



DNOs, IDNOs, consumer groups
and representatives and other
interested parties

*Promoting choice and value for
all gas and electricity customers*

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Consultation on Ofgem's Approach to assessing Stakeholder Engagement and Guidance Notes (Reference 24/12)

We would like your views on our approach to assessing Distribution Network Operators' (DNOs)' stakeholder engagement activities from 1 April 2012 in light of the implementation of the broad measure of customer satisfaction in April 2012. Responses to this consultation will inform our final assessment and should be sent to us by 27 April 2012.

In this letter we propose a framework by which we can assess the DNOs' stakeholder engagement activities. Additionally, we include Guidance Notes for the network companies to inform their submissions for the trial period 2011/12 in Annex 1.

Background

Stakeholder engagement is one element of the broad measure incentive which was introduced in the electricity distribution price control for 2010 to 2015 (DPCR5). The incentive is being trialled during the first two years of DPCR5 with no financial award attached. It goes live from 1 April 2012. The maximum financial award available to each DNO under the incentive is between £0.3m and £0.9m per year.

Assessment of each DNO's performance on stakeholder engagement takes place via an independent panel following the end of each financial year. The first assessment in terms of financial reward will be in summer 2013. DNOs qualify for assessment by the panel only if they meet certain minimum requirements.

We propose to test the approach we set out here in our assessment of the second year of trial (2011/12) in summer 2012. We will update the guidelines later in 2012 to take account of consultation responses and lessons learnt from the second year of trial. We will also formally update the regulatory instructions and guidance (RIGs). If necessary, we will continue to update the Guidance Note to take account of developments as the scheme progresses. Annex 2 to this letter sets out a timeline for next steps.

Minimum requirements

Our final proposals for DPCR5 set out a number of requirements that a DNO needs to meet in order to qualify for assessment under the incentive:

- the DNO must have in place an up to date engagement strategy addressing how they inform and obtain feedback from a range of stakeholders on the impact of their business activities
- a range of stakeholders must have been engaged and have commented on the DNO's approach to stakeholder engagement and on the changes the DNO is making in response to their views
- the DNO must have made use of a variety of mechanisms to inform and engage its stakeholders (and possibly demonstrated a year on year improvement)
- the DNO must be adapting its internal processes and policies in response to feedback from stakeholders.

First year's trial and lessons learnt

Under the DPCR5 incentives we proposed to trial the stakeholder engagement component for two years prior to the implementation of the broad measure. Stakeholder engagement was trialled alongside the electricity customer service reward scheme in 2010/11. In April 2011 we circulated a Guidance Note on stakeholder engagement which included the minimum requirements as set out in Final Proposals and the best practice principles which were informed by last year's customer service panel and an independent consultant. All of the DNOs provided a summary of their stakeholder engagement activities for 2010/11. The panel used to assess submissions for the electricity scheme also assessed the stakeholder engagement submissions and provided feedback on the assessment process.

The panel recognised that DNOs appear to be using a variety of mechanisms to engage stakeholders. However, they noted that DNOs were failing at that time to measure the benefits and outcomes of their stakeholder engagement on customers and business activities. In addition, it was not clear to the panel how DNOs adapted their internal processes in response to the feedback they received or how they informed stakeholders of changes in approach.

The panel provided some high level principles to inform the assessment process in future. They suggested that Ofgem or an independent body should audit DNOs' submissions and that arrangements should be established to assure the panel regarding the quality of each DNO's engagement activities. Additionally, the panel thought that its assessment should focus on the outcomes or activities resulting from engagement rather than the process of engagement itself.

Proposed assessment framework

Our proposed framework takes account of the lessons learnt to date from our first year trial and discussions with our stakeholders. We discussed the framework with the Customer Issues Working Group (CIWG)¹ on 28 November 2011 and 9 February 2012 and with Ofgem's Consumer Challenge Group (CCG)² in January 2012.

We propose a two part assessment process (detailed below) that will enable DNOs to demonstrate to us that they have met the minimum requirements, and that will allow the panel to focus on evaluating the quality of stakeholder engagement activities and the

¹ The Consumer Issues Working Group (CIWG) is an industry working group made up of Ofgem, DNOs and other relevant parties. It provides a forum to discuss policy issues relating to services provided by the DNOs to energy consumers in the UK.

² As part of the Price Control Review process, we engage with the Consumer Challenge Group (CCG). The CCG was first used successfully on the last Electricity Distribution Price Control (DPCR5) and consists of a number of professional consumer advocates. The CCG meets with Ofgem teams working on the Price Control reviews as well as a Committee of the Authority to raise important consumer concerns.

outcomes these activities have helped deliver. This year DNOs will need to submit parts one and two to us by Friday 8 June 2012.

As part of this assessment framework, DNOs will have some flexibility as to how they gather and present relevant evidence to meet the requirements of each stage. However, in assessing the quality of stakeholder engagement activities and their effectiveness in bringing about positive change, both we and the panel will want to be satisfied that the evidence they are examining is sound, robust and verifiable. As such, DNOs are encouraged to consider the following means of gathering evidence to support their submissions at both stages:

1. Independent evaluation / audit – to assess the DNO's approach to stakeholder engagement covering: process of engagement, quality of engagement, senior management buy in, impact on culture, organisational activities and senior decision making, cost effectiveness, likely outcomes for customers/communities etc.
2. Relevant accreditation schemes.
3. Results and feedback from stakeholder engagement surveys.
4. Evidence of culture change, senior management buy in, e.g. as reflected in key strategic documents and decision making.

We will take into account a number of factors to assess the suitability of the evidence provided, including:

- independence and reputation of evaluator/auditor; robustness of the evaluation methodology (performance indicators, logical implementation process, appropriate evaluation design); whether the evidence shows persuasive linkages between implementation and achievement of outcomes
- level of compliance with recognised and relevant accreditation scheme
- robustness of stakeholder engagement surveys – eg whether the sample was sufficiently balanced and inclusive of all relevant stakeholders
- evidence that written policies have been translated into practice.

Assessment of minimum requirements

Under part one of the assessment process, DNOs should provide evidence that they believe is sufficient and appropriate to demonstrate they have met minimum requirements. This is likely to involve the provision of evidence of activities/compliance under each minimum requirement in an agreed framework. This may draw on evidence from some or all of 1-4 mentioned above.

We will review the evidence submitted and will use it to assess whether each DNO has met minimum requirements.

Our proposal is that companies that have not met minimum requirements will not attend the panel session and will not be eligible for a financial reward under the stakeholder engagement incentive.

We seek views on approaches to providing assurance that minimum requirements regarding stakeholder engagement have been met and whether there should be a common approach across all companies - for example, a common evaluation or an independent audit administered by Ofgem.

Panel Assessment

Part two of the assessment involves an independent panel assessment of the quality of a DNO's stakeholder engagement activities and the outcomes these activities have helped deliver.

DPCR5 final proposals require DNOs to submit an annual summary of their stakeholder engagement activities³ specifying outcomes or action plans resulting from this engagement. The independent panel will assess these submissions to identify leading performers and best practice. The panel will then make recommendations on the allocation of a financial reward under the incentive mechanism where appropriate.

DNOs who have met the minimum requirement as assessed by Ofgem will attend a question and answer session to present their submission to the panel. We propose:

- that the panel will assess all DNOs' performance in the second year of trial in summer 2012. This will aid the trial process
- for the 2012/13, 2013/14 and 2014/15 financial years, that the panel assesses only DNOs that have passed part 1 of the process set out above to our satisfaction.

The panel's assessment will focus on DNOs' knowledge of their stakeholder group, the quality of their stakeholder engagement activities, lessons learned from stakeholder engagement and DNOs demonstrating how engagement has impacted on their policies, procedures, business plans, organisational culture and activities. We invite views on this approach.

Alternative approach

At the last CIWG in February 2012, DNOs showed broad support for the two part process set out above. This process means that a DNO needs to achieve success in part one of the process to qualify for panel evaluation and for consideration by the panel for a financial reward.

Some DNOs argued that within this process they should be rewarded for achieving accreditation (for example, 15% of the available reward) and a 'successful' survey result (for example, 15% to 35% of the available reward) to leave 50%-70% of the reward open to the panel to allocate.

Our initial view is that rewarding accreditation and a 'successful' survey outcome is not appropriate since these are steps to ensure that minimum requirements are met and would not represent good value for consumers. The purpose of the incentive is to reward the company based upon the outcomes of the stakeholder engagement process. The assessment of a financial reward by the panel will ensure that the focus of rewards under the incentive is on the outcomes of engagement. We believe that the DNOs' approach does.

Consultation Questions

We seek views on our proposed approach. In particular:

1. What other approaches to providing assurance should be considered appropriate?
 - a. Whether evidence submitted by DNOs should be subject to a common evaluation or independent audit administered by Ofgem.

³ Under our price control (DPCR5) Final Proposals all DNOs have to send us an annual summary of their activities.

- b. Whether there is a case for proposing a common assurance approach across all companies - for example a common accreditation standard or survey.
2. Your views on our approach to allocating the financial reward.
 - a. Do you think this is a fair and proportionate approach?
 - b. Can you suggest any other approaches and why do you think they are appropriate?
3. Factors the panel should take into account for the assessment of outcomes of engagement.
4. Any additional information or ideas on how the DNOs should be assessed for the purposes of this incentive.
5. Whether this approach to assessment should be applied to stakeholder engagement incentive schemes in other industries, i.e. Gas Distribution, Gas or Electricity Transmission.
6. Any concerns or further suggestions about our proposals.

Next steps

Our proposed timeline for next steps is set out in Annex 2 to this letter. Responses should be sent to Lia Santis, preferably by email to lia.santis@ofgem.gov.uk by **27 April 2012**. Unless clearly marked as confidential, responses may be published on our website.

If you have any queries in relation to consultation please contact Lia Santis by email or on 0207 901 1856.

Yours faithfully,



Andy Burgess
Associate Partner, Transmission and Distribution Policy

Annex 1 - Guidance notes for Stakeholder Engagement Incentive scheme– 2011/12



The aim of the incentive strategy is to encourage DNOs to engage with stakeholders in order to better anticipate their needs and deliver a more consumer focused, socially responsible and sustainable energy service. DNOs should be able to engage proactively with their stakeholders in order to inform and align their business goals with consumer needs.

The 2011/12 year is the second year of trial of the stakeholder engagement incentive. No financial awards are payable in respect of the 2011/12 financial year, however lessons learnt will help bed in and inform the process going forward. Where possible we intend that the assessment approach trials our two step approach for 2012/13 onwards.

Scope of the scheme

Stakeholders are individuals or organisations affected by the activities of the DNO. They may have a direct or indirect interest in the DNO's business, and their contact with the DNO may be anything from a daily interaction to those who have occasional contact. Stakeholders can include customers, investors, shareholders, regulatory authorities, NGOs and other interested organisations, workers and civil society with particular attention to vulnerable constituents.

We aim to incentivise DNOs to carry out a range of activities including to:

- encourage DNOs to identify who their stakeholders are and the best ways to elicit and collect stakeholder views
- identify instances in which lack of understanding or lack of information prevent feedback on key debates and ways to address it
- identify top concerns from stakeholders about DNO performance and implement plans to address them
- understand that different types of customers will have different needs and their needs will change with time and tailor information accordingly
- assess how consumers might change their use of the networks and understand how this should shape the service provided by DNOs
- produce robust business plans for the next price control informed by stakeholder engagement feedback.

We are inviting DNOs to put forward a submission in relation to stakeholder engagement activities carried out during the 2011/12 regulatory year which meets the minimum requirements as set out below.

Minimum Requirements

Our aim for the stakeholder engagement component is to encourage DNOs to focus on the outcomes achieved rather than the engagement process itself. Submissions under this category are expected to meet the following minimum requirements:

- the DNO has in place an up to date engagement strategy addressing how they inform and obtain feedback on the impacts of their business activities from a range of stakeholders
- a range of stakeholders have been engaged and have commented on the DNO's approach to stakeholder engagement and on the changes the DNO is making in response to the views of stakeholders

- The DNO has made use of a variety of mechanisms to inform and engage their stakeholders (and possibly demonstrated a year on year improvement)
- The DNO is adapting its internal processes and policies in response to feedback from shareholders.

Application Process

DNOs should note the approach to stakeholder engagement set out in our February 2012 consultation letter⁴ and provide evidence that they have trialled this process insofar as is possible.

DNOs will have some flexibility as to how they gather and present relevant evidence to meet the requirements of each stage. However, in assessing the quality of stakeholder engagement activities and their effectiveness in bringing about positive change, both Ofgem and the panel will want to be satisfied that the evidence they are examining is sound, robust and verifiable. As such, DNOs are encouraged to consider the following means of gathering evidence to support their submissions at both stages:

1. Independent evaluation / audit – to assess a DNO's approach to stakeholder engagement covering: process of engagement, quality of engagement, senior management buy in, impact on culture, organisational activities and senior decision making, cost effectiveness, likely outcomes for customers/communities etc;
2. Relevant accreditation schemes;
3. Results and feedback from stakeholder engagement surveys;
4. Evidence of culture change, senior management buy in, eg as reflected in key strategic documents and decision making.

Part two of the process is aimed at reviewing the outcomes and outputs of such engagement. DNOs should submit a summary of their stakeholder engagement activities specifying outcomes/action plans resulting from this engagement. Please note:

- Submission:

The submission should include the nature of the stakeholder engagement activities undertaken, demonstrate knowledge of their stakeholder group, the quality of stakeholder engagement activities, lessons learned from stakeholder engagement and how engagement has impacted on their policies, procedures, business plans, organisational culture and activities.

- Panel assessment:

The independent panel will assess all DNO entries this year. Their feedback to DNOs will bear in mind that in future years DNOs who do not meet minimum requirements as set out above will not be assessed by the panel and will not qualify for a financial reward.

Format of entries

DNOs should complete the attached entry form for this year's submission providing evidence that they have met minimum requirements and an overview of such evidence. Additional documentation supporting this form should be included as supplementary information.

DNO part two submission to the panel (as set out above) should not exceed **ten A4 pages** in total.

⁴ These guidelines are draft and responses to our consultation letter will be considered in any updates to these guidelines.

The format of the application and the use of graphics are flexible and there is no restriction on the font sizes used in submissions.

All submissions (part one and part two) should be received by Ofgem by **Friday, 8 June 2012**. All submissions should be sent to Ofgem's address in London for the attention of Lia Santis and emailed to lia.santis@ofgem.gov.uk.

Panel members

The Panel will be comprised of five or six voting members and a non voting Chair. The chair will be Philip Cullum, Partner, Consumer and Demand Insight from Ofgem. The remaining five members will be drawn from organisations with expertise in stakeholder and customer engagement.

Tenure on the Panel will be time limited, with a proportion changed from time to time to allow for a diversity of views, regions and organisations to be represented. Ofgem expects to confirm the membership of the Panel, as well as the date of the meeting, in the first quarter of 2012.

Panel meeting

Ofgem will collate the submissions and send them to the Panel prior to their meeting in July 2012. DNOs will be notified of the exact date and timetable for the day nearer the time.

Ofgem will provide some guidance to the Panel to assist them in making their recommendations regarding the rewards. This will take the format of some high level principles which the Panel should consider when assessing submissions from the DNOs.

The principles the Panel should consider include:

- which initiative(s) should be recognized as best practice and an example of excellence within the industry
- which initiative(s) are part of a holistic approach embedded in broader business processes
- which initiative(s) demonstrate a genuine change in the company's culture or improvement in the organization's decision making process leading to better outcomes for customers
- which initiative(s) have best served the interests of customers/communities throughout the year and resulted in measurable benefits.

Question and Answer session

DNOs that submit an application for the 2011/12 trial session will be invited by Ofgem to attend a 20 minute question and answer session with the Panel on the day of the meeting.

Feedback

Ofgem will perform a secretariat role at the Panel meeting. As was the case with previous year's customer service reward schemes, it is intended that after the Panel has made its decision there will be an opportunity for open discussion between the Panel, DNOs and Ofgem on the future of the scheme. There will also be an opportunity for the Panel to provide some general feedback on submissions to DNOs on the day. Attendance of the feedback session does not preclude further feedback discussions between Ofgem and the DNOs at a later date.

Annex 2 - Timeline of Scheme

