Assessment of potential incentives

DCC identified a number of potential incentives that could potentially be applied to DCC's involvement during the Transitional Phase of the Switching Programme. These are:

- Number of bidders
- DCC participation in workstreams
- DCC Switching Business Case quality
- General product quality
- Stakeholder engagement
- Product timeliness
- Time taken to transpose solution into technical specifications
- Variance to DCC Switching Business Case forecasts / materiality thresholds.

We have assessed each potential incentive against the principles set out above. The summary of the assessment is set out below.

The points made in bold reflect a higher level of risk associated with a particular principle.

Number of bidders

Description of incentive: DCC is incentivised to attract a minimum number of companies to bid for the contract, who are key players in their field.

Principle	Positive or negative alignment to principle?	Rationale
No duplication	Neutral	This does not directly duplicate any existing rewards or penalties However, DCC can already have uneconomic and inefficient costs disallowed through its annual price control which means it is incentivised to ensure it secures pricing from an appropriate number of suppliers DCC also has a natural incentive to deliver a high quality procurement as it will be responsible for delivering the CRS solution and will want to ensure that it does so successfully to demonstrates its ability to deliver new areas of work
Encourage behaviour	Positive	This incentive would encourage DCC to engage with a certain number of bidders. A larger bidder market should encourage lower supplier prices and higher quality outcome of the procurement

Principle	Positive or negative alignment to principle?	Rationale
Proportionate	Negative	The cost of establishing and maintaining the incentive is likely to outweigh any benefit
Capable of being measured	Positive	Measuring the number of bidders is objective. The measurement should also take into account a pre-qualification assessment to ensure bidders are suitably qualified
Quantified limits	Positive	The limits of risk and reward can be easily applied by setting the bounds of the number of bidders i.e. a minimum and maximum. However, there may be some challenges in identifying the appropriate target number of bidders
Upside	Positive	Can apply rewards as well as risk e.g. above a certain number of bidders could be upside
Perverse incentives	**Negative**	**This places excessive focus on the number of bidders, instead of the quality of the procurement process** **Diminishing marginal returns on the engagement of additional bidders – the costs of additional DCC procurement resource and upside incentives may outweigh the benefit of lower bidder prices**
Reasonable control	**Negative**	**DCC can only encourage suitably qualified bidders to bid for CRS, but cannot compel potential suppliers to bid.** **Dependent on the chosen solution, there may be such a small number of suitably qualified bidders that the minimum number of bidders is unachievable**

Table 1 – Assessment of incentive for number of bidders

Because of the perverse incentives and lack of reasonable control, DCC considers that applying an incentive arrangement to this area would not be effective.

DCC participation in workstreams

Description of incentive: DCC is incentivised to participate to a specified quality level in Ofgem-led Switching workstreams.

Principle	Positive or negative alignment to principle?	Rationale
No duplication	Neutral	As a commercial organisation, DCC already has a strong commitment to its stakeholders with reputational incentives to achieve high levels of stakeholder satisfaction
Encourage behaviour	Neutral	This incentive would encourage proactive participation in workstreams, ensuring DCC attendance and contribution; however there is

Principle	Positive or negative alignment to principle?	Rationale
		unlikely to be a significant impact in addition to the existing commitment to stakeholders. This is not directly linked to achieving core Switching Programme outcomes.
Proportionate	Negative	The cost of establishing and maintaining the incentive (i.e. the cost of designing, running and analysing a survey) is likely to outweigh any benefit
Capable of being measured	Negative	Quality of participation is very difficult to measure objectively, therefore establishing parameters and measuring performance would be challenging
Quantified limits	Negative	It would be difficult to set limits for risk/reward due to the subjective nature of the assessments
Upside	Negative	It would be difficult to apply upside due to the subjective nature of the assessments
Perverse incentives	Negative	Good programme delivery does not always equate to satisfied stakeholders. For example, it may be in the interests of the programme for DCC to challenge vested interests in relation to the current arrangements or to challenge the quality of the design work carried out by other parties, where doing so results in a more robust design that better meets the objectives of the programme
Reasonable control	Positive	DCC would be in control of its participation in the programme and can plan accordingly

Table 2 - Assessment of incentive for DCC participation in workstreams

Because of the number of negative impacts, DCC considers that applying an incentive arrangement to this area would not be effective.

DCC Switching Business Case quality

Description of incentive: DCC is incentivised to produce a DCC Switching Business Case to a specified quality level.

Principle	Positive or negative alignment to principle?	Rationale
No duplication	**Negative**	**The quality of the DCC Switching Business Case is already fully scrutinised under ex post plus price control arrangements and Switching Programme governance** **In addition, there is a natural existing incentive to develop a high quality DCC Switching Business Case as DCC wishes demonstrate quality delivery in order to secure future work**
Encourage behaviour	Neutral	Whilst it may incentivise a high quality DCC Switching Business Case document, which is an important enabler for the programme, this does not

Principle	Positive or negative alignment to principle?	Rationale
		target the key outcome of successful Switching Programme delivery which can only apply to the DBT and Live Operations phases
Proportionate	Negative	An incentive value linked to the quality of the DCC Switching Business Case (a relatively immaterial cost) will not be proportionate to the cost of implementing the incentive
Capable of being measured	Negative	Quality is difficult to measure objectively, therefore establishing parameters and measuring performance would be challenging. This would require Ofgem to issue clear guidance on what constitutes high quality. Quality could mean that the business case is well reasoned.
Quantified limits	Negative	It would be difficult to set limits for risk/reward due to the subjective nature of the assessments
Upside	Negative	It would be difficult to apply upside due to the subjective nature of the assessments
Perverse incentives	Positive	DCC Switching Business Case quality does not carry any risk of perverse incentives
Reasonable control	Positive	The quality of the DCC Switching Business Case is within DCC's control

Table 3 - Assessment of incentive for DCC Switching Business Case quality

Because of the duplication with ex post plus governance arrangements and the lack of any other compelling positive case, DCC considers that applying an incentive arrangement to this area would not be effective.

General product quality

Description of incentive: DCC is incentivised to deliver its products to a specified quality level to minimise the number of reviews.

Principle	Positive of negative alignment to principle?	Rationale
No duplication	Neutral	This does not directly duplicate any existing rewards or penalties However, there is a natural incentive to do this already as DCC wishes demonstrate quality delivery in order to secure future work
Encourage behaviour	Positive	This should incentivise quality products, which are the foundation of the programme, therefore this should be aligned to the right outcomes It should also ensure that products are on track to support wider Switching Programme milestones e.g. ready for planned consultation dates
Proportionate	Negative	The cost of establishing and maintaining the incentive is likely to outweigh any benefit

Principle	Positive of negative alignment to principle?	Rationale
Capable of being measured	Negative	Measuring the number of required reviews would be easy to measure, however, the quality measure would be more subjective. This would require Ofgem to issue guidance on what constitutes high quality The scope of all the products and activities for the Transitional Phase is not yet clear so it would be difficult to set the incentives in advance.
Quantified limits	Neutral	Easy to set limits for risk/reward based on the number of review cycles for products It would be difficult to set limits for risk/reward for the subjective nature of the assessments
Upside	Neutral	Easy to apply upside to a desirable level maximum number of review cycles for products It would be difficult to apply upside due to the subjective nature of the assessments
Perverse incentives	Negative	DCC may be incentivised to withhold products from Ofgem until they are complete, reducing the early visibility of Ofgem to key thinking with which it may not agree. The failure to surface these debates quickly could result in nugatory work and delays to the overall Switching Programme
Reasonable control	Negative	Whilst DCC is in control of the products it is allocated, it is not in control of the Ofgem review process and how reviewer's interpret the acceptance criteria for products There are also dependencies on Ofgem for information to allow the completion of products to a satisfactory level

Table 4 - Assessment of incentive for general product quality

Because of the overriding number of negative impacts, DCC considers that applying an incentive arrangement to this area would not be effective.

Stakeholder engagement

Description of incentive: DCC is incentivised to engage with its stakeholders at the right time and in an effective manner.

Principle	Positive or negative alignment to principle?	Rationale
No duplication	Neutral	As a commercial organisation, DCC already has a strong commitment to its stakeholders with reputational incentives to achieve high levels of stakeholder satisfaction However, DCC is already required to engage with stakeholders under ex post plus price control

Principle	Positive or negative alignment to principle?	Rationale
		reporting arrangements and Switching Programme governance e.g. design teams and user groups
Encourage behaviour	Neutral	This would encourage the collaborative and consultative behaviour desired by Ofgem. However, this does not directly target the key outcome of successful Switching Programme delivery
Proportionate	Negative	The cost of establishing and maintaining the incentive (i.e. the cost of designing, running and analysing a survey) is likely to outweigh any benefit
Capable of being measured	**Negative**	**Quality of participation is very difficult to measure objectively, therefore establishing parameters and measuring performance would be challenging. The measurement of effectiveness will be subjective and parties may have vested interests around what they judge as effective engagement**
Quantified limits	Negative	It would be difficult to set limits for risk/reward for the subjective nature of the assessments
Upside	Negative	It would be difficult to apply upside due to the subjective nature of the assessments
Perverse incentives	Positive	Good programme delivery does not always equate to satisfied stakeholders. For example, it may be in the interests of the programme for DCC to challenge vested interests in relation to the current arrangements or to challenge the quality of the design work carried out by other parties, where doing so results in a more robust design that better meets the objectives of the programme
Reasonable control	Negative	Ofgem controls the forums which DCC has with stakeholders for the Switching Programme

Table 5 - Assessment of incentive for stakeholder engagement

Because of the subjective nature of measuring DCC's effectiveness, the vested interests of assessing parties and the lack of any compelling other reasons, DCC considers that applying an incentive arrangement to this area would not be appropriate.

Product timeliness

Description of incentive: DCC is incentivised to deliver DCC products, for example impact assessments to time and to agreed quality standards (acceptance criteria).

Principle	Positive or negative alignment to principle?	Rationale
No duplication	Neutral	This does not duplicate any existing rewards or penalties. However DCC has existing obligations in its licence to carry out its activities in support of the Switching

Principle	Positive or negative alignment to principle?	Rationale
		Programme in a timely manner There is also a natural incentive for DCC to demonstrate timely delivery in order to secure future work
Encourage behaviour	Neutral	As long as minimum quality levels could be defined, the timely delivery of DCC products would support the timely delivery of the Switching Programme Difficult to target programme critical tasks, as the overarching Switching programme plan is not sufficiently detailed and stable to define the critical path activities. There would be no tangible benefit to incentivising accelerated delivery of activities which are not on the critical path
Proportionate	Negative	The cost of establishing and maintaining the incentive may outweigh any benefit. The associated requirement for close management of dependencies is likely to require additional management overhead, particularly in relation to defining acceptance criteria, managing change and determining the root cause of any delays.
Capable of being measured	Negative	Time of delivery of a product would be easy to measure, although measurement of quality would be more subjective. However, the overarching Switching programme plan is not sufficiently detailed and stable to define the critical path activities, therefore it is not possible to identify definitively which milestones would be suitable candidates for incentivisation
Quantified limits	Positive	It would be possible to apply limits of risk/reward e.g. setting bounds of time
Upside	Positive	It would be possible to apply rewards as well as risk e.g. if earlier there is upside However, this may exacerbate the potential perverse incentives
Perverse incentives	**Negative**	**This incentive may encourage DCC to be overly cautious in its planning to reduce the risk of late delivery, which may result in longer delivery timescales** **This incentive may encourage DCC to make compromises in the procurement approach it plans to adopt such that it prioritises faster delivery over depth or breadth of competition, which may not support the best interests of the programme**
Reasonable control	Negative	Many products will be dependent on timely Ofgem and industry stakeholders input. The associated requirement for close management of those dependencies is likely to require additional management overhead, particularly in relation to defining acceptance criteria, managing change and determining the root cause of any delays. Changes to the scope of a product will affect the timing of its delivery

Table 6 - Assessment of incentive for product timeliness

Because of the number of negative impacts and the key perverse incentive impact, DCC considers that applying an incentive arrangement to this area would not be effective.

Time taken to transpose solution into technical specifications

Description of incentive: DCC is incentivised to transpose the solution into technical specifications to time based on a specified quality level.

Principle	Positive or negative alignment to principle?	Rationale
No duplication	Neutral	This does not duplicate any existing rewards or penalties. However DCC has existing obligations in its licence to carry out its activities in support of the Switching Programme in a timely manner There is also a natural incentive for DCC to demonstrate timely delivery in order to secure future work
Encourage behaviour	Neutral	As long as minimum quality levels could be defined, the timely delivery of DCC products would support the timely delivery of the Switching Programme Difficult to target programme critical tasks, as there is no detailed programme plan (and resulting critical path) for the Transitional Phase. There would be no tangible benefit to incentivising accelerated delivery of activities which are not on the critical path
Proportionate	Negative	The effort associated with managing target delivery dates may be disproportionate to the level of benefit. The associated requirement for close management of dependencies is likely to require additional management overhead, particularly in relation to defining acceptance criteria, managing change and determining the root cause of any delays.
Capable of being measured	Negative	Time of delivery of a product would be easy to measure, although measurement of quality would be more subjective However, the overarching Switching programme plan is not sufficiently detailed and stable to define the critical path activities, therefore it is not possible to identify definitively which milestones would be suitable candidates for incentivisation
Quantified limits	Positive	It would be possible to apply limits of risk/reward e.g. setting bounds of time
Upside	Positive	It would be possible to apply rewards as well as risk e.g. if earlier there is upside However, this may exacerbate the potential perverse incentives
Perverse incentives	**Negative**	**By focusing on the time of delivery to a minimum quality level it might encourage DCC to do the minimum required and focus on speed rather than quality, which could have a negative**

Principle	Positive or negative alignment to principle?	Rationale
		impact on the overall Switching Programme objectives. **This incentive may encourage DCC to be overly cautious in its planning to reduce the risk of late delivery, which may result in longer delivery timescales**
Reasonable control	**Negative**	**Changes to, or gaps within, the solution will affect timing. Many elements of the solution will not be produced by DCC and so will be beyond DCC's control** **The associated requirement for close management of those dependencies is likely to require additional management overhead, particularly in relation to defining acceptance criteria, managing change and determining the root cause of any delays**

Table 7 - Assessment of incentive for time taken to transpose solution into technical specifications

Because of the number of negative impacts and the key perverse incentive impact, DCC considers that applying an incentive arrangement to this area would not be effective.

Variance to DCC Switching Business Case forecasts / materiality thresholds

Description of incentive: DCC is incentivised to ensure incurred spend is in line with its forecasts as set out in the DCC Switching Business Case.

Principle	Positive or negative alignment to principle?	Rationale
No duplication	**Negative**	**The existing scrutiny and potential disallowance of costs through the ex post price control regime acts as a disincentive for unjustifiable spend** **An existing penalty interest regime on over recovery of DCC costs already exists to prevent over forecasting**
Encourage behaviour	Positive	This would further encourage DCC to accurately estimate its costs and to manage within that estimate, which would encourage behaviour in line with a target programme outcome of on-budget delivery
Proportionate	Negative	Additional incentives in this area would be disproportionate given the existing price control regime
Capable of being measured	Positive	Variance from forecast costs will be reported on as part of the ex post plus price control arrangements for this DCC Switching Business Case
Quantified limits	Positive	The limits to incentives could easily be implemented through the use of variation tolerance bands

Principle	Positive or negative alignment to principle?	Rationale
Upside	Positive	An upside incentive could easily be applied using a variance tolerance which DCC should keep within
Perverse incentives	Negative	The focus on delivery against the forecast might disincentivise DCC from proactively identifying additional activities that would support the achievement of the core Switching Programme objectives, or from identifying additional savings
Reasonable control	Positive	DCC is in control of its cost base, where this is strictly tied to a fixed scope of work Where DCC is a participant in Ofgem-led activity, scope change would lead to cost base movement outside of DCC's reasonable control. There would therefore need to be protective measures put in place to recognise this lack of control

Table 8 - Assessment of incentive for variance to DCC Switching Business Case forecasts / materiality thresholds

Because of the significant negative impact of the existing ex post price control disincentives for DCC to either over recover or overspend, DCC considers that applying an incentive arrangement to this area would not be effective.