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to customers*

Your Ref:
Our Ref: RBA/DPCR/QOS/17
Direct Dial: 020 7901 7306
Email: angela.bourke@ofgem.gov.uk

26 October 2005

Dear Colleague,

Open letter on Ofgem's Electricity Distribution Customer Service Reward Scheme

1. Introduction

Ofgem utilises a variety of regulatory tools such as price controls, financial incentives and standards of performance, to improve the quality of service received by customers from electricity Distribution Network Operators (DNOs) – the companies that own and operate the poles and wires that deliver electricity to peoples' homes.

Under the most recent price control, ("DPCR4"), Ofgem established a Discretionary Reward Scheme to encourage best practice in areas that cannot be easily measured or incentivised through more mechanistic incentives. The following three categories were selected as areas to be covered by the scheme:

- Priority customer care initiatives;
- Initiatives relating to corporate social responsibility (CSR); and
- Wider communication strategies implemented by distribution companies.

The scheme has a total annual reward of £1 million available.

Over the past several months, Ofgem has been developing the format of the discretionary reward scheme. As part of this process, Ofgem has reviewed information provided by DNOs, considered their proposals and suggestions, met with staff from the Cabinet Office's Charter Mark scheme and consulted with energywatch.

The purpose of this letter is to advise stakeholders of the proposed structure and format of the Discretionary Reward Scheme and invite views on various aspects of the scheme.

2. Views invited

The proposed structure and format of the scheme is summarised in the attached Annex along with the aspects of the scheme on which Ofgem is seeking stakeholder views.

Responses to this open letter should be received by Friday 9 December 2005. They will be considered in finalising the development of the Discretionary Reward Scheme for implementation in April/May 2006.

The responses should be sent to Angela Bourke by e-mail to angela.bourke@ofgem.gov.uk or alternatively addressed to Angela Bourke, Quality of Service Manager, Ofgem, 9 Millbank, London, SW1P 3GE.

Unless marked as confidential, all responses will be published by placing them in Ofgem's library or on the website. It would be helpful if responses could be submitted both electronically and in writing. Any questions on this letter should, in the first instance, be directed to Angela Bourke, who can be contacted on 020 7901 7306 or on the above email.

Yours faithfully,

Martin Crouch
Director, Electricity Distribution
Ofgem

Annex – Proposed format for the Discretionary Reward Scheme

1. The Discretionary Reward Scheme

The aim of the discretionary reward scheme is to encourage better service for consumers in areas that cannot be easily measured or incentivised through more mechanistic incentives.

The scheme should achieve this by recognising leading performance and beacons of excellence within the industry and driving innovation and creativity through the promotion of best practice.

The scheme is designed to reward the performance of those DNOs which best serve the interests of customers across these categories throughout the year, particularly those DNOs which have a holistic approach to these areas embedded in broader business processes, not necessarily 'flagship' projects or one-off initiatives.

2. Proposed format for the scheme

The scheme has a total annual reward of £1 million available across all DNOs and will cover three areas:

- | | |
|--|-------------|
| 1. Priority customer care initiatives | (£ 600,000) |
| 2. Initiatives relating to corporate social responsibility (CSR) | (£ 200,000) |
| 3. Wider communication strategies implemented by DNOs | (£ 200,000) |

A greater focus has been given to the 'priority customer care initiatives' category as this has been identified as an area with many challenges and where much improvement can be made. It is anticipated that for future years the Panel will recommend the weighting of the reward across the categories.

For each of the three areas assessed under the Discretionary Reward scheme, Ofgem will specify a number of minimum requirements which should be included in any best practice example. DNOs would have to demonstrate that their initiatives incorporate these minimum requirements in order to be eligible to apply for a reward.

DNOs would be required to complete a submission outlining the details, results and impacts of their initiatives for each category they wished to apply for. DNOs would be required to provide information to substantiate their application and demonstrate that it meets (and exceeds) the minimum requirements identified by Ofgem (see Figure 1). Provided the minimum requirements are met, the aim of the scheme would be to identify which DNOs are achieving best outcomes for their customers. DNOs would therefore be expected to demonstrate the impacts of their initiatives both directly and as part of broader business processes. A standard application form would be developed by Ofgem for DNOs to submit when applying for a reward as part of this scheme. Each DNO would submit one application per year if it wished to participate.

It is suggested that DNOs have their submission supported by two or three relevant stakeholder organisations as a way of validating the information provided by the DNO and ensuring the integrity of the scheme. Another standard form could be developed for the stakeholder organisation to rate the DNO against a number of aspects of the initiative and to support the application for the reward.

3. Assessing reward recipients

Ofgem staff would review submissions from the DNO, clarify and seek any additional information, if required. Those submissions which include the minimum requirements identified by Ofgem would be forwarded to a multi-disciplinary Panel along with Ofgem's

summary of the submissions. The Panel would make a recommendation to the Authority as to which DNOs should receive a reward under the scheme (if any).

The Authority would then review the Panel's recommendations and make a formal decision on the reward recipients. It is expected that, in general, the Authority would endorse the Panel's recommendations. The Authority would then issue a Determination for each reward awarded under the scheme as per the relevant licence condition (Special Condition C2).

Those DNOs who received a reward under the scheme would have the details of their initiative(s) published and promoted on a 'Best Practice Register'. It is anticipated that this would include a short description of the initiative, why it was highlighted as a best practice example and contact details should further information be required. The format of the Register has yet to be decided and may be a web-based database or annual publication (or both).

A summary of the scheme format and proposed minimum requirements are included below. See Figure 1.

4. Discretionary Reward Scheme panel members

The panel will be comprised of five voting members and a non-voting Chair. It is proposed that a Managing Director from Ofgem would chair the Panel and the remaining five members would be drawn from the various consumer and industry organisations, including energywatch.

5. Views invited

Ofgem invites views on the proposed format of the scheme and in particular on the following issues:

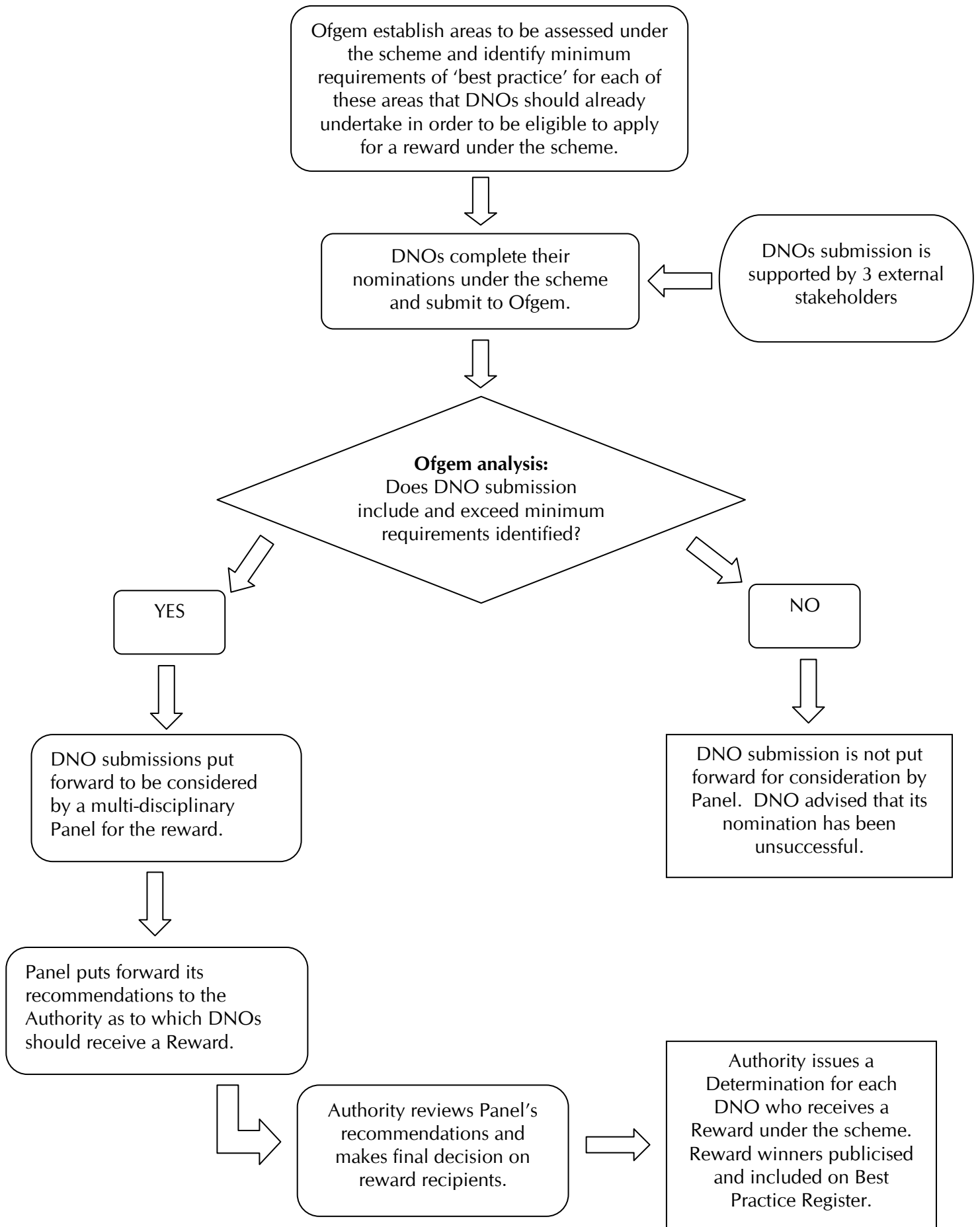
- The proposed split of the total reward across the three categories;
- Should the Panel decide the scope of the categories and how the reward is weighted across those categories in future years?
- The proposed minimum requirements of best practice outlined for each category; Any other information that could be used to assess DNO performance in each of these areas?
- Is it appropriate that DNOs have their reward submissions supported by relevant external stakeholder organisations? What would be the most effective way to do this? Ofgem would be particularly interested in hearing from such organisations on the practicality and impacts of this proposal.
- The format of the Best Practice Register;
- Possible members for the Panel.

6. Next Steps

Responses to this consultation letter will be reviewed and used to finalise the format of the Discretionary Reward Scheme. Ofgem may also undertake additional work with energywatch on further developing the minimum requirements outlined above.

It is anticipated that by February 2006, Panel members will have been invited and Ofgem will publish a decision letter setting out the final format and detail of the scheme. The Panel will then be in place to decide the rewards for 2005/06 regulatory year which would be announced in (approximately) June 2006.

Figure 1: Discretionary Reward Scheme Process



Proposed minimum requirements for each category covered by the scheme.

1. Priority Customer Care Initiatives

- DNOs are pro-active in ensuring that their priority registers are up-to-date and accurate and that customers are aware of the register;
- DNOs have effective and efficient procedures and processes in place to ensure that information on customers eligible for inclusion on the register is transferred readily between themselves and suppliers (and vice versa);
- DNOs have procedures and standards for staff on contact with priority customers and monitor performance against these standards; and
- DNOs seek feedback from priority customers and other stakeholders regarding the services it provides for priority customers and whether it is meeting their needs. DNOs use this feedback to improve the services that it offers.

2. Corporate Social Responsibility (CSR)

- DNOs have a CSR programme which is linked to its distribution business and result in benefits to its customers;
- DNOs CSR programmes have been incorporated into wider community programmes at local level through working with partners (where appropriate);
- DNOs seek feedback from stakeholders regarding its CSR initiatives and their effectiveness, including whether programmes and initiatives are reaching their target audience. The performance of CSR initiatives is regularly monitored and DNOs use feedback to improve their CSR programme; and
- CSR is recognised as important with DNO management level reporting responsibility.

Note: initiatives in this category should be at a DNO level rather than a wider company or corporate level.

3. Wider communication strategies

- DNOs have a range of communication strategies which reach their target audiences and are regularly monitored to ensure that they are meeting customers needs; and
- DNOs seek feedback from stakeholders regarding its wider communication initiatives and their effectiveness. DNOs use this feedback to improve their communication strategies.