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Dear Mr McEachran,

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

We were grateful for the opportunity to give feedback on the proposed changes at the informal consultation stage. Distribution networks have an important role to play in addressing consumer vulnerability. This was recognised by the introduction, under RIIO, of 'social obligations' as one of the six output categories for all network companies. At present, the proposed SECV incentive is the main driver for activity in this category, so it is essential that it is well targeted.

There should be ambition for real and meaningful results from the new consumer vulnerability component of this incentive. A significant amount of bill payers' money is at stake. The SECV incentive as a whole consists of up to 0.5% of DNOs' revenues, approximately £15m/year, and under current proposals a quarter of this is dedicated to the consumer vulnerability component, a little under 4m/year. On the one hand, it is not clear that this is enough to proportionately drive the change needed (see below). On the other, it is certainly enough that it would be regrettable if levels of ambition and acceptable performance were set too low. As a benchmark, this is more than three times the annual funding received by the Energy Best Deal and Energy Best Deal Extra programmes in 2014-15, developed by Ofgem and run by Citizens Advice.[1] As Ofgem's 'top 10' progress report on consumer vulnerability points out, more than 350,000 targeted consumers have substantially benefited from these programmes since they were launched.[2] We would expect to see a corresponding scale of demonstrable impacts from the SECV over the lifetime of the incentive.

We are pleased to see that much of our feedback on the guidance at the informal consultation stage has been acted on. This includes the clarification that the SECV will not reward activities which have an adequate primary driver elsewhere (in 5.2), and that the

[1] Funding received from British Gas, EDF Energy, First Utility, Scottish Power, SSE and Utility Warehouse for Energy Best Deal and Energy Best Deal Extra in 2014-15 was £1.235m: https://www.citizensadvice.org.uk/Global/CitizensAdvice/Energy%20Best%20Deal/CSEEBDEvaluationReport2014-15.docx.pdf

[2] https://www.ofgem.gov.uk/sites/default/files/docs/2015/10/er_top_ten_tips_v4_2_0.pdf

consultants' report will directly determine the consumer vulnerability criterion score unless the panel explicitly states otherwise (in 4.28).

On two other issues, we recognise that some adaptation has been made in response to our feedback, but we are still concerned that problems have not been fully addressed:

- At the informal consultation, we raised the concern that that nothing in the guidance would prevent a DNO giving the same submission each year and being rewarded for it, rather than being required to make progress. Although we welcome the addition of paragraph 2.4 - 'Where appropriate, we envisage that network companies will build on and highlight progress they have made, and are making, on their activities from previous years' - we believe this could be strengthened. Progress from the previous year should not be an optional extra. It should be the basic requirement that justifies awarding an extra incentive payment over and above the base return each year. A better wording might be: 'Network companies should build on and highlight progress they have made, and are making, on their activities from previous years. In a given year the panel will only reward initiatives that are either new in that year or have required genuine and demonstrable ongoing business activity from previous years.'
- We also raised the need to encourage DNOs to share best practice, research findings and successful partnerships. We recognise this is a difficult goal to achieve, since even though the assessment process is not explicitly benchmarked the DNOs may feel they are to an extent in competition with each other. However, better sharing would have an important positive impact, and make the spending of bill payers' money more efficient. We welcome the addition made to 4.13 specifying that the panel's feedback will include points 'that could, in future, be shared as best practice with other network companies'. But there is still a question as to how feedback is used. One approach to this would be to specify in the next paragraph, 4.14, that when informing each network of the scores of all the others, the panel may also include any non-commercially sensitive research or best practice that has not yet been published, if it judges that it would stimulate better performance in the next year. The requirement to publish findings should be analogous to the LCNF, since in both cases it is bill payers who foot the bill for research and experiment.

There were also a number of points that we raised at the informal consultation stage which we believe, if implemented, could improve the effectiveness of this incentive:

- First, we consider the weighting between stakeholder engagement (criteria 1-4, 75%) and consumer vulnerability (criterion 5, 25%) gives too little importance to consumer vulnerability. The statement in 4.28 that 'performance addressing consumer vulnerability issues is relevant to all of the Panel Assessment Criteria, most notably criterion five' only muddles the issue further. This arrangement gives too little certainty and will not be conducive to networks taking vulnerability seriously. Our view is still that a more straightforward and proportionate approach would be to allocate half of the incentive to stakeholder engagement and half to consumer vulnerability. This would make the total pot available for each approximately

£7.5m/year across all six DNOs, still a modest sum given that this is almost the sole driver in the RIIO 'social obligations' category.

- Second, we would like to reiterate our request that Ofgem revisit its decision regarding how it converts the panel score into a financial reward. We remain concerned that the current methodology could lead to over-rewarding, as under a 'kinked' scoring mechanism where financial rewards are only given between 4 and 9, panel members may be discouraged from using the full scoring mechanism. In practice, this is exactly what happened - in the dry-run assessment undertaken by Frontier Economics, out of 90 scores given across all the subcategories, not a single score under 4 was awarded.

  Our calculations suggest that an unkinked scoring mechanism centred around a mean score of 5 could lead to significant consumer savings. We appreciate that this saving might not be fully realised if panel members did not centre their scores around an average of 5. However, we believe that a superior scoring mechanism can be devised and we look forward to revisiting this issue with Ofgem.

Having raised these points at the informal consultation stage, we understand Ofgem's view may be that it is too late in the process to address them fully. We were informed, however, that Ofgem would be open to revisiting the guidance between the first and second years. We would like to see this taken forward and would welcome communication on this from Ofgem as the thinking develops. None of the issues we have raised would constitute a serious change of direction in such a way as to disrupt long-term planning by the DNOs, and lack of time and planning capacity should not be made an excuse for accepting negative consequences for consumers. The SECV guidance should be revisited after the first iteration with these issues in mind in the same way that the RIGs are often fine-tuned and adapted.

We would also like to draw an additional issue to your attention, which we believe may not have come up previously in the consultation process. Of the DNOs, WPD scored the highest mark in the dry-run assessment. It also made the most concerted effort to present a cost-benefit assessment of their major projects in their submission, a fact identified for positive feedback in the report by Frontier Economics. We think it is commendable to commit to this kind of self-evaluation.

However, their analysis demonstrates a net benefit, on their evaluation methodology, of £142k. This is impressive, but their score of 8.8 (even ignoring any impact on Panel Criteria 1 to 4 and only considering the 0.125% revenue linked to Criteria 5) would entitle them to 96% of the total reward available. This would be a 0.12% incentive payment on an annual revenue of almost £1bn: that is, approximately £1m, or seven times the benefit found in their own analysis. As WPD are the only DNO to undertake this self-evaluation and received the highest marks overall, it suggests that this may be a problem for other DNOs as well. We appreciate that there may be a range of benefits that are hard to quantify, and that the extent of the projects may grow substantially in future, but it is important to note this discrepancy so that it can be challenged in future if necessary.

Lastly, we would highlight the current discrepancy with GD1. We appreciate that different aspects of social obligations exist for the gas networks, namely fuel poor connections and carbon monoxide awareness. Equally some responsibilities for DNOs are less relevant to GDNs, such as outage response. Overall, though, there are many issues in common between them: both work with the PSR, the staff of both face similar communications and training issues, and both might benefit from a similar range of partnerships. However, the only social obligations incentive for GDNs at present is the Discretionary Reward Scheme (DRS). We think the £4m/year across the DNOs available under the SECV may not be enough to incentivise the necessary work on consumer vulnerability, but it is still far more than the DRS. The total DRS budget for the whole eight years of GD1 is only £12m, and this is split between social obligations, environmental obligations and promotion of carbon monoxide awareness. The amount available purely for social obligations for GDNs (not counting carbon monoxide awareness and fuel poor connections) is therefore only £4m over the price control, or £500k/year. Ofgem have expressed to us that this is an area they are likely to consider in future, and we would be happy to engage further on this issue.

Citizens Advice will continue to examine these issues, within the broader context of 'social obligations' as they have so far played out under RIIO and as they could and should play out in future. This will be the subject of a forthcoming short report, which we hope will contribute to an area where we feel substantial progress has been made but should not be considered a finished job.

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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