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27th July 2015.

Kersti Berge
Electricity Transmission
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London SW1P 3GE.

Dear Kersti,

Consultation on values within the stakeholder satisfaction output arrangements

Thank you for the opportunity to respond to the consultation regarding the values within the stakeholder satisfaction output arrangements. This is a non confidential response on behalf of the Centrica Group, excluding Centrica Storage.

We have a number of significant concerns with the values proposed. The values for 2013-5 are likely to provide poor value for money for customers and we are unable to assess whether the values for the remainder of the period will do so. Our main concerns are:

- **The retrospective targets for 2013-15 appear to be inappropriate when compared to the evidence of actual performance and no justification is offered for how the values have been calculated.**
- **TOs cannot reasonably have expected to be rewarded on the basis of baseline values contained within annual reporting, as these values had not been consulted upon and were acknowledged by Ofgem as not based on evidence¹ and ‘conservative’².**
- **It is not possible for any party other than the TOs to properly assess the proposed baseline targets without access to the underlying data and methodology used to generate them.**

We believe incentive mechanisms should be designed so as to deliver value for customers and be calibrated so that companies are required to make continuous improvements in order to earn rewards. As such, whilst we agree that “...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...”, we also believe that baseline performance should include improvement factors over the course of the price control period to ensure that performance

¹ Transmission Annual Report 2013-14, 2.11: ‘In the absence of evidence, we set the baseline or bar at 5’.

² RIIO Transmission Annual Report 2013-14, 2.12
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improvements are required to maintain rewards and companies are not rewarded simply for standing still.

We do not agree with the rationale proposed with respect to the setting of the retrospective baseline targets. The difficulty with setting targets in retrospect is recognised in the consultation: *'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.'* However, it is clear from T1 Final Proposals³ and the licence terms that there were no values established to direct away from and that values would be based on evidence. The TOs cannot have reasonably expected to receive rewards based upon values within annual reporting that were not consulted upon and were described by Ofgem as not based on evidence⁴ and 'conservative'⁵. To be considered for use, these values need to be justified on their own merits and not because they appeared elsewhere, without consultation and without formal standing.

We understand and accept the reasons why Ofgem had not set values before this stage – namely that Ofgem did not consider they had sufficient evidence to set robust values. We support evidence-based approaches to the calibration of the incentive mechanisms and therefore would agree that in such circumstances it was appropriate to wait until they had sufficient evidence to set robust targets. However, having now acquired the evidence it was lacking in 2013, this should be used to ensure the retrospective baseline values proposed for 2013-2015 are credible when compared to the evidence it now has available.

Retrospectively setting baseline levels for the stakeholder satisfaction survey at 5.0 for 2013-15 is not justified by the evidence Ofgem has now acquired⁶, being lower than both the collar at which the maximum penalty is received under the customer satisfaction survey (5.3) and the collar proposed for stakeholder satisfaction survey for future years (5.8). Similarly, the KPI baseline for SP Transmission and SHE Transmission, which Ofgem propose to set at 50 for 2013-15, is inappropriate when the evidence now acquired demonstrates that such a baseline would provide rewards for business as usual.

Although it is not ideal that robust baseline levels are only now being proposed by Ofgem, this may be appropriate if sensible values could be derived that reflect good value for customers. However, as described above, by comparison to the evidence this has not been demonstrated in this instance. So, in the absence of formal baseline values being consulted upon and implemented into licence in time for regulatory years 2013/14 and 2014/15 it is inappropriate for TOs to be either rewarded or penalised for performance in those years, particularly if it will result in significant sums of money being paid by consumers for performance levels that, the evidence suggests, do not warrant it. We recognise that Ofgem may wish to reflect that some TOs may have outperformed others and so

³ For example, section 2.47 of the NGT Final Proposal states: *'The specific baseline metrics for the stakeholder element are being developed in light of evidence from the now completed dry run, and we expect NGET to propose metrics by April 2013'*. Given the time delay, we are assuming that the proposed values for 2013-5 are not based on the dry run and so are not as per expectations

⁴ Transmission Annual Report 2013-14, 2.11: *'In the absence of evidence, we set the baseline or bar at 5'*.

⁵ RIIO Transmission Annual Report 2013-14, 2.12

⁶ Ofgem propose a value of 7.4 for 2015/16 onwards using data from 2012/13-2014/15 although no supporting data or calculations have been provided.

suggest a fair approach to customers and stakeholders is to set targets around the average performance such that the overall reward is zero, but individual TOs may receive rewards/penalties.

Finally, for both schemes, we would require the data from which the relevant incentive values were derived and the detailed methodology used to derive those targets to be able to assess properly. Without such content, it is difficult for any party other than the TOs to properly assess whether the proposals will result in appropriately-calibrated incentive mechanisms. We welcome the opportunity to engage with you on these issues.

We hope you find our comments helpful and look forward to engaging with you on the development of this policy. Please do not hesitate to contact me if you have any questions.

Yours sincerely,

Andy Manning
Head of Network Regulation, Forecasting and Settlements