

All interested parties

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Dear Stakeholders,

Consultation on values within the stakeholder satisfaction output arrangements (electricity transmission licence, special condition 3D and gas transporter licence, special condition 2C)

Purpose

Since the start of RIIO-T1 in April 2013, the electricity transmission and gas transporter licences have provided for customer and stakeholder related incentives. These provisions are set out in special condition 3D of the electricity transmission licence and special condition 2C of the gas transporter licence. These licence conditions include various values denoted by a series of letters (focused on the stakeholder satisfaction part of the incentive). There was limited evidence available when RIIO-T1 final proposals were set in 2012 to determine these values.

This letter consults on what we propose these values should be and explains our approach to determine these. The letter also identifies next steps.

Background

The stakeholder satisfaction output licence conditions include multiple components, which all contribute to the output. These components are different for National Grid’s businesses, compared to the Scottish transmission owners (TOs). We have set out these components in Table 1.

Table 1: Applicable components of the stakeholder satisfaction output

Component	What this is	National Grid	Scottish TOs	In scope of consultation
Stakeholder engagement reward	Discretionary reward scheme	Yes	Yes	No
Customer satisfaction survey	Reward/penalty based on score against baseline	Yes	No	No
Stakeholder satisfaction survey	Reward/penalty based on score against baseline	Yes	Yes	Yes
Stakeholder key performance indicators (KPIs)	Reward/penalty based on score against baseline	No	Yes	Yes
External assurance	External audit of activities	No	Yes	No

Further details are outlined in our RIIO-T1 final proposals¹ and accompanying letter to the Scottish TOs.²

The values we are determining include:

- The baseline level for the stakeholder satisfaction survey for all companies
- The baseline level for the KPIs for the Scottish TOs only
- The cap and collar associated with National Grid's stakeholder survey incentive
- The relative proportions of the incentive components for each TO.

The baselines set the level above which the companies must score to achieve a reward. Any scores below will result in a penalty.

We consider that the baseline values should be defined so as to stretch and incentivise/reward performance in this area, beyond business as usual, whilst ensuring that under-performance is not rewarded. Using as much evidence as possible is therefore important in setting these values. While the TOs followed the appropriate process by making proposals at the end of April 2013 for the level of these baseline values we considered that we needed greater evidence to set robust values.

We recognise that while the process established in 3D12 of the electricity transmission special conditions and 2C12 of the gas transporter special conditions did not include a timetable, determining these values earlier would have been preferable, however we did not consider we had sufficient evidence to do so at the time. Our proposal takes account of this delay and consults on values which we now consider are better informed.

Proposal and reasons

Summary

The customer/stakeholder satisfaction incentive, whose combined results provide scope for rewards/penalties of $\pm 1\%$ of the relevant year's revenue for each TO, includes the following values that we are consulting upon:

National Grid (electricity transmission and gas transmission)

- Stakeholder satisfaction survey baseline – the level of stakeholder survey result that causes no extra, nor less revenue to be recovered
- Cap and collar – maximum and minimum levels that provide for the full increase or decrease in revenue to apply without requiring an average score at the extremes of the survey range
- The respective proportions of the incentive revenues that relate to the customer satisfaction survey and the stakeholder satisfaction survey.

SP Transmission and SHE Transmission

- Stakeholder satisfaction survey baseline – the level of stakeholder survey result that causes no extra, nor less revenue to be recovered
- KPI baseline – the level of stakeholder KPI result that causes no extra, nor less revenue to be recovered
- The respective proportions of the incentive revenues that relate to the stakeholder satisfaction survey/KPIs/external assurance performance.

¹ National Grid: <https://www.ofgem.gov.uk/publications-and-updates/riio-t1-final-proposals-national-grid-electricity-transmission-and-national-grid-gas-%E2%80%93-overview>

Scottish TOs: <https://www.ofgem.gov.uk/publications-and-updates/riio-t1-final-proposals-sp-transmission-ltd-and-scottish-hydro-electric-transmission-ltd>

² SP Transmission: <https://www.ofgem.gov.uk/publications-and-updates/direction-not-implement-key-performance-indicators-submitted-authority-under-special-condition-3d-stakeholder-satisfaction-output-sp-transmission-limited%E2%80%99s-spt-electricity-transmission-licence>

SHE Transmission: <https://www.ofgem.gov.uk/publications-and-updates/direction-not-implement-key-performance-indicators-submitted-authority-under-special-condition-3d-stakeholder-satisfaction-output-scottish-hydro-electric-transmission-plc%E2%80%99s-she-transmission-plc-electricity-transmission-licence>

Our proposed values for National Grid are in Table 2 below.

Table 2: Proposed values (National Grid Electricity Transmission and National Grid Gas)

Term	What the term does	Proposed value 2013-15	Proposed value 2015-2021
X	Stakeholder satisfaction survey baseline	5	7.4
Y	Cap	8	9
Z	Collar	3	5.8
AA – HH	Proportion of incentive customer:stakeholder	0.9 (AA & BB)	0.7 (CC, DD, EE, FF, GG, HH)

Our proposed values for SP Transmission and SHE Transmission are in Table 3 below.

Table 3: Proposed values (SP Transmission and SHE Transmission)

Term	What the term does	Proposed value 2013-2015	Proposed value 2015-2021
X	Proportion of incentive – survey	0.3	0.6
Y	Proportion of incentive – KPIs	0.6	0.3
Z	Proportion of incentive – external assurance	0.1	0.1
AA	Stakeholder satisfaction survey baseline	5	7.4
BB	KPI baseline	50	71 (SP Transmission) 84 (SHE Transmission)

Given years 1 and 2 of RIIO-T1 are now complete, we do not propose to direct values away from their expectations in this area for the first two years of RIIO-T1. These were the values the companies used as part of their annual reporting.

For years 3 to 8 however, we have used the greater evidence now available to us from the latest actual performance data (where relevant) to inform our proposal.

We have used the following data to inform our proposed values:

- Stakeholder satisfaction survey baseline – data available from 2012-13³, data from years 1 and 2 of the RIIO-T1 price control (2013-14, 2014-15)
- KPI baseline – data from years 1 and 2 of the RIIO-T1 price control.

The greater evidence now available to us has also informed our proposals to increase the weighting associated with the stakeholder satisfaction survey.

Survey baseline and the relative proportion of the incentive driven by the stakeholder satisfaction survey

The performance in stakeholder satisfaction surveys over this period, for all the TOs provides us with an average value of 7.4. We think it is appropriate to use data from all the companies to reach an understanding of where to place this baseline. This is because the format of the surveys is the same and the sample sizes of the surveys are reasonably consistent. We also gain confidence from the reasonable level of stability in all the companies' individual scores over the three years. Increasing the baseline level is consistent with providing an incentive to the TOs to continue strong engagement work with

³ Data was collected for this year as a 'dry run' though as it preceded RIIO-T1, there was no financial impact for that year's performance.

stakeholders and seek further improvements, while protecting consumers from paying for normal levels of performance.

As above the evidence now available enables us to have more confidence in the survey part of the incentives. Changing National Grid's weightings for the customer satisfaction survey and stakeholder satisfaction survey to 70% and 30% respectively (from 90% and 10%) means that both materially matter to the end result of the incentive, whilst also recognising the more limited number of respondents to the stakeholder satisfaction survey and retaining the focus on the customer component. Similarly for the Scottish TOs, while the KPIs are still useful indicators of performance, given our increased confidence in the stakeholder survey, we propose to change the relative proportions of the survey, the KPIs and the TOs' external assurance to 60%, 30% and 10% respectively (from 30%, 60% and 10%).

Key performance indicators

Both SP Transmission and SHE Transmission have KPIs as part of their stakeholder satisfaction incentive. We now have two years of results for the KPIs (no dry run was carried out). The two companies have materially different sets of KPIs. Therefore in setting their baselines we think it appropriate only to take account of their own KPIs for the two years rather than the performance against KPIs of both companies. This leads to the different levels in Table 2.

On 31 May 2013⁴, we stopped the automatic implementation of SP Transmission and SHE Transmission's KPIs. We recognised that the KPIs were generally acceptable. We noted a potential issue of double-counting against the incentive to deliver timely connections in SP Transmission's KPIs (since removed) and a question on one element of SHE Transmission's KPIs (that was also quickly resolved). We confirm by this letter that the TOs' current stakeholder KPIs are approved. This does not affect the provisions in the licence requiring the TOs to consider updating their KPI methodologies over time. We think that the KPIs could be improved and made more challenging (further removed from the TOs' licence requirements which we consider are business as usual). We want the TOs to demonstrate to us that they have reviewed and considered the level of challenge of their KPIs for year 4 onwards, in line with the process described in special condition 3D.23 of the electricity transmission licence. We would also like both Scottish TOs to revisit whether it is possible to develop joint KPIs, to enable a more effective assessment.

Cap and collar

National Grid have a cap and collar in their stakeholder satisfaction survey incentives to enable the full revenue impact (positive or negative) to be recovered/incurred without needing to average at the extremes of the survey scores (as this would be impossible or highly unlikely). We have proposed symmetric caps and collars at a higher level, around the new baseline. These are aligned with the cap and collar set for the customer satisfaction survey.

Achieving the full range of the incentive (SP Transmission and SHE Transmission)

We recognise that setting these proposed values, assuming no other changes, limits the scope for the Scottish TOs to obtain the full potential upside of the incentive whilst maintaining the full potential downside. This is because of the way the licence applies a type of cap and collar to remove the need to score the extremes to get the top and bottom revenue numbers. While the licence enables us to determine whatever values we feel appropriate in the specific areas, it is not our intention to reduce the scope of what can be recovered in all circumstances, ie the relevant proportions of the $\pm 1\%$ of revenue. Therefore we would like to discuss with the Scottish TOs how the licence might be changed

⁴ See footnote 2.

to enable the full incentive to be recovered, where warranted. We will discuss and consult separately on this but in time to be effective from year 3 results onwards.

Next steps

The consultation period ends on 27 July 2015. We welcome views on our proposals. We will consider any responses received ahead of making a decision on setting the values.

This consultation sets out proposed values for the rest of the control period. We will however continue to monitor and assess how well this incentive is working in reflecting real stakeholder satisfaction.⁵ We plan to ask stakeholders for their views and if we do not consider the incentive is working effectively in driving the appropriate behaviours then we reserve the right to review the incentive for years 5 to 8 of the RIIO-T1 period. We would not make any changes to years 1 to 4 as part of any such review.

We would like the TOs to continue, as they did in relation to the first year results, to review details of the survey performance. This includes the qualitative responses.

If you have questions about this letter please contact Karen Mayor (Karen.Mayor@ofgem.gov.uk, 020 7901 3089).

Yours faithfully,



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⁵ We noted in our 'RIIO-T1: Final Proposals for NGET and NGGT – Outputs, incentives and innovation' that we "may consider the stakeholder baseline and related metrics in 2016 looking at the wider evidence that we will have at that time about how stakeholders respond to this type of survey under different conditions and company performance": <https://www.ofgem.gov.uk/ofgem-publications/53600/2riiot1fpoutputsincentivesdec12.pdf>