



Making a positive difference
for energy consumers

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

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Dear Stakeholders,

Decision on Ofgem's governance arrangements for the Gas Discretionary Reward Scheme under RIIO-GD1

Earlier this year we published a consultation on the proposed governance arrangements for the Gas Discretionary Reward Scheme (DRS) during RIIO-GD1 (the current price control that runs from 2013 to 2021).¹

We have taken into account the responses to the consultation and the feedback we have received from the companies and panel members. This letter explains our decision on governance arrangements for the RIIO-GD1 DRS.

Background

The aim of the DRS is to encourage gas distribution network operators (GDNs) to improve performance in social and environmental areas that could not be measured or incentivised through more mechanistic regimes.

The DRS was introduced as part of the gas distribution price control for 2008-2013 (GDPCR1). Under GDPCR1, the scheme had a total reward of £4 million to be allocated across gas companies on an annual basis. The allocation would reward activities of the companies 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 RIIO-GD1 arrangements, the DRS will run every three years, with the first assessment taking place in summer 2015. The total reward available for the price control period will be £12 million to be allocated across the GDNs.

Consultation

On 19 April 2013, we sought stakeholder views on the proposed governance arrangements for the DRS during RIIO-GD1. In our letter we set out -

¹ <https://www.ofgem.gov.uk/publications-and-updates/consultation-ofgem%E2%80%99s-governance-arrangements-gas-discretionary-reward-scheme-under-riio-gd1>

- the type of initiatives that we expect the GDNs to put forward for each output category
- the proposed approach for applying to the DRS with associated minimum eligibility requirements and
- the proposed assessment approach.

In our consultation we asked stakeholders for their views on our proposals.

Consultation Responses

The consultation closed on 3 June 2013. We received four responses to our consultation. All responses are from GDNs. Most respondents are broadly supportive of the proposed arrangements.

All respondents support a robust and objective approach to assessing the outputs of this scheme. Most of them believe the two stage approach is fit for purpose but would welcome the development of a more transparent framework and scoring mechanism. Some GDNs also welcome greater visibility of other GDNs' submissions in advance of the Panel assessment.

All respondents support appointing an independent panel to undertake the assessment. Two GDNs would welcome more active involvement from the Panel, either by increasing the time available at the panel session or by inviting the Panel to a site visit.

Several GDNs consider that the DRS assessment framework should promote collaboration amongst the GDNs, rather than foster competition. To help the panel assessment, one respondent considers that GDN activities associated with licence condition or incentives should be flagged to the Panel.

Several responses note the potential crossover between the DRS and the RIIO-GD1 Stakeholder Engagement Incentive. Two respondents suggest incorporating the value and outputs of the DRS into the Stakeholder Engagement Incentive. Two GDNs also suggest widening the scope of the DRS to allow it to reward other output areas (eg on helping to integrate with European-wide gas network and multi-utility issues).

Decision

Having taken into account the lessons learnt throughout the scheme, discussions with our stakeholders through the RIIO-GD1 Customer and Social Issues Working Group (CSIWG)², discussion with previous panel members and responses from our April consultation, we have decided on the content of the RIIO-GD1 DRS governance arrangements.

The RIIO-GD1 governance arrangements are broadly similar to those that we consulted on and are outlined in an Annex to this letter.

To confirm the governance arrangements for each DRS assessment, we will publish a Guidance Document in the calendar year prior to the allocation of the reward. The Guidance Document will confirm -

- the exact process for applying to the DRS (eg the dates for submission),
- guidance on the type of initiatives that we expect to be in each GDN's submission, and
- the high level considerations that the Panel may take into account.

² The RIIO-GD1 Consumer and Social Issues Working Group (CSIWG) is an industry working group made up of Ofgem, GDNs and other relevant parties. The forum was established to help develop the RIIO-GD1 price control and it provides a forum to discuss policy issues relating to services provided by the GDNs to energy consumers in the UK.

The Guidance Document will clarify the delineation between the DRS and the Stakeholder Engagement Incentive and provide the Panel with a principled framework to help its decision making.

We agree that the DRS should foster collaboration amongst the GDNs and each GDN submission should contain evidence demonstrating that companies have worked in partnership with other stakeholders to ensure that they play a full role in tackling key issues affecting consumers. We will guide the Panel to consider this as part of its assessment.

We can confirm that the DRS will reward GDNs against environmental, social and CO safety outputs. These output categories are purposefully flexible to allow GDNs to provide information on a wide range of activities. We do not consider that there is a need for additional output categories.

Unfortunately, the Panel will not have time to undertake site visits. However, we will ensure there is sufficient time in the agenda for a Question and Answer section of the panel session.

If you have any queries in relation to this consultation please contact Stephen Perry by email or on 0207 901 1806.

Yours faithfully,

A handwritten signature in blue ink that reads "Andy Burgess". The signature is written in a cursive, flowing style.

Andrew Burgess
Associate Partner, Transmission and Distribution Policy

Annex 1 – Guidance on applying for the RIIO-GD1 DRS and our approach to assessing submission

Governance Arrangements

We have listed below the type of initiatives we expect GDNs to put forward under each output category. This is not an exhaustive list and GDNs should not consider themselves limited to the examples we have provided. We may provide further guidance on the type of activities that we expect to be submitted under each output category, as part of our Guidance Document.

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 (eg 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).

Applying for the RIIO-GD1 DRS

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

1. 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.
2. 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. As part of their submissions GDNs should highlight any relevant licence requirements or incentives.

The exact process for submission of an application (eg the date of submission, the address to send submissions to) will be outlined in the Guidance Document

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 a requirement 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 and
- 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 specified regulatory years prior to the year of the assessment. 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. We will do this before the meeting of the expert panel. We will then provide the expert panel with a report on each of the applicant company's application, stating whether the minimum requirements were met.

Assessment by the DRS expert panel

An independent panel will assess each GDN's initiatives. The first assessment in terms of financial reward is expected to take place during the summer of 2015. 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 it in making its recommendations. This will take the format of some high level considerations which the Panel should take into account in its assessment.

These considerations will include –

- initiative(s) which should be recognised as best practice and an example of excellence within the industry
- initiative(s) which are part of a holistic approach embedded in broader business processes
- initiative(s) which meet and exceed the minimum requirements we specify;
- initiative(s) which have been supported by external stakeholder organisations (both other GDNs and other external stakeholders) and
- initiative(s) which have best served the interests of customers throughout the period and resulted in measurable benefits.

Question and Answer session

GDNs who submit an application for the DRS 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 GDNs do not have to stay for this session. Attendance at 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, to provide 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 in early 2015.

The decision

Drawing on the views expressed by the Panel, we will make a final decision in relation to the award of the DRS. Our 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. Our decision will be published in the autumn following the panel assessment.