?
2. **Cost reflectivity and incentives for cost efficiency:** Do the unit rates reflect efficient delivery costs likely to be incurred, while providing appropriate efficiency pressure (i.e., stretching but achievable)?
3. **Delivery incentives and volume efficiency:** Does the approach encourage delivery of the right activities and volumes (including proactive work), avoiding systematic under-delivery and/or inefficient over-delivery?
4. **Evidence quality and proportionality:** Is the approach evidence-based and replicable using available data, transparent to stakeholders, and proportionate to implement?

These criteria reflect Ofgem's objectives for the unit cost drivers at the ED2 Final Determination stage, ensure consistency with Ofgem's ED3 documentation to date, and facilitate differentiation between the options. Setting out the criteria upfront provides a structured and transparent appraisal framework and provides an audit trail showing how evidence and judgement have been applied in arriving at our recommendation.

2.2. DESCRIPTION OF OPTIONS

2.2.1. Shortlisted options

We agreed with Ofgem to assess four shortlisted options:

Option	Description
(1) Use current unit rates	Maintain the existing ED2 unit rates for OHL and UG services (i.e. no recalculation or updates).
(2) Use rates based on updated methodology, applied to costs in ED2 business plan	Apply the ED2 methodology on a consistent per-addition basis, by removing the volume-doubling treatment for ENWL and NGED (which was applied by Ofgem at ED2).
(3) Use rates based on updated methodology and ED2 outturn data	As in Option 2, remove the ENWL/NGED volume-doubling treatment; plus update unit rates for ED2 Years 4-5 based on ED2 Years 1-2 outturn costs and volumes as reported by DNOs in the 2025 RRP ¹² .
(4) Use DNO forecast rates	As in Option 2, remove the ENWL/NGED volume-doubling treatment; plus update unit rates for ED2 Years 4-5 based on DNOs' forecast unit cost data for those years, where available.

¹² This includes making further cost and volume adjustments for NGED. NGED's OHL unit costs for EMID, SWALES and SWEST in its outturn submission dated 19 November 2025 were materially higher than those reported by other DNOs and were treated as outliers. Following an Ofgem information request, NGED confirmed this issue and, in its response dated 14 January 2026, explained that a project cost review identified that some unlooping project work had been reported against LV Service (OHL) reinforcement but should instead have been reported against other activities in table CV2. We have implemented the cost and volume reallocations described by NGED in that response; as a result, the recalculated unit costs and the industry median benchmark used under Option 3 (ED2 outturn-based rate) differ from those implied by the November 2025 submission.



Each option is deliberately simple and distinct. In principle, hybrid approaches could also be considered, e.g., triangulating between Option 2 (ED2 forecast-based evidence with an updated methodology) and Option 3 (outturn-based evidence), recognising that each data source has different strengths and weaknesses. However, for this assessment we have prioritised a simple, transparent comparison, consistent with discussions with Ofgem.

2.2.2. Options discounted

Ofgem's focus for this mid-period review is on proportionate changes required to update the LVSVD unit rates for ED2 Years 4-5. Therefore, this section summarises the main options raised by DNOs that fall outside of the scope set by Ofgem for this unit rate update, which is why we do not take them forward for full assessment.

Company-specific unit rates (rather than an industry benchmark/median). Some DNOs have suggested using company-specific unit rates instead of a common benchmark. The rationale for this is that the resulting unit rates would better reflect company-specific delivery approaches. However, moving to company-specific rates would represent a material change to the mechanism design, moving away from ED2's use of an industry median benchmark to provide a common basis for funding and efficiency incentives.¹³

Separate unit rates for different types of activity (e.g. proactive versus reactive). To ensure consistency with Ofgem's ED2 methodology, we do not consider separate unit rates for proactive and reactive work.¹⁴

Separate unit rates for different engineering solutions. DNOs have suggested disaggregating unit rates to reflect differences in the nature of the work delivered (for example, where 3-phase services are not directly comparable to standard services). To ensure consistency with Ofgem's ED2 methodology, we do not consider this option. It would also require additional (more granular) data to reliably set unit rates in this way.

2.3. UNIT RATES UNDER DIFFERENT OPTIONS

Table 2.1 and **Error! Reference source not found.** present the resulting unit costs for each DNO alongside the median benchmark rate for OHL and UG respectively.

For Options 1-3, we calculate the implied unit costs using Ofgem's disaggregated model (CV2 sub-model for LV service reinforcement), based on DNO costs and volumes reported in the 2025 RRP (see Footnote 9). We do not present forecast-based unit costs (Option 4) because not all DNOs responded to the RFI, meaning a robust benchmark cannot be derived.

¹³ Benchmarking to an industry median is a well-established feature of Ofgem price controls and has been applied in RIIO-ED2 to calibrate unit cost benchmarks across a number of activity categories. (See Ofgem RIIO-ED2 Final Determinations Core Methodology Document.) The RIIO-ED2 documentation contains limited LV-services-specific discussion of the rationale for the median benchmark, although it does not appear to have been a key point of debate in consultation.

¹⁴ Ofgem RIIO-ED2 Draft Determinations Core Methodology Section 3.69.

Table 2.1: Comparison of OHL unit costs by option (£k, 2020/21 prices) - * individual unit costs are redacted

Company	(Option 1) Current UC	(Option 2) Updated methodology UC	(Option 3) ED2 outturn UC
ENWL			
NPGN			
NPGY			
WMID			
EMID			
SWALES			
SWEST			
LPN			
SPN			
EPN			
SPD			
SPMW			
SSEH			
SSES			
Median	0.35	0.44	1.44

Table 2.2: Comparison of UG unit costs by option (£k, 2020/21 prices) – *individual unit costs are redacted

Company	(Option 1) Current UC	(Option 2) Updated methodology UC	(Option 3) ED2 outturn UC
ENWL			
NPGN			
NPGY			
WMID			
EMID			
SWALES			
SWEST			
LPN			
SPN			
EPN			
SPD			
SPMW			
SSEH			
SSES			
Median	1.60	2.21	2.65



Source: CEPA analysis of DNO data.

Unit costs vary across the options both at company level and for the industry median benchmark.

For OHL services (left hand panel, above), removing the volume adjustment (going from Option 1 to 2) only results in a modest increase in the median unit cost, from £0.35k to £0.44k per addition. By contrast, estimating unit costs using ED2 Y1-Y2 outturn data (Option 3) increases the median to £1.44k, i.e. more than a threefold uplift relative to the updated methodology rate. The pattern is consistent with the narrative in DNO RFI responses, which indicated that LV service delivery has required additional works relative to FD assumptions. This points to a material gap in cost reflectivity if current rates are retained (i.e. under Options 1 or 2).

For UG services, the methodological choice has a larger absolute impact than for OHL services, but a smaller proportional impact. Removing the volume adjustment (from Option 1 to 2) increases the median unit cost from £1.60k to £2.21k. Using ED2 outturn data (Option 3) increases it further to £2.65k. Unlike OHL, the company-level movements are mixed: several DNOs show lower actual unit costs in Y1–Y2 (Option 3) than the corrected forecast (Option 2) – notably ENWL, WMID, EMID and SWEST – while other DNOs show higher actuals under Option 3. The increase in the median in Option 3 is driven primarily by upward movements among companies around the middle of the distribution.

Box 2: Materiality of unit cost differences

The increase from Option 1 to Option 3 is proportionally much larger for OHL than for UG, suggesting the current OHL rate may be less cost reflective. However, the implications for overall cost recovery are limited for OHL – in comparison to UG – because OHL volumes are very small relative to UG. For UG, the difference between Options 1 and 3 is smaller in unit-cost terms, but it has a much larger impact on total cost recovery, because UG volumes are high.

ENA¹⁵ analysis indicates that, under current unit rates, under-recovery is around £1m for OHL and around £23m for UG across the first two years of ED2. This illustrates that higher-volume activities can drive the majority of overall under-recovery even where the unit cost gap is relatively modest; whereas low-volume activities can show large percentage gaps with only limited impact in £ terms.

Note: Figures compare cost recovery against reported outturn costs and do not assess cost efficiency.

In Appendix A, we compare the ex-ante allowance to the magnitude of the total cost changes under these options.

2.4. ASSESSMENT OF SHORTLISTED OPTIONS

Each option is assessed below against the criteria set out in Section 2.1. Our assessment is illustrated using a RAG-rating: A red cross indicates the option is unlikely to meet the criterion; an amber triangle indicates it partially meets the criterion; and a green symbol indicates it is likely to meet the criterion.

2.4.1. Option 1: Maintain current rate

The simplest option is to maintain the current unit rates for OHL and UG. Our assessment of this option is set out in Table 2.3 below.

Table 2.3: Assessment of Option 1: Maintain current rate

Criteria	RAG	Rationale
Methodological coherence		<ul style="list-style-type: none"> Retains the existing unit rates, including the volume adjustment. The rate is effectively calculated on a property-unlooped basis while funding is applied on an additions basis.

¹⁵ Referenced in Ofgem’s presentation: Load Related Expenditure Volume Drivers Review, 15th December 2025.

Criteria	RAG	Rationale
Cost reflectivity and incentives for cost efficiency		<ul style="list-style-type: none"> • Rates were set based on forecast data, without a strong substantial evidence base (such as a long time series of historical data). Early ED2 evidence suggests outturn unit costs are materially above the current rates. • A lower unit rate could, in principle, strengthen incentives for cost efficiency. However, if the unit rate is set materially below efficient costs it might become unrealistic and would be unlikely to incentivise companies effectively or drive genuine cost efficiency.
Delivery incentives and volume efficiency		<ul style="list-style-type: none"> • High risk of under-delivery, particularly for proactive works, if the rate under-recovers actual costs incurred. • For both OHL and UG, current rates are below median DNO reported ED2 actual costs for proactive volumes.
Evidence quality and proportionality		<ul style="list-style-type: none"> • Proportionate and straightforward to implement. • Unit rates were based on DNO information submission in advance of ED2, but this option does not reflect the latest evidence.

Option 1 offers no benefits beyond stability and ease of implementation. It contains a methodological inconsistency which artificially reduces the unit rate. In addition, it utilises a dataset based on forecasts for ED2 – rather than having a substantial evidence base from historical data – which creates further risks to its cost reflectivity.

The key incentive risk is that, if the unit rate is materially below efficient cost – which is a risk, as per DNO reported costs in ED2 to date – the unit rate ceases to provide a genuine cost efficiency incentive and instead creates a loss-making price for the activity. In this scenario, additional delivery wors

ens financial performance, so the dominant incentives are to reduce or defer volumes, prioritise only unavoidable work, reduce the quality of works, and potentially distort recording or timing, rather than drive genuine efficiency improvements. Low volumes will hinder the ability for DNO's to support delivery of net-zero.

2.4.2. Option 2: Use updated methodology rate

This option removes the volume adjustment applied by Ofgem to ENWL's and NGED's unit costs for OHL and UG services when setting the ED2 unit cost allowances. As a result, unit costs are calculated on a consistent per-addition basis across all companies, aligned with the basis of the unit rate on which DNOs are funded. Our assessment of this option is set out in Table 2.4 below.

Table 2.4: Assessment of Option 2: Use updated methodology rate

Criteria	RAG	Rationale
Methodological coherence		<ul style="list-style-type: none"> • Corrects for inconsistency in original unit rates. • Applies a consistent per-addition basis for OHL and UG.
Cost reflectivity and incentives for cost efficiency		<ul style="list-style-type: none"> • More cost reflective than Option 1 because it removes distortion. However, it does not leverage most recent data from ED2 to date, so may not capture additional works now observed in ED2. • May incentivise cost efficiency.
Delivery incentives and volume efficiency		<ul style="list-style-type: none"> • Reduces the risk of under-delivery versus Option 1. • If the rate is still below efficient cost, incentives may still favour deferral of activity and lower volumes.
Evidence quality and proportionality		<ul style="list-style-type: none"> • Simple and proportionate to implement. • While ED unit cost allowances are based on the forecast volumes for ED2, this option does not reflect the latest available outturn evidence from ED2.

Option 2 is an improvement on maintaining current unit cost allowances (Option 1), as it corrects the identified methodological inconsistency and restores a consistent per-addition basis. For UG services, the updated methodology rate appears broadly in line with ED2 Y1–Y2 outturn unit costs and, in principle, could encourage cost efficiency.

However, for OHL services the updated methodology unit rate remains materially below ED2 outturn unit costs (around three times lower). If that cost data is representative of underlying costs, it suggests that the rate (Option 2) is unlikely to be cost reflective and, in turn, creates an under-delivery risk. In particular, if the unit rate under-recovers efficient costs, DNOs may rationally prioritise only unavoidable delivery and defer discretionary activity, with the greatest risk falling on proactive works. This risk is consistent with observed ED2 delivery patterns, where several DNOs report limited or no proactive volumes.

2.4.3. Option 3: Use ED2 outturn rate

This option estimates unit costs using ED2 outturn data for Years 1-2, and, consistent with Option 2, does not apply the volume doubling adjustment for ENWL and NGED. Our assessment of this option is set out in Table 2.5 below.

Table 2.5: Assessment of Option 3: Use ED2 outturn rate

Criteria	RAG	Rationale
Methodological coherence		<ul style="list-style-type: none"> Resolves the inconsistency embedded in the original unit rate derivation. Applies a consistent, per-addition basis across OHL and UG.
Cost reflectivity and incentives for cost efficiency		<ul style="list-style-type: none"> Cost reflective of activity to date in ED2, as data is grounded in actual ED2 costs incurred by DNOs. However, actual volumes in ED2 to date are not guaranteed to be fully representative of future volumes. E.g. For OHL, the sample size is relatively small, due to low levels of activity to date (total ED2 spend of less than ~£1.5m across all DNOs). May reduce cost efficiency pressure if outturns include inefficiency or atypical one-offs.
Delivery incentives and volume efficiency		<ul style="list-style-type: none"> Reduces under-delivery risk: a higher unit rate reduces the incentive to defer LV services volumes, particularly proactive works.
Evidence quality and proportionality		<ul style="list-style-type: none"> Simple and proportionate to implement, although requires quality assurance on data. It is based on the most recent evidence, although estimated from two years of data with relatively low volumes (particularly for OHL).

Option 3 uses realised ED2 costs to calibrate the unit rates, thereby reflecting additional work that was not fully captured in the FD assumptions. This improves cost reflectivity and, in turn, mitigates one of the principal risks identified in this review: that a lower unit rate discourages delivery, particularly of proactive activity. Implementation is also relatively practical. However, it is contingent on appropriate quality assurance of DNOs' cost data submissions. For example, NGED's unit cost data (included in the DNOs' November 2025 RFI submissions) contained material outliers that were subsequently corrected.

DNOs' submitted ED2 outturn costs (Option 3) are a more reliable measure of the unit costs of volumes to date during ED2, compared to Options 1 and 2 which are based on forecasts originally used for the ED2 allowance. However, there may be limitations as to whether ED2 outturn volumes and costs (Option 3) will be representative of volumes and costs over the remainder of ED2. For example, UKPN's RFI submission suggests that caution should be applied when considering DNO reported unit costs for OHL, given "low levels of activity in this area" in ED2 to date.¹⁶

2.4.4. Option 4: Use DNO forecast rates

This option would set unit rates for ED2 Years 4-5 using updated forecast unit costs from DNOs. The DNO groups that responded to the November 2025 RFI (SSEN, UKPN and SPEN) provided forecast unit costs for their expected Y3-Y5 delivery, as summarised in Box 3 below. In some cases, these forecasts are informed by ED2 Years 1-2 outturn evidence, similar to Option 3. Some of the DNOs proposed methodologies that are outside the scope of our analysis, e.g. proposals for company-specific unit rates, rather than using the industry-wide median.

¹⁶ For example, see UKPN's RFI1 commentary, p5. For OHL, DNOs were funded ex ante for around 2,500 additions across the first two years of ED2, whereas outturn volumes over Years 1-2 were around 50% lower.

Box 3: DNO forecast approaches

- **SEEN:** Proposes updated unit rates largely based on its Year 1–2 outturns. However, it argues against applying a simple industry median, noting that costs vary by licence area due to factors such as delivery maturity, geography and local markets.
- **UKPN:** Bases proposed unit costs on 2025/26 year-to-date internal reporting (Apr-Oct 2025). It annualises Year 3 volumes and then derives Years 4–5 volumes by applying the change between the July Price Control Financial Model (PCFM) volumes and the annualised 2025/26 forecast to produce updated Y3-Y5 volume forecasts.
- **SPEN:** For UG services, proposes that, where it delivers 3-phase as standard, unit rates should be calibrated to SPEN outturn costs. For other categories, SPEN references the industry median Year 1–2 outturn unit cost.

Our assessment of this option is set out in Table 2.6 below.

Table 2.6: Assessment of Option 4: Use DNO forecast rates

Criteria	RAG	Rationale
Methodological coherence		<ul style="list-style-type: none"> • Removes the identified volume-adjustment inconsistency. • Forecasts are not prepared on a consistent basis across DNOs.
Cost reflectivity and incentives for cost efficiency		<ul style="list-style-type: none"> • Forecasts may incorporate company-specific forward-looking information, which may improve cost reflectivity. • Provide limited cost-efficiency incentive, since DNOs may not propose stretching unit rates for themselves.
Delivery incentives and volume efficiency		<ul style="list-style-type: none"> • Less likely to discourage delivery, particularly regarding proactive volumes, compared to options with lower unit rates (e.g. Option 1). • There might be a risk of over-incentivising delivery if rates are too high.
Evidence quality and proportionality		<ul style="list-style-type: none"> • Forecast assumptions and derived unit costs (Option 4) are not evidenced in sufficient detail to demonstrate they are more appropriate than an outturn-based approach (Option 3). • Not all DNOs provided forecasts, which limits comparability and makes a robust benchmark difficult. • Given this is a mid-period review, a full reconciliation of forecast methodologies and assumptions across DNOs would not be proportionate.

We recognise that DNOs are best placed to understand the costs and volumes they expect to incur in ED2 Years 3–5. However, taken as a whole, the evidence provided does not demonstrate that company forecasts would deliver a more robust or cost-reflective benchmark than calibrating rates using available ED2 forecast or outturn data. Forecasts have been prepared using different approaches and assumptions across respondents, and DNOs have limited incentive to propose unit rates that embed stretching cost efficiency.

There are also implementation concerns. Not all DNOs provided forecast information, preventing the derivation of a robust, comprehensive benchmark from existing data. A full reconciliation of forecast methodologies, scope and assumptions would be resource intensive for both Ofgem and the DNOs. Given this is a mid-period review, requiring all DNOs to develop, evidence and align forecasts to a consistent standard, and then subjecting these to comprehensive review, would not be proportionate.

2.4.5. Summary of assessment

The table below summarises our RAG assessment across the shortlisted options.

Table 2.7: Summary of assessment

Criteria	Option 1: Current rate	Option 2: Updated methodology rate	Option 3: ED2 outturn rate	Option 4: DNO forecast rate
Methodological coherence				
Cost reflectivity and incentives for cost efficiency				
Delivery incentives and volume efficiency				
Evidence quality and proportionality				

Source: CEPA analysis

Considering the different options, our view is that – as a minimum – Option 1 should not be taken forward, due to the methodological inconsistency, i.e. unit rates should be set on a basis that is consistent with the data used to calculate DNOs' unit costs. Option 4 does not provide a comprehensive, robust evidence base across DNOs.

There may be advantages to Ofgem 3 (using the ED2 outturn-based unit rate), because it is based on outturn data for ED2, whereas Option 2 would still rely on DNOs' forecast cost data. However, in choosing between Options 2 and 3, there are several key questions to consider.

First, which set of cost data is most likely to be representative of volumes over the remainder of ED2?

Option 3 has the advantage of being outturn data. However, it is not certain to precisely reflect future unit costs: The DNOs' submitted costs are based on relatively low volumes (especially for OHL), there has been a higher-than-forecast proportion of reactive volumes (which are higher cost than proactive work), and outliers have been identified within initial datasets.

Second, how would Ofgem balance the different risks under Options 2 and 3?

Under Option 2, the modest increase in unit rates risks a continuation of under-delivery on proactive volumes, which could inhibit Ofgem's objectives to support LCT uptake. On the other hand, if the rates under Option 3 were slightly too high (due to some of the reasons discussed above), that would pass risks to consumers through higher bills. If volumes during the remainder of ED2 follow a similar profile to ED2 to date (Y1-2), Option 3 would increase DNOs' allowed revenue by £30m relative to Option 2 (i.e. £256m in Option 3, compared to £226m in Option 2, as set out in Figure A.1 in Appendix A).

Our view is that Ofgem should use the consultation to seek further evidence on the relative 'reliability' of the existing datasets, considering both current ED2 forecasts (used in Option 2) with ED2 outturn data (Option 3). Based on the set of data currently available, Option 3 (based on ED2 outturn data) might have the most robust evidence base to set unit rates, because it is grounded in observed cost data. However, as noted above, Ofgem will need to consider which set of cost data is most likely to be representative of volumes over the remainder of ED2. Therefore, we recommend that Ofgem seeks further evidence and assurance, as discussed in the following section.

Once further information and evidence is obtained, Ofgem may be in a position to consider the merits of hybrid options, for example, by triangulating between Options 2 and 3.

2.4.6. Priorities for Ofgem's mid-period review

As noted above, the key judgement between Options – particularly between Options 2 and 3 – is which is more likely to reflect efficient unit costs for ED2 Years 4–5. Whilst Option 3 is grounded in observed data for ED2 delivery – and may help to mitigate the any risks of under-delivery of LV services across ED2 – further assurance on the reliability of outturn unit cost data is merited.

Therefore, in Ofgem's consultation and ahead of the decision, our recommendation is that Ofgem seeks additional evidence as follows:

- To request further quality assurance on the data submitted. Further assurance from DNOs on their cost allocation methodology can ensure greater confidence and mitigate the risk of any outliers skewing the median unit cost. Quality assurance by DNOs can also identify whether there are any temporary effects (or 'one-off' factors) within the ED2 outturn data that might reduce their which might make Years 1–2 not fully representative of efficient steady-state unit costs during the remainder of ED2.
- To increase the supporting narrative in relation to ED2 outturn costs and volumes. This could include evidence to support an explanation of what has been driving higher outturn costs relative to the current unit rates.
- To review the mix of reactive and proactive delivery in outturn data compared to during the remainder of ED2. Reactive interventions are typically more expensive than proactive works due to site-specific complexity, whereas proactive programmes can often be planned and standardised. If ED2 delivery to date is weighted towards reactive activity¹⁷ (as some DNOs report limited proactive programmes), this may increase the outturn-based unit cost (Option 3). That, in turn, can affect incentives for the remainder of ED2: a higher unit rate may reduce the risk that proactive volumes are deferred due to under-recovery, but it may also reduce the incentive to move delivery towards lower-cost proactive interventions if the unit rate is driven by a more expensive reactive mix.

¹⁷ The drivers of lower-than-forecast proactive activity to date in ED2 are not definitive. It may reflect a rational operational response to unit rates perceived as under-recovering efficient costs, with DNOs prioritising only essential customer-initiated reactive reinforcement and deferring proactive activity. It is also possible that the prospect of a mid-period review influenced delivery timing, which could have brought forward some higher-cost interventions and delayed some lower-cost activity.

3. CONSIDERATIONS AHEAD OF ED3

If a similar volume-driver approach is retained in ED3, there are broader design questions that go beyond what is proportionate for an ED2 mid-period update. These questions are outside the scope of this review. However, we have collated them here in case they are of use to Ofgem in its wider thinking as it develops its proposals for ED3. Ofgem will need to decide how far the mechanism should seek to address heterogeneity and non-comparability across DNOs, and how to balance cost reflectivity against simplicity.

Optimising the volume driver to ensure DNOs are reimbursed for efficient costs. DNOs may be unlooping different numbers of properties ‘per service addition’, and if so, a unit cost based on service additions may under-reward some DNOs and over-reward others.¹⁸ An alternative could be to set costs based on the number of properties unlooped – or even potentially a more complex ‘hybrid’ driver which takes into account both the number of interventions and the number of properties unlooped. However, costs may not increase linearly with the number of properties unlooped, due to the potential for fixed costs per intervention (e.g. mobilisation, traffic management, site set-up), so there are likely to be pros and cons to different drivers.

In advance of ED3, Ofgem could further investigate the relationship between the number of interventions, the number of properties unlooped (per intervention), and costs. If the unit-rate derivation is standardised on a per-property basis, then, conceptually, funding would also need to be tied to the same volume definition (e.g. properties unlooped rather than additions) to avoid the type of denominator mismatch observed in ED2.

Other sources of non-comparability. Beyond properties-unlooped assumptions, there are other factors that may drive systematic differences in reported unit costs across DNOs. These include differences in the mix of reactive versus proactive delivery (with reactive works typically higher-cost due to site-specific complexity), and differences in the nature of engineering solutions delivered (for example, where 3-phase service upgrades are not directly comparable to standard services, or where other “non-standard” solutions are deployed). For ED3, Ofgem could consider whether to account for these factors explicitly (e.g. through disaggregated reporting and separate unit rates) or to retain a simpler single-rate approach.

Benchmarking approach: industry median versus company-specific rates. A further strategic choice is whether unit rates should continue to be set using an industry benchmark (e.g. the median) or move towards more company-specific calibration. Median benchmarking provides a common funding basis and can strengthen comparative efficiency incentives, but may be less cost-reflective where legitimate cost differences are not captured in the unit definition. Conversely, company-specific rates can better reflect genuine differences in delivery context or outputs, but weaken comparative efficiency pressure and increase the risk that inefficient costs are funded and passed through to consumers. Ofgem’s ED3 design will therefore need to balance several factors: the potential for standardisation and simplicity; the incentive strength it wants the mechanism to provide; data and assurance requirements needed to support a more granular approach; and ensuring proportionality by considering the materiality of financial impacts under different options.

¹⁸ This provides the rationale for Ofgem’s ‘volume adjustment’ (for deriving ED2 unit rates), as it was intended to improve comparability across DNOs where business plan forecasts implied different relationships between an LV service intervention (“addition”) and the number of properties unlooped (e.g. 1:2 versus 1:1).

Appendix A Impact on Allowed Expenditure

This appendix considers the impact on DNOs' allowed expenditure of changing the methodology used to set unit rates, which impacts both DNO cost recovery and costs to consumers.

This appendix utilises Option 3, given it is grounded in ED2 outturn data for Y1-2, although our analysis sets out that further work is required to substantiate the evidence base and obtain assurance that ED2 outturn costs for Y1-2 are likely to be representative of unit costs incurred for volumes over the remainder of ED2.

If Ofgem were to adopt Option 3 (use the ED2 outturn rate), the median unit cost for ED2 Years 4-5 would increase from £0.35k to £1.44k for OHL services and from £1.60k to £2.65k for UG services. This represents a material uplift relative to the unit rates set at ED2 Final Determinations, especially for OHL services.

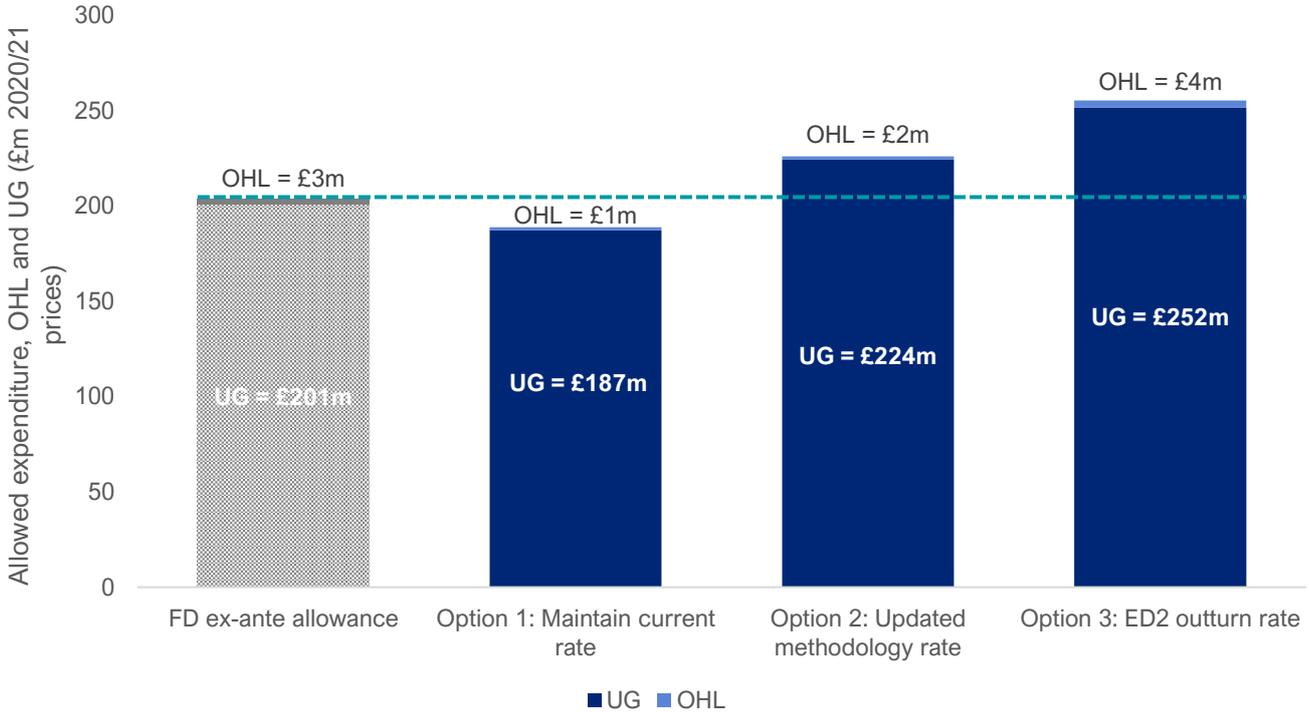
Error! Reference source not found. illustrates the indicative impact of the updated unit rates on total ED2 allowed expenditure for LV Services OHL and UG additions, aggregated across all DNOs and across proactive and reactive reinforcement. Values are shown in £m (2020/21 prices). Because UG additions have both higher volumes and higher unit rates than OHL additions, the resulting allowed expenditure is dominated by UG.

The ED2 total is constructed by applying the existing ED2 unit rates to Years 1–2 outturn volumes and to an assumed set of Year 3 volumes, and applying the option-specific unit rates to assumed Years 4–5 volumes. This is consistent with the Ofgem guidance that unit-rate updates would apply only in the remainder of ED2. Volumes for Years 3–5 are estimated by scaling implied Final Determinations volumes¹⁹ using an adjustment factor, based on the average outturn-to-FD volume ratio observed in Years 1–2. The results are therefore illustrative: actual Years 3–5 volumes (and hence allowed expenditure) may differ from the assumptions used here. Given the uncertainty around volumes for Years 3-5, we have also modelled some sensitivities (volume scenarios) further below.

¹⁹ At final determinations, Ofgem set an ex-ante allowance for UG and OHL LV services based on a combination of the disaggregated model and the totex model. This allowance is then divided by the allowed unit rate to derive an 'implied volume' i.e., the level of activity the DNO is funded to deliver, assuming delivery at the allowed unit rate. These implied volumes are distinct from the DNOs' submitted forecast volumes for ED2.



Figure A.1: Forecast impact of unit cost options on allowed expenditure for OHL and UG (ED2 total; £m 2020/21 prices)



Source: CEPA analysis of DNO data. Years 1–2 use ED2 outturn volumes and ED2 Final Determinations unit rates. Year 3 uses the current (FD) unit rate. Volumes for Years 3–5 are estimated by scaling implied Final Determinations volumes using an adjustment factor based on the average outturn-to-FD volume ratio observed in Years 1–2 (see Scenario 2 below). Unit rates for Years 4–5 vary by option.

Under Option 1 (maintain current rates), indicative total allowed expenditure for UG+OHL over ED2 is around £190m. This is below the FD ex ante allowance due to lower-than-expected volumes during ED2 to date. Under Option 2 (updated methodology rate), total allowed expenditure increases to around £225m (an uplift of roughly £35m relative to Option 1). Under Option 3 (ED2 outturn-based rate), the total rises to around £255m, an increase of roughly £65m relative to Option 1. The increase in costs under Options 2 and 3 is due to the increase in unit rates, applied in Years 4 and 5. Across all three options, OHL contributes only a small share (around 1–2%) of the combined UG+OHL total.

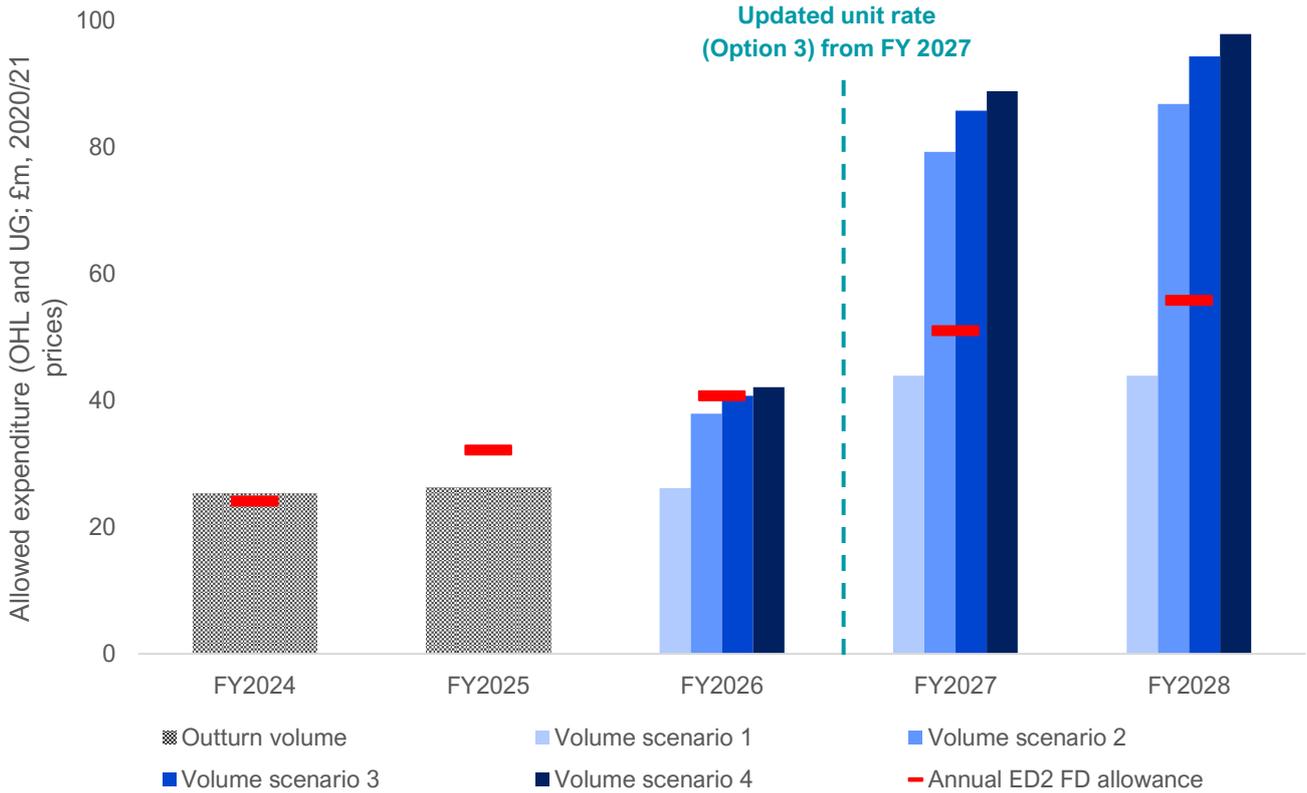
We also test the sensitivity of allowed expenditure in Years 3–5 to alternative volume assumptions, using Option 3 (unit rate derived from ED2 outturn data). We plot these against the notional ex-ante allowed expenditure set at Final Determinations. The volume scenarios are:

- **Scenario 1:** Years 3–5 volumes set equal to the latest outturn volumes, i.e., as per Year 2.
- **Scenario 2:** Years 3–5 volumes are based on the implied forecast volumes used for the ED2 Final Determinations, scaled by an adjustment factor reflecting the industry-level average difference between FD-implied volumes and outturn in Years 1–2, calculated as: $avg(\frac{outturn\ volume\ Y1}{implied\ FD\ volume\ Y1}, \frac{outturn\ volume\ Y2}{implied\ FD\ volume\ Y2})$. This approach is used in **Error! Reference source not found.** above.
- **Scenario 3:** Years 3–5 volumes set equal to the implied forecast volumes used for the ED2 Final Determinations.
- **Scenario 4:** Years A-5 volumes ‘catch-up’ such that the total ED2 volumes are the same as the total implied forecast volumes (over the whole of the ED2 period) used in the Final Determinations.



In Figure A.2, the red markers show the annual ex-ante allowance for OHL and UG additions set at Final Determinations. For ED2 Years 1–2, the grey bars show allowed expenditure calculated using existing ED2 unit rates, applied to outturn volumes. The blue bars show allowed expenditure under the four alternative volume scenarios (discussed above) for Years 3–5. In Year 3, allowed expenditure is calculated using the existing ED2 unit rates (as any update to unit rates would only apply from Year 4). In Years 4–5, allowed expenditure is calculated using Option 3 (the ED2 outturn-based unit rate), which is applied to the four different volume scenarios.

Figure A.2: Impact of volume scenarios on annual allowed expenditure for OHL and UG (Option 3: ED2 outturn-based rate; £m, 2020/21 prices)



Source: CEPA analysis of DNO data. FY2024–FY2025 (grey bars) show allowed expenditure calculated using ED2 Final Determinations unit rates applied to outturn volumes. FY2026 shows allowed expenditure using ED2 Final Determinations unit rates under the alternative volume scenarios. FY2027–FY2028 show allowed expenditure under the updated unit rate (Option 3) under the same Years 3–5 volume scenarios.

For Years 4-5, applying the outturn-based unit rate (Option 3) increases implied allowed expenditure relative to the ED2 FD allowance in three of the four volume scenarios. Only if volumes remain depressed at FY2025 levels (Scenario 1) does allowed expenditure remain below the FD ex-ante allowance. Under higher-volume scenarios, allowed expenditure exceeds the ex-ante allowance.

The different volume scenarios reflect the ED2 forecast volume profile and outturn volumes from ED2 Years 1-2. First, ED2 volumes were forecast to increase over time, so holding volumes constant across Years 3-5 based on Year 2 outturn (Scenario 1) would result in the lowest forecast allowance. Second, outturn volumes for ED2 Year 1-2 were slightly below forecast: UG outturn volumes (which are significantly more material than OHL) were around 18% below forecast in 2025.²⁰ Scenario 2 is designed to (proportionately) roll forward the observed under-delivery

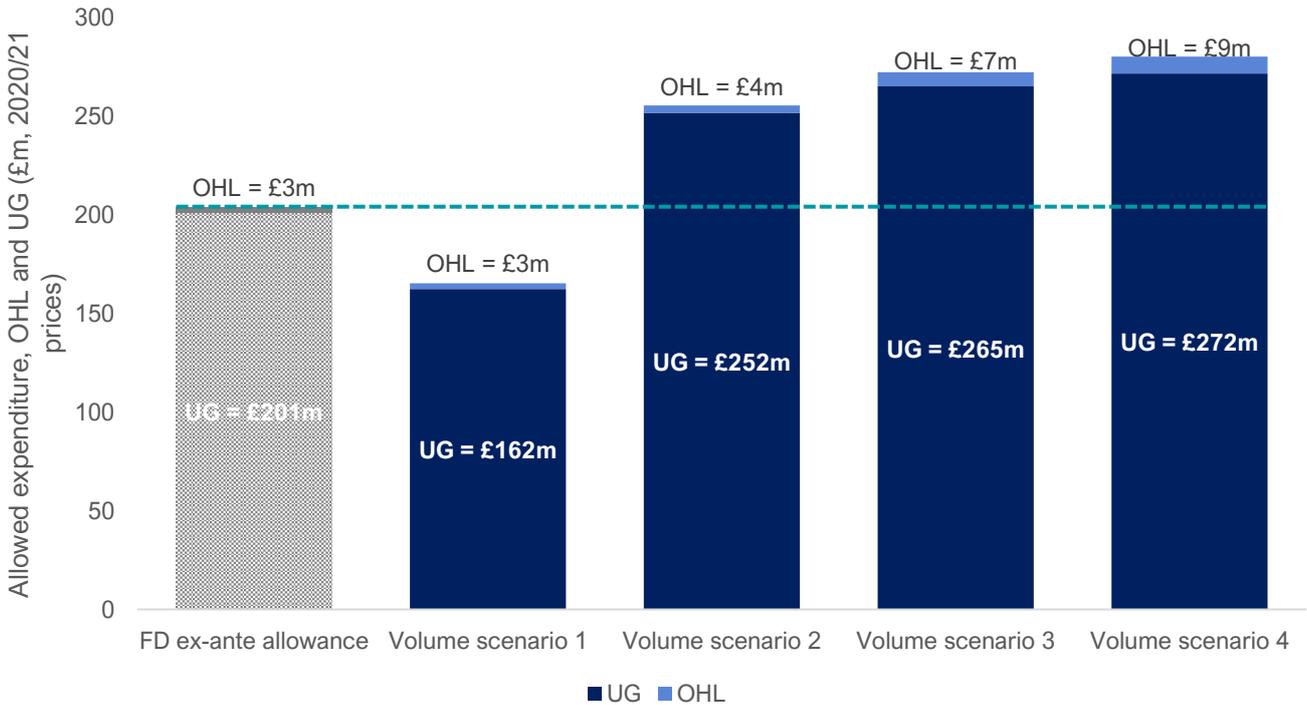
²⁰ OHL outturn volumes were also below ED2 forecasts in Years 1 and 2 (by 61% and 44%, respectively). However, OHL additions are a low-volume activity and therefore have only a limited impact on the overall expenditure profile.



from Year 1-2 to Years 3-5, whereas Scenarios 3 and 4 do not have this feature, so Scenarios 3 and 4 forecast higher allowed revenues than Scenario 2.

To illustrate the overall impact across ED2, we sum the annual values (in Figure A.2) to derive the ED2 totals. Figure A.3 presents total allowed expenditure over ED2 under each volume scenario, including the split between OHL and UG, if ED2 outturn-based unit rates are implemented (Option 3) for Years 4-5.

Figure A.3: Impact of volume scenarios on total ED2 allowed expenditure for OHL and UG (Option 3: ED2 outturn-based rate; £m, 2020/21 prices)



Source: CEPA analysis of DNO data.

If Option 3 (ED2 outturn unit rates) is implemented, under volume Scenario 1 (where volumes in Year 3-5 are set equal to Year 2 outturn volumes), total allowed expenditure remains below the FD ex-ante allowance. Under Scenarios 2, 3 and 4, allowed expenditure is higher than the FD allowance. The highest-volume scenario (Scenario 4, where volumes ‘catch up’ to ED2 forecast levels) results in allowed expenditure around £75m higher than the FD allowance. All of these figures assume the implementation of Option 3 unit rates in Years 4–5.

Below, Tables A.1–A.3 illustrate the impact of the different unit rate options for each licensee. Across unit rate Options 1, 2 and 3, the tables present ED2 total allowed expenditure, assuming Volume Scenario 2, which is the same volume scenario used in Figure A.1 above. The allowed expenditure figures for each DNO are indicative, because they depend upon the assumed volumes for the remaining years of ED2.²¹

²¹ The tables report ED2 totals. Options 1, 2 and 3 use a common volume assumption (Scenario 2). Across Options 1, 2 and 3, allowed expenditure for Years 1-3 remains the same for each DNO, whereas there is variation in allowed expenditure during Years 4-5, based on the unit rate applied under each Option. Across the Options, the proportionate change in total ED2 allowed expenditure can differ between DNOs because each licensee has a different volume profile across ED2 (and therefore a different ratio of volumes in Years 1-3 versus Years 4-5).

Table A.1. ED2 allowed expenditure for OHL under Volume Scenario 2 by licensee (£m, 2020/21 prices)

Allowed expenditure, £m	Ex-ante allowance	Option 1	Option 2	Option 3
ENWL	-	0.01	0.01	0.01
NPGN	-	-	-	-
NPGY	-	-	-	-
WMID	0.02	0.02	0.02	0.04
EMID	0.02	0.01	0.01	0.02
SWALES	0.01	0.01	0.01	0.02
SWEST	0.01	0.02	0.02	0.02
LPN	-	-	-	-
SPN	1.29	0.57	0.64	1.52
EPN	1.45	0.64	0.73	1.78
SPD	-	0.00	0.00	0.00
SPMW	-	0.08	0.08	0.08
SSEH	0.03	0.01	0.01	0.02
SSES	0.11	0.05	0.06	0.12
Total	2.94	1.42	1.60	3.64

Source: CEPA analysis of DNO data. Volume scenario 2 is assumed for ED2 years 3-5. The unit rate is updated for ED2 years 4-5. Dashes indicate that the relevant DNO reported zero volumes for that activity in the underlying data, so a unit cost cannot be calculated.

Table A.2. ED2 allowed expenditure for UG under Volume Scenario 2 by licensee (£m, 2020/21 prices)

Allowed expenditure, £m	Ex-ante allowance	Option 1	Option 2	Option 3
ENWL	13.48	15.32	18.08	20.11
NPGN	21.30	22.54	27.29	30.81
NPGY	36.08	32.62	40.93	47.08
WMID	17.61	12.73	15.30	17.21
EMID	19.73	13.63	16.61	18.81
SWALES	6.12	5.45	6.54	7.34
SWEST	8.65	6.71	8.16	9.23
LPN	3.40	2.58	3.24	3.73
SPN	3.28	4.06	4.62	5.04
EPN	3.70	3.44	4.12	4.61
SPD	34.68	35.50	41.59	46.09
SPMW	19.92	24.88	28.34	30.91
SSEH	5.17	2.71	3.30	3.73
SSES	7.76	5.18	6.25	7.04
Total	200.89	187.36	224.37	251.75

Source: CEPA analysis of DNO data. Volume scenario 2 is assumed for ED2 Years 3-5. The unit rate is updated for ED2 years 4-5.

Table A.3. ED2 allowed expenditure for OHL and UG under Volume Scenario 2 by licensee (£m, 2020/21 prices)

Allowed expenditure, £m	Ex-ante allowance	Option 1	Option 2	Option 3
ENWL	13.48	15.33	18.09	20.12
NPGN	21.30	22.54	27.29	30.81
NPGY	36.08	32.62	40.93	47.08
WMID	17.63	12.75	15.33	17.24
EMID	19.75	13.64	16.62	18.83
SWALES	6.13	5.46	6.55	7.36
SWEST	8.66	6.73	8.17	9.25
LPN	3.40	2.58	3.24	3.73
SPN	4.57	4.62	5.27	6.56
EPN	5.15	4.08	4.85	6.39
SPD	34.68	35.50	41.59	46.10
SPMW	19.92	24.96	28.43	30.99
SSEH	5.19	2.72	3.30	3.75
SSES	7.88	5.24	6.31	7.17
Total	203.83	188.77	225.97	255.38

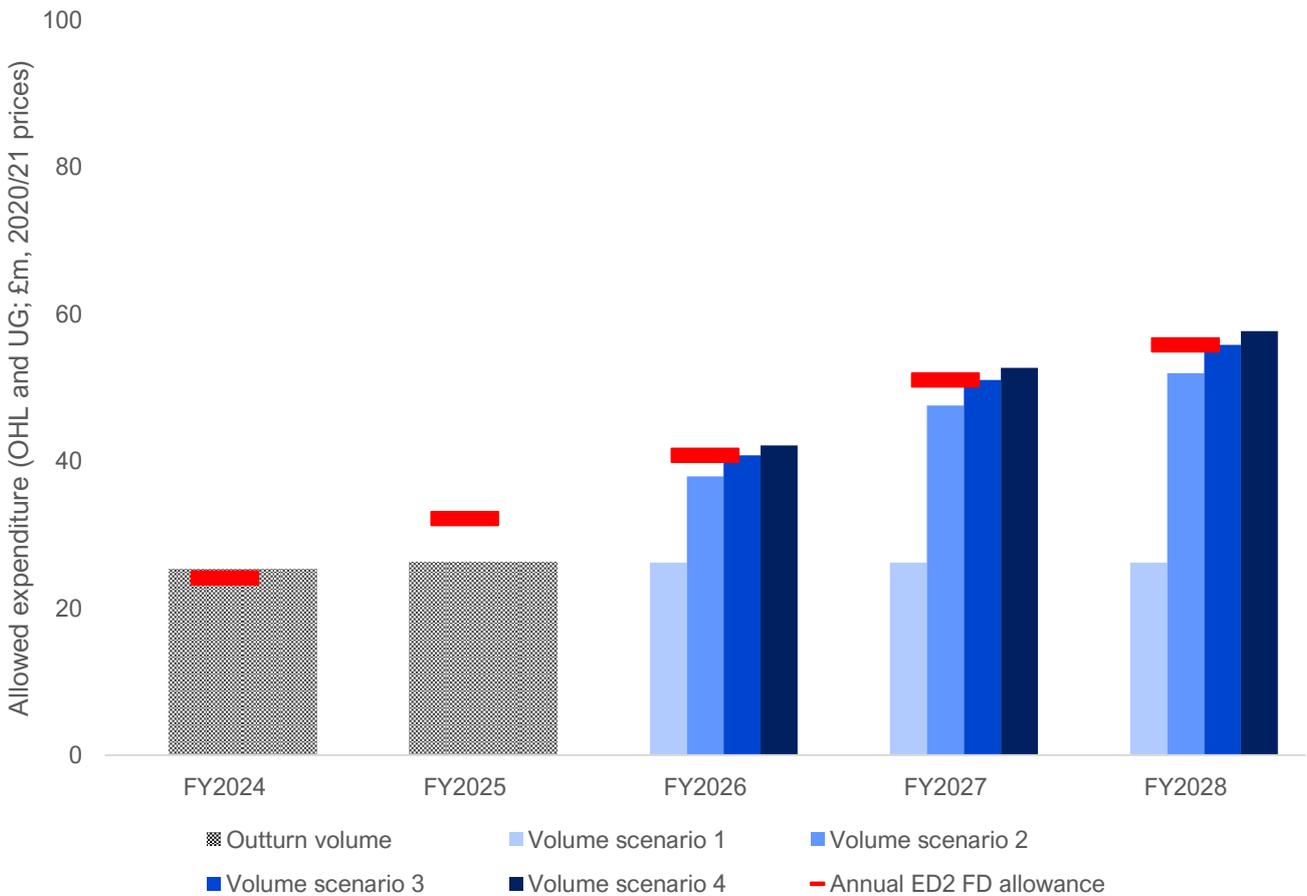
Source: CEPA analysis of DNO data. Volume scenario 2 is assumed for ED2 Years 3-5. The unit rate is updated for ED2 years 4-5.

Appendix B SENSITIVITY ANALYSIS

B.1. ALLOWED EXPENDITURE UNDER DIFFERENT UNIT RATES AND VOLUME SCENARIOS

These charts replicate the approach used in Figure A.2. However, instead of applying the Option 3 outturn unit rate in ED2 Years 4–5, these charts show the equivalent annual allowed expenditure profiles assuming the unit rates in Options 1 and 2 (respectively). The equivalent chart for Option 4 is not shown as forecast costs were only submitted by a subset of DNOs.

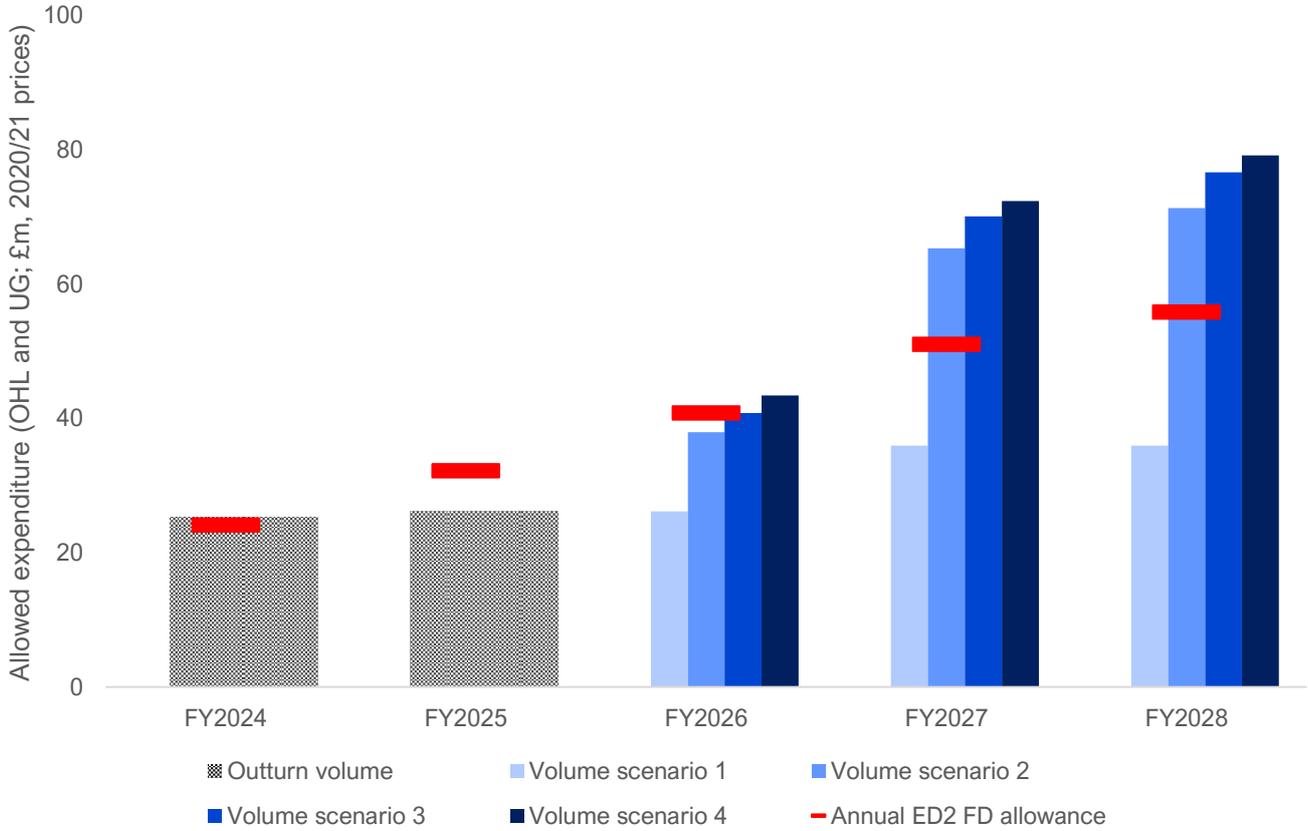
Figure B.1: Impact of volume scenarios on annual allowed expenditure for OHL and UG (Option 1: Maintain existing unit rates; £m, 2020/21 prices)



Source: CEPA analysis of DNO data. Using Option 1 (maintain existing unit rates) as updated rate in Y4-5.



Figure B.2: Impact of volume scenarios on annual allowed expenditure for OHL and UG (Option 2: Updated methodology unit rates; £m, 2020/21 prices)



Source: CEPA analysis of DNO data. Using Option 2 (updated methodology unit rates) as updated rate in Y4-5.

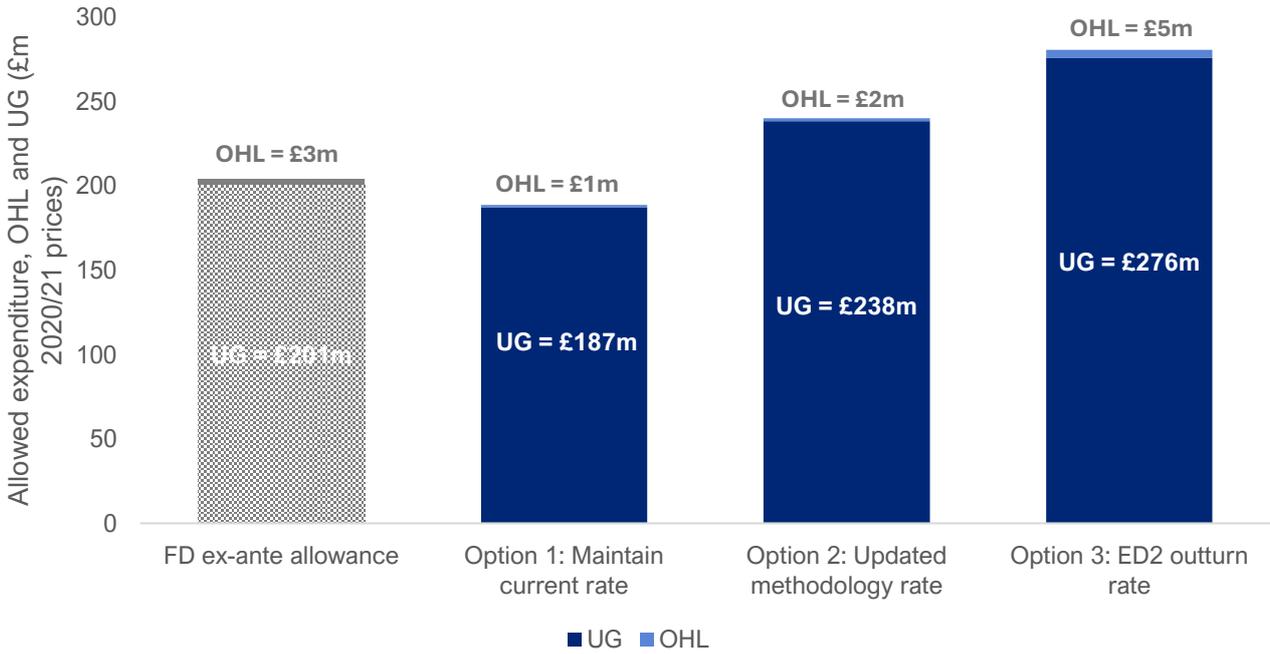
B.2. SENSITIVITY ON ALLOWED EXPENDITURE, ASSUMING UNIT RATES ARE UPDATED FROM YEAR 3 (INSTEAD OF YEAR 4)

At Ofgem’s request, the charts in this section show the impact on allowed expenditure, both the ED2 total and the annual profile, if unit rates were updated from FY2026 (Year 3) rather than FY2027 (Year 4). Ofgem is not considering updating rates in Year 3, but requested this sensitivity to illustrate the potential impacts on allowances.

Figure B.3 indicates that – if unit rates were updated in Year 3 compared to Year 4 – ED2 allowed expenditure would be approximately £15m higher under Option 2, and approximately £25m under Option 3. Figure B.4 provides the annual breakdown.

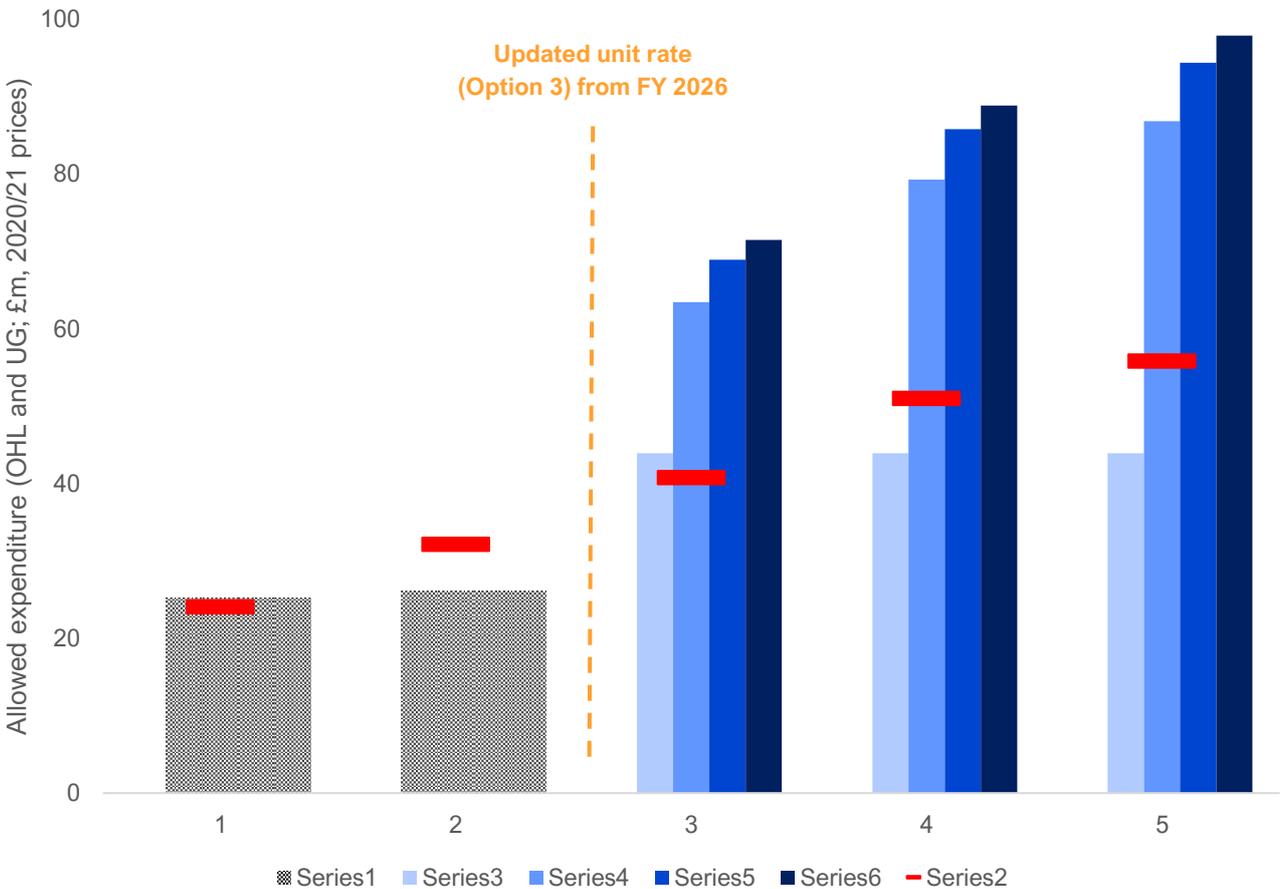
These sensitivity results are presented for completeness and do not imply that a Year 3 update is being proposed.

Figure B.3: Impact of unit cost options on allowed expenditure for OHL and UG (ED2 total; £m 2020/21 prices)



Source: CEPA analysis of DNO data. Unit rates are updated from Year 3.

Figure B.4: Impact of volume scenarios on annual allowed expenditure for OHL and UG (Option 3: ED2 outturn-based rate; £m, 2020/21 prices)



Source: CEPA analysis of DNO data. Unit rates are updated from Year 3.



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