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Dear Mr McEachran,

Citizens Advice is pleased to respond to Ofgem's informal consultation on the new RIIO-ED1 Stakeholder Engagement and Consumer Vulnerability (SECV) Incentive guidance.

We welcome the new consumer vulnerability element being added to the RIIO-ED1 incentives. As this is the only DNO incentive that explicitly relates to the 'social obligations' category, one of six output categories under RIIO, it is important that the guidance on it delivers real benefit for vulnerable consumers.

We have previously had input into the process of developing this guidance at the discussion and read-through stages. We have recommendations on five aspects of the draft guidance, based on our work in this area and our wider experience of service provision for vulnerable consumers. More detail follows, but in summary they are:

1. **More direct reward for consumer vulnerability performance**
   - Allow the consultants' scores to directly determine the fifth Panel Assessment Criterion, exclude consideration of the Consultants' Report from the first four criteria, and increase the weighting of the fifth criterion to at least 50%.
2. **Avoiding double-counting between criteria**
   - DNOs should make it clear in their submission where they feel an action or result deserves to be considered against more than one criterion, and the Consultants and/or Panel should ensure that they are not rewarded twice.
3. **Fairer conversion of scores into financial reward**
   - Move to a straight-line incentive (SE_t = MSER x OPS / 10) to avoid the score inflation clearly indicated by the dry-run assessment.
4. **More emphasis on ongoing improvement**
   - Either include an emphasis on demonstrable progress since the last assessment in the individual criteria, or make this expectation clear overall elsewhere.
5. **More sharing of best practice**
   - Update the wording of each of the Consumer Vulnerability Sub-Criteria to set the expectation that DNOs actively seek out best practice from one another and actively share their own.

- Consider accepting a collaborative submission in addition to the individual submissions from some or all of the DNOs, as in the Discretionary Reward Scheme in GD1.
- Consider adding a 'consumer vulnerability' section to the Smart Networks Portal, or to set up a similar website for this purpose.

1. **Performance on consumer vulnerability should be more directly rewarded.** Under the current draft guidance, there is a risk that the detailed work that has gone into the Consultants' Report will be wasted because there is no clear mechanism for translating it into a financial outcome. The proposed arrangement is that the Panel 'will use the Consultants' Report to help assess network company performance', without specification of how this will work. Our view is that this is like renting a high-resolution camera (at cost to consumers) and then using the output as the basis for a felt-tip sketch.

   Our understanding of the rationale for this approach is that it tries to fit the new independent scrutiny of consumer vulnerability into the framework of the Panel Assessment Criteria (introduced following the previous SECV consultation in January 2015).[1] The fifth criterion, on consumer vulnerability specifically, is only worth 25% of the total score, so it makes sense that vulnerability would need to be considered under the other criteria. However, this method is too indefinite. It is counterintuitive and risks watering down how seriously consumer vulnerability is taken. It would be better to *allow the consultants' scores to directly determine the fifth Panel Assessment Criterion, exclude consideration of the Consultants' Report from the first four criteria, and increase the weighting of the fifth criterion*.

   As the SECV incentive is the only direct driver for social obligations outputs, we would recommend that the fifth criterion ('the quality of the DNO's strategy to address consumer vulnerability and the quality of the outputs delivered') should be worth *at least 50% of the total*. It would then not matter that the areas covered by the other four Panel Assessment Criteria, such as innovation and measurability, are also relevant to consumer vulnerability, as these will already be considered in the Consultants' Report. Effectively this would mean that the role of the Panel was to consider stakeholder engagement according to Panel Assessment Criteria 1-4, and to have oversight over the consultants' assessment of consumer vulnerability under Panel Assessment Criterion 5.

2. **There is a risk of double-counting between the categories.** Related to the lack of clarity in how the reward for consumer vulnerability performance is to be calculated, there is also a possibility of over-reward due to overlap between the categories. This is true both within the Consumer Vulnerability Sub-Criteria and between the Panel Assessment Criteria. The approach suggested above, of distinguishing clearly between consumer vulnerability (Panel Assessment Criterion 5) and stakeholder

[1] Ofgem, RIIO-ED1 Stakeholder Engagement and Consumer Vulnerability (SECV) Incentive Consultation (2014) https://www.ofgem.gov.uk/publications-and-updates/riio-ed1-stakeholder-engagement-and-consumer-vulnerability-secv-incentive-consultation

engagement (Panel Assessment Criteria 1-4), would partly address this. However, it may be that some measures are genuinely relevant to more than one criterion. If this is the case, *DNOs should make it clear in their submission where they feel an action or result deserves to be considered against more than one criterion, and the Consultants and/or Panel should ensure that they are not rewarded twice.*

3. **The mechanism for converting the Panel Score into a financial reward should be more rigorous.** This also applies to the scores in the Consultants' Report. The 'kink' in this reward was the subject of a consultation in 2014, and we argued then that a kink would lead assessors to disregard any scores below the lower limit for reward, in this case 4.[2] Based on the dry-run assessments carried out so far, this is exactly what has happened. *Therefore we again strongly recommend a straight-line incentive*, based on the simple formula SE_t = MSER x OPS / 10.[3]

   The rationale for a lower kink, i.e. a wide bottom band of scores which earn no reward, is that in an upside-only incentive, companies should not be receiving payments for poor performance. This makes sense. But a kink will only be an effective solution if it does not push the scores upwards. Unfortunately this is exactly what seems to have happened in Frontier's dry-run assessments, as we predicted, and we would expect it to continue in the actual Panel scores as well. Frontier allocated a total of 90 scores (15 subcategories across six DNOs). If these had been evenly distributed across the whole scale from 1 to 10, about 30% of the scores should have been below 4 - that is, the scores 1, 2 or 3 would have been awarded around 27 times out of 90. In the event, using a scoring system based on the Panel Assessment, not a single score below 4 was given (and only one 4).

   This would be a less serious problem if it was symmetrical, with the upper kink pushing scores down in the same way the lower kink evidently pushes them up. Following the earlier consultation, an upper cutoff of 9 was introduced on the basis that otherwise it would be unfair to companies, since none could expect to score a 10. In the dry run assessment, nine 10s were awarded (i.e. exactly 1/10 of all the scores). If the trend indicated by the rough scores in the dry-run assessment continued, with companies scoring an average total of 7.6 rather than scores being evenly distributed around the midpoint of 5, we calculate using the proposed methodology that this will cost consumers over £3m in each year of ED1, for no benefit of better incentivising the DNOs.[4]

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[2] Citizens Advice, response to Ofgem's Stakeholder Engagement Consultation (2014) https://www.citizensadvice.org.uk/Global/Migrated_Documents/corporate/cita-submission-on-stakeholder-engagement-incentive-may-2014-final.pdf

[3] Where SE_t is the stakeholder engagement (and consumer vulnerability) reward in year t, MSER is the maximum stakeholder engagement (and consumer vulnerability) reward available and OPS is the overall panel score out of 10, as per section 6 of the draft guidance. The current proposal is for SE_t to be 0 if OPS is 4 or less, to be equal to MSER if OPS is 9 or 10, and for a linear increase for scores between 5 and 8.

[4] The SECV incentive is up to 0.5% of DNOs' revenue. Averaged across RIIO-ED1, this revenue is around £3bn/year in total across the DNOs, so the maximum SECV reward is £15m/year. Using the kinked formula proposed in the draft guidance, assuming an average score of 7.6 as in the dry-run assessment, would result in an annual award of £10.8m (£15m x 0.2 x (7.6 - 4)). Using the unkinked formula we propose, assuming an average score of 5, would result in an annual award of £7.5m (£15m x 5 / 10).

We note that a parallel recommendation has been made by Frontier Economics themselves. In their report they recommend 'revisiting whether it is appropriate to retain a wide scoring range (0- 5) is available for "weak"' (p.88) and add 'we would expect that the Expert Panel scoring system would suffer from similar issues to the ones we found, and therefore that should also be updated' (p.89). We would question why Ofgem has not acted on this in the draft guidance.

4. **There is a need for a medium-term plan for continuing improvement.** The proposed arrangements give a good mechanism for providing a one-time snapshot. It is less clear that they will motivate consistent progress. Almost all of the Panel Assessment Criteria and Consumer Vulnerability Sub-Criteria might be met with no reference to past context and trajectory. This is an even greater risk if the consultants carrying out the assessment might change from year to year. This would mean that consumers were paying extra without seeing any improvement. It is welcome that some of the DNOs are already high-scoring, but they should not receive incentive payments simply for carrying on what they are already doing. *Either the wording of the individual criteria should include an emphasis on demonstrable progress since the last assessment, or this expectation should be made clear overall elsewhere*.

5. **There should be more emphasis on sharing results and best practice.** For example, if DNOs are incentivised to carry out research into consumer vulnerability, as per Consumer Vulnerability Criterion A, they should also be incentivised to publish and actively share their findings. Some of these findings might be specific to that DNO, but many will be useful to others or to wider stakeholders. There is a similar principle to the one raised by the LCNF and NIA/NIC: findings funded by the consumer should be publically available for the consumer's benefit.

   This applies not only to research but also to other initiatives, including the embedding of staff training under Criterion E. For the dry-run assessment a number of the companies undertook projects such as working with a particular training provider or adopting a particular predeveloped standard. If this works well, the default expectation should be that other DNOs are made aware, and if they choose not to adopt the same standards they should be able to explain why. This could allow economies of scale through shared training. Fundamentally, if network staff in one region can be trained to support consumers who are partially sighted, for example, there is no reason consumers elsewhere in the country should not have the same benefit. The approach to supporting consumer vulnerability in this way should not be a piecemeal series of optional extras.

   DNOs should also be incentivised to share their partnerships (criterion D). This is one of the areas where the widest range of scores was allocated in the dry-run assessment, with one company receiving the lowest of any average score and another the joint highest. This suggests there is a lot to gain by collaboration, but companies will not be incentivised to take this opportunity unless it is spelled out in the guidance. By their nature some partnerships (not all) will be highly scalable. Best practice should also be shared and sought out on PSR management (criterion C) and information gathering (criterion B) - that is, on all five Consumer Vulnerability Sub-Criteria.

One way to motivate better sharing of best practice would be to adopt the approach taken in the Discretionary Reward Scheme under RIIO-GD1, of a*ccepting a collaborative submission* in addition to the individual submissions, from some or all of the DNOs, provided there were clear provisions in place to ensure this did not allow free-riding or lower standards of individual performance. Another option would be *to add a 'consumer vulnerability' section to the Smart Networks Portal, or to set up a similar website*.[5] In addition to this, *the wording of each of the Consumer Vulnerability Sub-Criteria should be updated to set the expectation that DNOs actively seek out best practice from one another and actively share their own*.

Please do not hesitate to contact me if you would find it useful to discuss any of the points raised in this response further.

Yours sincerely,

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[5] http://www.smarternetworks.org/