



Making a positive difference
for energy consumers

Gas distribution networks,
consumer groups'
representatives and other
interested parties

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Dear colleague,

Consultation on Ofgem's Governance Arrangements for the Gas Discretionary Reward Scheme under RIIO-GD1

We would like your views on our proposed governance arrangements for the Gas Discretionary Reward Scheme (DRS). The Gas DRS is one of the incentive mechanisms available for the Gas Distribution Networks (GDN) under the RIIO-GD1 price control arrangements. Responses to this consultation will inform our final assessment and should be sent to us, preferably by email, to connections@ofgem.gov.uk at by 3 June 2013.

The aim of the DRS scheme is to deliver outputs that contribute to environmental and social objectives beyond those funded through the price control. It should also contribute to the promotion of schemes to tackle risks associated with Carbon Monoxide (CO) poisoning. The scheme aims to recognise leading performance and drive innovation and creativity through the promotion of best practice. We expect successful schemes to serve as best practice and be replicated across the industry for the benefit of consumers.

In this letter we propose governance arrangements and an assessment process for the gas companies applying to the Gas DRS during the RIIO-GD1 price control period.

Background

The Gas discretionary reward scheme (DRS) was first introduced through the gas distribution price control for 2008-2013 (GDPCR1). The aim of the DRS was to encourage gas distribution network operators to improve performance in social and environmental areas that could not be measured or incentivised through more mechanistic regimes.

Under GDPCR1, the scheme had a total reward of £4 million to be allocated across gas companies on an annual basis in three main areas: reducing the environmental impact of gas distribution activities; facilitating new network connections for fuel poor consumers; and schemes to promote gas safety.

Under the new RII0-GD1 arrangements, the DRS scheme will run every three years starting from 2016 with a final tranche in year 2021.¹ We will publish a Guidance Note at the beginning of the calendar year when the scheme is due to take place.

Proposed Governance Arrangements

We have listed below the type of initiatives we expect GDNs to put forward under each output category. This is not a closed list and GDNs should not consider themselves limited to the examples we have provided.

1. Environmental outputs

- Initiatives that show commitment to delivering low carbon/environmental objectives within the company's daily operations.
- Initiatives that display an innovative approach to network development/planning for low carbon future (connections from bio-methane producers and/or other low carbon technologies).
- Initiatives that tackle the environmental impact of gas distribution activities (leakage/shrinkage).

2. Social outputs

- Development of energy solutions for the fuel poor.
- Initiatives that facilitate sustainable energy solutions to the fuel poor by building partnerships with other parties in the sector (e.g. electricity distributors, suppliers, technology providers, local councils, agencies).
- Initiatives that improve the knowledge that the company has regarding vulnerable and fuel poor customers in their service area.

3. CO safety outputs which include but are not limited to

- Initiatives showcasing an innovative approach to raising awareness of impacts of CO exposure among high risk groups.
- Initiatives that demonstrate good use of partnerships with relevant stakeholders (local and health authorities, NGOs, voluntary sector organisations, Suppliers).

¹ The total reward available for the price control period will be £12 million to be allocated across the gas companies.

- Initiatives that improve the development and/or access to data in order to identify and target high risk groups.

Eligibility

Applying for the Gas DRS Scheme (2016 to 2021 scheme)

We are proposing two key requirements in the application process for the DRS Scheme:

- Submission of an application in which each company demonstrates performance against the minimum requirements. The application form will be a standard template with text fields for the companies to briefly explain how they have met the minimum requirements and how it is linked to their main submission.
- A main submission where the companies set out those initiatives in the environmental, social and safety areas they want to present for the panel's consideration.

Minimum requirements

The application form requires evidence of how the companies have met the minimum requirements for each of the three categories during the relevant scheme year. The minimum requirements proposed include requirements that -

- GDNs have robust project management processes in place, appropriate resources and buy in at a senior level within their organisation to ensure commitment to the initiatives proposed.
- GDNs have performance indicators in place which monitor the impact of their initiatives.
- GDNs' systems and procedures put forward under this initiative show a marked improvement from initiatives previously put forward and have not been funded or incentivised through the price control or other incentive schemes.
- GDNs have engaged with a number of relevant stakeholders and can provide evidence of an existing engagement strategy which informs the development of initiatives and allows them to understand their impact.

Assessment approach

Each company must put forward initiatives for the three output areas defined above during the relevant scheme year. The activities can span one or more of their local distribution areas. They should have taken place during the three regulatory years prior to the year of the scheme, i.e. for 2016 scheme the activities should have taken place during 2013-14 and/or 2014-15 and/or 2015-16. Some of the companies (National Grid Gas Distribution, Scotia Gas Networks) operate more than one gas distribution network. For the avoidance of doubt, each company is limited to one application only in each year of the scheme.

Initial internal review by Ofgem

The first stage of the assessment process will involve an initial assessment of each application by Ofgem. This will be carried out by us in the period prior to the meeting of the expert panel. We will then provide the expert panel with a report on each of the applicant company's application, setting out if the minimum requirements were met.

Assessment by the DRS expert panel

An assessment of each GDN's initiatives will take place through an independent panel. The first assessment in terms of financial reward is expected to take place during the summer of 2016. GDNs will qualify for assessment by the panel only if they meet the minimum requirements.

We will provide some guidance to the Panel to assist them in making their recommendations. This will take the format of some high-level considerations which the Panel should take into account in their assessment.

These considerations should include -

- Which initiative(s) should be recognised 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) meet and exceed the minimum requirements specified by Ofgem
- Which initiative(s) have been supported by external stakeholder organisations, and
- Which initiative(s) have best served the interests of customers throughout the period and resulted in measurable benefits.

Question and Answer session

GDNs that submit an application for the DRS Scheme will be invited to attend a 15-20 minute question and answer session with the Panel on the day of the meeting.

Feedback

There will be an opportunity for the Panel to provide some general feedback on submissions to GDNs on the day, although it is not compulsory for GDNs to stay for this session. Attendance of the feedback session does not preclude further feedback discussions between Ofgem and the GDNs at a later date.

Panel composition

The Panel will be composed of six members, including a non-voting chair. The chair will be an Ofgem employee. Tenure on the Panel will be time-limited and we will seek to include representatives on the Panel from a range of organisations providing us with a diversity of views. Panel members' tenure will be limited to four

years initially, with an option to extend in some cases to allow for retention of panel experience.

We will announce the first membership of the Panel, as well as the date of its first meeting in early 2016.

The Authority's decision

Drawing on the views expressed by the Panel, Ofgem will make a recommendation to the Authority in relation to the award of the DRS Scheme.

The Authority will make a final decision in relation to the award of the DRS Scheme. Its decision will be informed by the assessment process outlined in this letter but it will not be bound by any recommendations or analysis made by us or the Panel. The Authority's decision will be published in the autumn following the Panel assessment.

Consultation Questions

We seek views on our proposed approach and in particular -

1. Whether the proposed assessment approach is appropriate and whether a panel review instead of a session would be more appropriate.
2. whether the approach to allocating the financial reward is proportionate?
3. Any additional information or ideas on how the GDNs should be assessed for the purposes of this scheme.
4. Any concerns or further suggestions about our proposals.

Next steps

Responses should be sent, preferably by email, to connections@ofgem.gov.uk by **3 June 2013**. Unless clearly marked as confidential, responses will be published on our website.

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

Yours faithfully,



Andrew Burgess
Associate Partner, Transmission and Distribution Policy