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RIIO-T1: Consultation on values within the stakeholder satisfaction output arrangements

Dear Geoffrey,

This response is submitted on behalf of National Grid Electricity Transmission (NGET) and National Grid Gas Transmission (NGGT). We operate the gas and electricity transmission networks in Great Britain. We also own and manage the gas transmission assets in Great Britain, and the onshore electricity transmission assets in England and Wales.

We recognise and support the importance of ensuring we effectively engage with our customers and stakeholders and welcome the introduction of the relevant incentive arrangements over the RIIO-T1 period. Incentive mechanisms benefit consumers and stakeholders by providing direct financial reward or penalty for our performance through the eight years of the current RIIO-T1 price controls.

For incentives to work appropriately, it is important that there is transparency for all parties on the targets companies should strive to exceed and the reward/penalty framework they face. We support the need to provide this clarity and certainty to allow companies to appropriately respond to incentives and we believe this provides the best outcome for consumers. If incentive properties are retrospectively changed, then this risks reducing the effectiveness of this incentive mechanism itself.

Therefore National Grid Transmission supports taking forward the Option 2 approach in the consultation, as this preserves the integrity of the incentivisation approach by ensuring incentives are transparent ahead of their period of applicability. We agree with Ofgem that Option 1 is flawed in this regard and hence should not be taken forward.

In terms of the other key elements of the consultation:

- 1) We support using historical evidence to set the baseline value now that we have three years' actual scores. This is a sound principle and will ensure that a realistic benchmark is set from which to reward good performance. It also means that only relatively good performance is rewarded.
- 2) On the weighting for different components of the incentive, there are two components relevant for National Grid's networks' incentives: the customer satisfaction and the stakeholder satisfaction survey. Setting the weightings is the method by which switching off the stakeholder incentive element for the first three years can be achieved. As such we support the Option 2 approach with 100:0 weighting on customer and stakeholder satisfaction respectively for the first three years of the price control. We then propose a weighting of 80:20 for years 4-8 of the price control rather than the proposed 70:30 weighting to reflect the fact that the stakeholder satisfaction incentive is still less mature than the customer satisfaction measures.
- 3) We propose setting the cap and collar at +/-1.1 around the baseline in order to align the stakeholder cap with the customer satisfaction element of the incentive and provide a realistic upper target to appropriately incentivise networks to improve.

Our response is appended and we hope you find it helpful. Please contact me if you would like to meet to discuss this further or if you have any questions.

Yours sincerely

Paul Auckland
Strategy and Regulation Manager

National Grid Transmission response to Ofgem consultation on values within the stakeholder satisfaction output arrangements

Question 1: Do you agree with our proposal to use the mean of the outturn data across TOs to set a robust baseline?

Yes, we agree that using the mean is the most appropriate basis upon which to set a robust baseline.

Question 2: Which of our two lead options for setting the survey baseline do you prefer?

Of the two options, we support Option 2 as the more appropriate methodology for setting the survey baseline because:

- It takes a similar approach to how the customer satisfaction survey baseline was set, i.e. by using past data to set the incentive parameters before the incentive is 'switched on'
- The retrospective first three years of RIIO-T1 therefore act as the dataset (the 'measuring phase')
- It avoids the situation where companies are being financially rewarded or penalised during the first three years of RIIO-T1 without a clear baseline to incentivise that year's activities and engagement, which we believe would be a fundamental misalignment with the original intent of the incentive.

We do not support Option 1 and agree with Ofgem that it is flawed because it sets a retrospective baseline that companies are unable to respond to. The aim of this incentive under RIIO was to encourage networks to positively change the way they work with their stakeholders, with the defined incentive/reward parameters helping to act as the driver for this change. Applying a target now for the first three years of RIIO-T1 would be retrospective regulation and be fundamentally at odds with the RIIO principles.

Question 3: Are there any other policy proposals for setting the survey baseline that you think are more appropriate?

As explained in our response to Question 1 above, we support Option 2 as the most appropriate way of setting the survey baseline.

Question 4: Do you agree with our rationale for setting the baselines for the KPI component of the stakeholder satisfaction output arrangements?

Not applicable for National Grid Transmission.

Question 5: Which of our two lead options for setting the KPI baselines do you prefer?

Not applicable for National Grid Transmission.

Question 6: Are there any other policy proposals for setting the KPI baselines that you think are more appropriate?

Not applicable for National Grid Transmission.

Question 7: Do you agree with our proposal to amend the licence algebra for the Scottish TOs should we implement baselines for the KPIs and the stakeholder satisfaction survey above 60 & 6 or below 40 & 4?

Not applicable for National Grid Transmission.

Question 8: Do you agree with our proposal to modify National Grid Electricity Transmission's licence to correct a typographical error?

Yes, we agree with this.

Question 9: Do you agree with our proposals for the weightings for the component parts of the incentive for National Grid and the Scottish TOs? If you consider there to be an alternative and well-justified basis for setting the weightings, we welcome views on this.

We have provided our views on the weightings for the first three years of RIIO-T1 in our response to Question 2 above. National Grid Transmission supports taking forward Option 2 as presented in the consultation with a weighting of 100:0 for the customer and stakeholder elements respectively for years 1-3, as this preserves the integrity of the incentivisation approach by ensuring incentives are transparent ahead of their period of applicability.

For 2016/17 onwards, our position on the weightings remains unchanged from our response to Ofgem's original consultation in July 2015 (https://www.ofgem.gov.uk/sites/default/files/docs/2015/10/national_grid_response_0.pdf).

Given the proposed rise in the survey baseline to 7.4 (from Ofgem's initial view of 5.0), we still believe that an increase in the stakeholder weighting to a maximum of 20% of the overall satisfaction incentive would be more appropriate.

Question 10: Do you agree with our suggestion to use the weightings to effectively switch off the incentive should Option 2 be the preferred option?

Yes, we agree that using the weightings would be the most appropriate way of doing this.

Question 11: Do you agree with our proposals to set the caps and collars for NG's and the Scottish TOs' stakeholder satisfaction survey at +/-1.6 around the baseline?

We suggest that a more appropriate cap and collar for stakeholder satisfaction would be achieved by setting the values at +/-1.1 around the baseline, in order to provide the same cap of 8.5 for both the customer and stakeholder satisfaction elements of the incentive. In doing so, this would:

- increase the power of the incentive, as incremental improvement or deterioration in performance would have a bigger impact on the company's incentive revenue
- recognise the constraints of a ten-point scale (for example, when compared to a percentage), where respondents are limited to ten options and achieving a score of 9 or 10 is rare, no matter how good the service provided
- appropriately incentivise networks to improve their performance, without feeling that the cap is unattainable. As with all objectives and incentives, targets should be achievable, and we believe that setting a cap at a level of 1.6 above the 7.4 baseline would create a target of 9.0 for average scores which would be extremely low probability to achieve.

Question 12: Do you agree with our proposals to set the caps and collars for SHE Transmission's KPI at +/-11 around its baseline (ie 100 and 78 respectively)?

Not applicable for National Grid Transmission.

Question 13: Do you agree with our proposals to set the caps and collars for SP Transmission's KPI at +/-16 around its baseline (ie 85 and 53 respectively)?

Not applicable for National Grid