Sustainability *first*

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13 March 2023

To: Dafydd.Burton@ofgem.gov.uk

Dear Dafydd

ED2 Annual Environmental Report Guidance

Sustainability First is a charity and think-tank focussed on social and environmental issues in energy and water. We have been closely involved in various regulatory debates, including around network charging and the RIIO price controls where we participated in Ofgem's Challenge Group and a number of Ofgem ED2 working groups. We have taken a particular interest in the environmental and decarbonisation aspects of ED2, in particular the environmental action plans. This includes submitting significant evidence in response to Ofgem's consultations and in particular the call for evidence on the company Business Plans where we provided a comprehensive review of the DNO strategies on SF6[1] and on losses[2].

We have consistently been concerned that the proposal to rely purely on reputational regulation for the environmental aspect of DNO performance risks creating the impression that this is of lesser importance compared to the range of other areas where Ofgem has provided financial incentives, including for strategy delivery. However, we have been assured by Ofgem colleagues, including on the stakeholder call for the ED2 Final Determination, that this is not the case and **we particularly welcome Ofgem's commitment in the draft guidance to carry out a mid-period review on EAP outcomes** which we hope will give more teeth to the AER ODI-reputational incentive.

That said, we are concerned that, as drafted, **Ofgem are seemingly already admitting defeat by highlighting the potential difficulties in making comparisons** – despite having set consistency and comparability as key principles at the start of the document. We note that Ofgem say there "would be merit in being able to make comparisons between licensees to identify examples of best practice but… the ability to draw direct comparisons may be limited" (5.2). In our view an essential part of the mid-term review should be publication by Ofgem of a detailed comparative report of DNO progress against company environmental action plan commitments and targets.

Throughout the guidance Ofgem "encourages" the companies to develop consistent reporting. This language needs to be strengthened with Ofgem setting a strong expectation (or ideally a requirement) around consistency. Consistent reporting is essential for transparency.

Along with the mid-period review (in effect a "deep dive") we assume that Ofgem will continue to produce the high level **RIIO annual reports** looking across the full range of aspects of company performance by sector. We would expect that, as now, these would include at least top level metrics

[1] https://www.sustainabilityfirst.org.uk/images/Sustainability_First_-_Commentary_-_DNO_ED2_SF6_STRATEGIES_-_final09022.pdf

[2] https://www.sustainabilityfirst.org.uk/images/Sustainability_First_-_Commentary_-_DNO_ED2_LOSSES_STRATEGIES_-_final090222.pdf

on SF6 and losses (which should be scrutinised in the same way that Ofgem would other metrics which will further help ensure reporting on a comparable basis).

On **SF6** we welcome the clear steer that companies should be looking at improving their reporting in ED2 with a view in ED3 to financially incentivising improved approaches to SF6 asset management and strategies for long-run phase-out.

We would like to see the same commitment in relation to **losses** ie to improved reporting with the expectation of stronger incentives in future controls, if not before.

We have noted in the attached annex our more detailed comments on the guidance.

As noted above, we are grateful to Ofgem for instituting a mid-period review and would be happy to talk further, nearer the time, about how to make this most effective – including the potential for oral hearings or other ways to increase senior management focus within the companies.

Yours sincerely

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Cc Judith Ward, Associate Sustainability First;

Zoe McLeod, Policy Director Sustainability First

Annex: Detailed comments on the guidance

Principles for Reporting

2.4 / 2.5 “As the purpose of the AER is to provide stakeholders with a picture of the impact their DNOs have on the environment, consistency and comparability is important”.

We agree that consistency and comparability are basic requirements. This is important because 'stakeholders’ include not only direct stakeholders of the DNO but also wider stakeholders with a national perspective (eg the Environment Agency, the CCC, environment NGOs etc). Even for local stakeholders the ability to judge ambition and delivery performance is helped by being able to compare across networks.

Report Structure

2.7 “In cases where a corporate group covers multiple licensees, a single AER can be published for the group”

A single document is acceptable but the performance of each DNO licensed area should be clearly identifiable in the report for each main environmental area

2.10 “The licensee’s AER must include information and data for the preceding Regulatory Year of RIIO-ED2”.

While year-on-year progress is important we would have expected the AER to provide a longer view, noting that many targets are set on the basis of performance over the full ED2 period. As generally provided for in the template, the AER should include runs of information and data from the final year of ED1, updated annually each year for every year of the ED2 price control.

2.11 The guidance says that for the final year of ED1 companies should follow SLC47. However, Ofgem should make clear that companies will also need to provide baseline data for the categories against which they will be reporting in ED2. That baseline data will need to reflect the position at the end of ED1.

AER Commentary

3.8 / 3.10 We welcome efforts to drive consistency in additional metrics including scope 3 reporting. However we are unclear why Ofgem only ‘encourage’ licensees to work collaboratively. There should be a clear expectation / requirement on DNOs to work together to develop a consistent and comparable approach. Collaborative working on scope 3 emissions is happening across many sectors[3] given that companies all have common value chains / suppliers.

3.12 We welcome the fact that offsets are being separately reported (and not counted towards overall reductions, in line with guidance from the Science Based Targets initiative).

3.13 On SF6 the text should be clearer and relate more explicitly to the Ofgem baseline expectations for SF6 strategies outlined in the Business Plan Guidance (30 Sept 2021. App 3. P.74). This included economic and efficient actions to reduce leakage rates and where appropriate, economic and efficient SF6 asset replacement; adopt a target for SF6 leakage reduction, and commit to reporting on total SF6 bank and leakage reduction rates using a common DNO methodology. It is important that in terms of qualitative reporting companies address both the level of SF6 leakage as well as their plans for managing the bank of assets they have with SF6 (which the template does) with an

[3] See for example this article on the pharmaceuticals sector

eye to containment and longer-term safe removal and disposal. It is not clear if companies are still adding SF6 assets when they carry out reinforcement work but if so this should be separately reported.

3.14 We welcome the acknowledgment of the need for reporting to evolve with an eye to SF6 removal being incentivised in future controls or sooner. In this context we note the clear steer being given at EU level through the F-gas Regulations and also through current DEFRA work to develop and adopt UK regulations.

3.15 Again we are concerned that Ofgem are only "encouraging" DNOs to collaborate on development of alternative equipment that is free of greenhouse gases and environmentally sustainable. There should be a clear expectation and they should report on that collaboration in the AER.

3.16 It is misleading for Ofgem to say that DNOs expect losses to increase "because of the uptake in distributed generation". In engineering terms losses increase quadratically with load (ie if load doubles losses increase four-fold). What is driving the expected increase in losses is the increased utilisation of existing network capacity that is anticipated in ED2 with the increase in the full range of distributed energy resources (including EVs, batteries and heat pumps – not solely, or even mainly, distributed generation) and also Ofgem's expectation that companies will make more use of flexibility – rather than network reinforcement - to keep costs down. However even then losses are not inevitable (as we made clear in our review of the DNO Losses Strategies) and Ofgem should be making clear that DNOs are expected to continue to innovate and find cost effective ways to better manage losses.

3.17 In that context we welcome the requirements on DNOs to report on what they have done to share best practice and to develop an improved framework for assessing and reporting losses during ED2. We have previously highlighted in particular the need for a better understanding of losses by time of day (noting that they are likely to be higher at peak times) which Ofgem might usefully mention explicitly.

3.18 This paragraph is a repeat of para 3.15 and appears out of place as it refers to SF6 not losses. We would however have liked to see a similar paragraph to 3.14 on SF6 flagging the potential for incentives on reducing losses in future controls.

3.31 On biodiversity companies should make clear where they are simply complying with the new legal requirements as part of planning and where they are going further. As Ofgem will be aware from November this year planning consent for development of a site in England will be subject to an obligation to improve the biodiversity of that site by 10%.

Key Performance Indicators

4.14 SF6: The guidance requires companies to report on the total number of assets that contain SF6 and total leakage in Kg. This information should be broken down for both bank and leakage by voltage level in the network. Voltage level is important (1) to aid comparability across networks given that 132KV is transmission level in Scotland (and SF6 volumes are greater at higher voltages) and (2) to understand the asset management challenge at lower voltages. DNOs should also report across their bank where units are sealed or not. In terms of the number of assets, new assets installed in ED2 should be separately reported. As part of reporting on total leakage it would also be helpful to understand the number of units affected (ie the number from which leakage occurred). Requiring this further level of reporting is important not just for transparency but also to ensure that both Ofgem and the DNOs develop a better understanding in the ED2 period of the scale, risk and

potential cost of DNO SF6 assets. This requires common approaches to SF6 inventories as well as proper monitoring and tracking of the performance on their networks of this increasingly important Business Carbon Footprint challenge.

4.16 Losses: The guidance requires companies to report on "interventions" they have taken to reduce losses. As set out in our review of the Losses Strategies as part of the Business Plan process it is clear that there are a range of very different forms of interventions that companies could take. To provide more transparency we would like to see Ofgem requiring the companies to report separately on "opportunistic asset replacement" (where the asset is being replaced for other reasons but will be replaced by lower loss equipment – either because that is all that is now available or where the incremental costs of low loss equipment can be justified); "proactive asset replacement" (where for some very old assets there is a case for asset replacement driven by the benefit in terms of reduced losses) and "operational actions" (eg voltage reduction).

The guidance also requires the impact of interventions to be reported in MWh and tCO2e. One problem we encountered in looking across the business plans was that these impacts were sometimes presented on a er annum basis and sometimes on the basis of savings over the lifetime of the asset. This needs to be clarified and made consistent across companies.

On the reporting of the total losses across the network requiring reporting in GWh, % and tCO2e helps paint a complete picture. However it would be helpful to explicitly show the assumed carbon intensity of the electricity system (which will be a key driver of falling tCO2e). AS we have noted previously losses remain important even as the grid de-carbonises because of the impact on the whole system costs of reaching net zero. Unpacking the reporting in this area is therefore important.

4.30 In the quantitative reporting on biodiversity it seems as if it only covers the biodiversity impacts of major capital projects (which helpfully delineates those requiring planning consent and others). However DNOs may also choose to carry out programmes to improve some of their existing sites where they see an opportunity and this should also be captured in the template.

On the **quantitative template**:

- It is essential that this includes data for the baseline year (presumably the end of ED1) to enable progress to be judged.
- It would also help the reader follow the numbers through if it could be made clear how the carbon emissions figures on the sub-sheets on SF6, IIG and losses flow into the top Business Carbon Footprint spreadsheet where there are lines for these elements.
- On SF6 there isn't a line to show the Global Warming Potential assumption (this may be in other Ofgem guidance but it would aid the reader if it were included here).