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Dear James,

Consultation on Ofgem's proposed stakeholder engagement incentive arrangements

Scotia Gas Networks (SGN) welcomes the opportunity to respond to Ofgem's consultation on incentive arrangements relating to stakeholder engagement.

Our response is structured to firstly provide a summary of our overall views on Ofgem's consultation. This is then followed by a detailed response to each of the questions raised.

Summary of SGN's views

In general terms SGN agrees with, and is committed to, Ofgem's overarching aim to have in place arrangements that incentivise appropriate behaviours for all network companies to deliver excellent stakeholder engagement. In order to achieve this, SGN considers that:

1. Option.B is the most appropriate mechanism for incentivising behaviours that will improve stakeholder engagement. We consider the threshold for reward should be a performance score of 2, and the maximum reward should be available at a performance score of 8.
2. Should Ofgem wish to pursue Option. C, both the thresholds for maximum and minimum reward should be set at a reasonable level with corresponding incremental payments at different levels. We therefore consider Ofgem should employ a linear incentive mechanism where a score of 2 allows 20% of the total reward, and a score of 7 allows 70% of the total reward to be made to network companies.



3. Any stakeholder incentive arrangements should not be allowed to be modified on an annual basis by Ofgem. We consider Ofgem should provide greater regulatory certainty to network companies on the future mechanism to be employed for the calculation of incentive payments made in relation to stakeholder engagement. We do not consider Ofgem's current proposals currently achieve this outcome.

SGN's detailed responses to the individual questions raised in Ofgem's consultation are provided below.

Question 1: Do you consider that companies should meet a threshold level of performance before they are entitled to receive a reward? If so, what should the threshold score be, and why?

SGN considers network companies should meet a minimum threshold of 2 and as provided in Option. B of Ofgem's consultation. The current process already requires network companies to pass an initial assessment of their stakeholder engagement activities. This sets a minimum threshold that must be overcome to progress further, and we consider setting this level at a score of 4 does not better incentivise network companies to achieve a minimum standard, especially if a cross-sectoral comparison is undertaken in establishing these minimum scores. We think it important that gas distribution companies are primarily assessed against each other in deciding whether a company has attained the minimum threshold. In SGN's view, a wider cross-sectoral assessment is unlikely to appropriately recognise the different stakeholder groups that are specific to each sector (i.e. gas distribution, electricity distribution and transmission).

Question 2: Do you consider that companies should be able to receive their maximum reward for performance above a specified level? If so, what should the maximum reward score be and why?

SGN consider network companies should receive a maximum reward if they achieve a score of 8 or more.



We consider that having too high a threshold to achieve a maximum reward may in practice prove to be unachievable, and thus lead to the rationale for setting such a high threshold to be questioned. Moving forward, it will also be important for Ofgem to share initiatives that the top scoring network companies employ to deliver exceptional stakeholder engagement, as this will raise the overall benchmark in future and benefit all stakeholders.

Question 3: What should the incentive rate be between the threshold score and the maximum reward score?

We agree that, under Option B, if the score is between 2 and 8 the incentive rate should be linear (i.e. a score of 2 should attract an incentive payment of 20% and a score of 7 should attract an incentive payment of 70%).

We also consider any decision to adopt Option C, or a variation thereof, should also accommodate a linear incentive rate as described above.

If you require any further information on our submission then please do not hesitate to contact either Margaret Hunter at margaret.hunter@sgn.co.uk or myself at paul.mitchell@sgn.co.uk.

Yours sincerely,

Paul Mitchell
Regulation Manager