

SGN Customer Engagement Group

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Dear RIIO2 team

Sector Specific Consultation Document – Gas Distribution

This response is on behalf of SGN's Customer Engagement Group which has been put in place to challenge SGN's Business Plan and to provide assurance to Ofgem on how it meets the needs and wants of consumers. As a part of this we are keen that the framework Ofgem puts in place around RIIO2 allows adequate opportunity for stakeholder and consumer input to SGN's proposals and that any centrally determined outputs and incentives reflect the interests of SGN's consumers.

As such we consider it appropriate that we respond to key Ofgem consultations in our own right and we have provided comments below on some the questions raised in the Sector Specific Consultation Document - Gas Distribution. We are sharing this response with SGN but it is our independent view. Some members of the CEG will also be submitting responses in their own right or on behalf of the organisations they work for. The following comments reflect points where there was a broad consensus that these were issues it was appropriate for us to raise as a CEG. We hope that as part of encouraging a stronger consumer voice in RIIO2 Ofgem will give due weight to these consumer views, representing the consumer voice in the process.

We also provide some comments on the CEG role in the process, noting where in the consultation Ofgem suggests the CEG could play a role. While we will clearly attempt to support Ofgem's process in whatever ways they would find helpful we are keen that our inevitably limited time and resources is devoted to where we can add most value.

Chapter 3: Meet the needs of consumers and network users

Q1 – The overall package

SGN's CEG is generally supportive of the proposed approach to RIIO2, which represents a clear expectation of continued focus and improvement on consumers and network users. We agree with the aim of consolidating the improvements seen during RIIO1 which we consider is best achieved through:

- stretching targets and commitments aimed at embedding good practice in customer service within business as usual;
- innovation and improved targeting of services aimed at customers in vulnerable situations, and
- concentrated efforts to better manage and support customers through interruptions.

We are especially supportive of the proposals to create more flexible and dynamic incentive packages in this area which would encourage GDNs to continue to explore new opportunities through the GD2 period.

Customer satisfaction survey - The SGN CEG is supportive of Ofgem's intention to build stretching customer satisfaction targets into the GD2 price control.

Complaints metric - The SGN CEG supports Ofgem's intention to update the complaints metric target score.

Q4 – Views on the Outputs Ofgem propose to remove

Stakeholder Engagement Incentive

The SGN CEG supports Ofgem's aspiration for high quality stakeholder engagement to become embedded within GDNs as a business as usual function. We feel strongly, however, that retaining this incentive is necessary to ensure Stakeholder Engagement remains a high priority for GDNs throughout the price control period, attracting the level of funding necessary to ensure continued improvement and – more importantly – build capacity among stakeholders to provide ongoing input, challenge and, where appropriate, co-creation in a complex and rapidly changing environment.

Discretionary Reward Scheme

The SGN CEG notes Ofgem's reasons for proposing to remove the Discretionary Reward Scheme and the proposal for the social and carbon monoxide safety elements to be replaced by the consumer vulnerability package. We are concerned, however, as noted below, at the loss of CO awareness and safety initiatives to all consumers, as opposed to vulnerable consumers only.

In addition, as discussed further below, the CEG is disappointed at the proposed loss of incentives for GDN to innovate and develop best practice in environmental initiatives. We are not aware of any other incentives that encourage GDNs to reduce their carbon footprint, and yet this is an issue that is important to SGN's consumers. While the Discretionary Reward Scheme may not be the most effective way to incentivise this behaviour among GDNs, it is essential that Ofgem continues to incentivise improvement in this area to ensure GDNs meet customers' expectations in this area.

Views on proposed outputs:

Q5/6 - Consumer vulnerability

We are very supportive of proposals aimed at continuing the improvements made by GDNs in supporting vulnerable consumers. It makes sense to ask GDNs to focus their efforts specifically on activities that relate to their existing role and areas of competence and to co-ordinate better with existing government schemes. The SGN CEG notes that stakeholders have highlighted the importance of flexibility and a longer-term view of the support provided to vulnerable consumers to ensure that this is appropriate to the customer's circumstances and is effective, relevant and sustainable beyond the short-term.

Carbon monoxide safety awareness

While the SGN CEG supports Ofgem in encouraging GDNs to address carbon monoxide safety awareness among vulnerable consumers we are concerned about the removal of incentives for GDNs to undertake carbon monoxide awareness activities among consumers more widely given the priority that we know consumers attach to safety. Arguably all customers could be considered vulnerable when faced with the risk of carbon monoxide poisoning (the "invisible killer"). While this is not necessarily a helpful extension of the definition of vulnerability it highlights why broader awareness activities should be in scope of the incentive.

Q7 – Use-it-or -lose it- allowance

In relation to the consumer vulnerability use-it-or-lose-it allowance, the SGN CEG believes that this would be a helpful and useful approach to funding activities alongside a reputational incentive. We would support a flexible approach that would allow SGN to fund new initiatives that are identified (and justified) during the RII02 period rather than expecting all the details to be set out in the Business Plan.

Q9 -Options for a Vulnerability Package

Like Ofgem, the SGN CEG believes the combined package of minimum standards, incentives and funding for activities that go beyond business as usual seems best-placed to consolidate progress to date and promote the innovation and competition required to underpin further progress in this area. We particularly support the proposal for a principles-based Licence Obligation requiring GDNs to support vulnerable consumers as part of business as usual – we believe a principles-based approach is more likely to encourage innovation and creative thinking within individual GDNs than a more prescriptive compliance-based approach.

The SGN CEG supports the proposals to evaluate approaches to consumer vulnerability via the wider business plan incentive but believes that a new reputational ODI is essential to encourage ambition across the GDNs and promote best practice across the sector. The SGN CEG is also supportive of proposals for an on-going role for CEGs in challenging GDNs efforts in relation to the consumer vulnerability incentives.

Q10-14: The Fuel Poor Network Extension Scheme

The SGN CEG is supportive of Ofgem’s proposals to retain the existing scope of the FPNES and to encourage better targeting and alignment with existing schemes but would like to see this done as part of a ‘whole house’ solution.

We would also encourage Ofgem to remain mindful of tensions between new gas network connections and broader decarbonisation objectives, but agree that the FPNES remains an appropriate and necessary part of GDNs’ activities. Thought could be given to increased support to district heating or a requirement to consider the carbon impacts as part of the current assessment of whether gas is the best option, as ways to help achieve this balance.

In terms of how best to incentivise GDNs to improve targeting of the FPNES (Q11), the SGN CEG believes that a more flexible, ex-post incentive is most likely to encourage innovation and improvements/adaptions within the price control period. We are also supportive of linking this incentive to the Stakeholder Engagement Incentive (which we strongly believe should be retained) to encourage partnership working, and to the proposed vulnerability reputational incentive to encourage sharing of best practice.

Incentivising GDNs to ensure that households receiving FPNES connections achieve a target level of energy efficiency is, in our view, essential in ensuring GDNs activities to support vulnerable consumers go beyond a short-term crisis-driven approach and result in affordable warmth which is

effective and sustainable for the customer in the longer term (Q13) – as well as supporting one of the clear “no regrets” strategies for heat de-carbonisation.

Q15-22 Guaranteed standards of performance

The SGN CEG welcomes a review of the GSOPs to ensure they are still relevant to current expectations of minimum standards. We agree that, in general, payment levels should increase in line with the CPIH and are supportive of Ofgem exploring whether payment levels in relation to some GSOPs should increase beyond that. We are also supportive of the proposal to make all GSOP payments automatic (Q18) to ensure consumers that are entitled to payments receive them without having to make a claim – we note the Citizen Advice assessment of the level of unclaimed payments in 2015/16. However, the benefits of all these changes to customers must be weighed against their strongly expressed view that SGN should focus on ‘keeping costs down’. Any changes that will involve material additional costs should be tested through willingness-to-pay research.

Q19 - We note that Ofgem is considering a new GSOP around guaranteed appointment times for re-connection following an interruption. We have not seen evidence of consumer demand for guaranteed appointments among SGN consumers and are concerned about the additional cost of this, especially as SGN customers have consistently identified ‘keeping costs down’ as their top priority. The CEG has encouraged SGN to look at the underlying issues relating to guaranteed appointment times to see how they can best be addressed without resulting in a large increase in customers’ bills.

Q23-25 Unplanned Interruptions

We support Ofgem looking at options to replace the current reputational incentive for total unplanned interruptions and would welcome the opportunity to work with SGN, alongside other stakeholders, in setting targets that are both challenging and achievable.

We believe that Option 3 – the hybrid approach – is the best way to ensure targets are realistic for individual GDNs while also allowing a role for relative benchmarking to shore up standards across the sector.

That said we are aware that for most customers these interruptions are extremely rare and that it is often the way they are handled (eg in terms of communications and on the ground support) that is as important as the duration (with the exception potentially of MOB). We encourage Ofgem to ensure that it has the evidence of consumers’ experience and priorities to support any changes that it makes if there is a risk that this will increase costs.

Chapter 4: Deliver an Environmentally Sustainable Network

Q26: The overall package

SGN’s CEG has been set up with a diverse membership chosen to bring in, inter alia, the perspectives of “future consumers” and non-traditional business models such as community energy, in line with Ofgem’s guidance. As such the CEG has taken a strong interest in this area.

We are also very aware that the Scottish government has a high level of ambition around de-carbonisation. While energy policy is clearly reserved to Westminster the Scottish government does

have devolved powers in relation to planning, energy efficiency and fuel poverty which it can use to take forward actions. For example, the Scottish Government could, if it so wished, give effect through its planning powers to the UK Committee on Climate Change's recommendation that no new homes should be connected to the gas network post 2025.

Similarly the GLA has high ambitions and a strong interest in the potential role of district heating.

As a CEG we are therefore disappointed in the level of ambition in Ofgem's proposals in relation to de-carbonisation for GD2. While there is flexibility for GDNs to propose bespoke ODIs, the tone of Ofgem's consultation is not encouraging and hence it is hard for us to press SGN to be more ambitious in this area when it is far from clear that proposals would secure Ofgem support. Ofgem seems to be assuming that nothing much needs to happen until the UK government has made its key decision, apart from providing evidence to support that. In practice changes will be happening through the GD2 period and it is vital that the GDNs are ready to respond and be proactive in anticipating the implications for their networks.

The Committee on Climate Change has set out clearly that it considers more emphasis needs to be put on blending renewable gas (biomethane) – upto 5% by 2030 – as a low regrets option. We want to see strong encouragement to the GDNs to do all they can to facilitate that. While the primary driver may be the level of RHI funding we know from the experience of renewable generators seeking to connect to the electricity distribution network that the attitude of the networks is also crucially important.

The stakeholder research that SGN has done shows strong support for action to support the future energy system. We also know that environmental action came out spontaneously in the deliberative events that SGN ran last year (coming through in the pre-work that consumers were asked to do about the areas they wanted to discuss), as a result of which it was added to their list of priority areas. The message from consumers was that they expected big companies like SGN to play their part in managing the environmental impacts of their own business. We have not yet seen the impacts of willingness to pay research that SGN are about to carry out and we are aware that keeping costs down is consumers' number one priority. However we are aware as a CEG that we need to think also about the interests of future consumers and hence will scrutinise any proposals carefully in terms of how SGN are achieving the appropriate balance.

On the flip side we are also pressing SGN to explore a full range of scenarios around the potential for reductions in gas demand over the GD2 period to minimise the risks of consumers having to pay for stranded assets in terms of unnecessary reinforcement, for example. The Scottish government has ambitious plans for energy efficiency and local authorities in Scotland are producing Local Heat and Energy Efficiency Strategies. BEIS has made significant funding available for district heating projects and the GLA already require all new developments to assess potential heat sources for district heating. We want to see SGN engaging with a broader set of local authority stakeholders to ensure they understand their ambitions in this space and to help them in shaping their plans as necessary.

Returning to Ofgem's proposals in this area it is not clear whether there would be a single clear ODI that could be proposed to capture the range of activity that could be needed. However the benefit of having some sort of an incentive is that it would encourage SGN throughout the GD2 period to find creative solutions to the issues as they arise in what will be a fluid landscape. We understand SGN are considering proposing a 'use it or lose it' allowance for de-carbonisation which we can see a case for, subject to understanding the scale of costs envisaged.

Another solution which we would strongly support would be to mirror the ET/GT arrangements by including this in the Business Plan Incentive and requiring annual reporting. Having a common approach across sectors would seem to be essential in an area such as this.

Q27 – Proposed outputs - Shrinkage / leakage

From an environmental perspective leakage of methane from the gas networks has historically been a major contributor to greenhouse gas emissions. Ofgem has acknowledged that the consultation is not as clear as it might be about the two separate incentives that currently exist around shrinkage (which is about cost) and leakage (which is about environmental impacts and where theft is not a relevant consideration). Both are important from a consumer perspective but they have different drivers.

We recognise that the repex programme has played a major role in reducing shrinkage / leakage but we understand that the incentive was intended to strip that out in the way the targets were set. If Ofgem has concerns with the methodology in the model then we would encourage them to address those issues directly rather than abandon having any financial incentive in this area.

Our understanding from SGN is that when they are considering asset management options under NOMs, for example, the CBA that they do will take account of the cost of gas lost through shrinkage and the carbon cost of leakage alongside potential risks around interruptions and the cost of emergency repairs etc. In making those business decisions it seems right that the cost of carbon equivalent is taken into account and having a leakage incentive is a way to get SGN to do that. We look to Ofgem to determine whether the modelling and baseline calculations are done correctly (and to ensure that the latest thinking on the impacts of methane as a more potent but shorter life emission are properly factored in).

Q29 – Outputs being removed - Biomethane Connections

Biomethane Connections

It seems to send completely the wrong message that this is being downgraded from a formal output with, going forward, nothing to drive performance in an area that is critical to de-carbonisation of gas through to 2030.

As indicated above we recognise that a quantitative incentive would be problematic as the interdependence with government policy on RHI could lead to it being out or under achieved. However the networks still have a critical role to play and can be a barrier or enabler. Learning the lessons from electricity, GDNs could produce heat maps to show where there is capacity, ensure their connection processes are accessible to people like farmers and provide them with tailored guidance and support. GDNs will have to think about how to cope with reverse flows on their networks and make them smarter as well as to understand and deal with gas of different specifications. We have heard from biomethane producers about the impacts of not being able to inject in summer months when pressures are low with the result that gas has to be flared off which is damaging to the environment and the reputation of the industry. Some small innovation projects are happening in this space but would need funding to roll out. In rural Scotland biomethane could be tankered in from areas not connected to the gas network with a question around what role if any SGN should play in that.

We are not advocating these specific actions (at least not at this stage) but are presenting them to give a flavour of the sorts of things that we would like SGN to have an incentive to think about – and to continue to think about – through GD2.

Carbon footprint reporting

For GDNs Ofgem is proposing to drop the requirement for carbon footprint reporting while for ET/GT it would be subsumed into a broader annual environmental report which makes more sense. While we recognise that the internal actions SGN can take are small compared to the savings from tackling heat de-carbonisation we do not think it is right for the company to be able to disregard that (given consumer views) and we see benefits in common reporting across all sectors.

To be effective as a reputational incentive we do see value in something that brings companies together with an expert panel or potentially making use of the CEG chairs to review performance. Sharing best practice should be an important element of this.

We recognise that there can be value in linking to broader industry standards and benchmarks and are aware that the BEIS streamlined Energy and Carbon Reporting will extend reporting obligations beyond quoted companies. However we believe that there could still be opportunities to build on these to provide some standard sector metrics and to present information in a readily accessible format to consumers and local stakeholders.

In terms of the practical actions that are open to the companies we have encouraged SGN to continue to look at options for their fleets for example (where suitable options may not currently be available but could become so during GD2). Services tendered by networks could have stipulated environmental standards attached.

Of course there will be limits on how much companies should be spending in this space but again technology and customer attitudes can shift rapidly (think single use plastics) and consumers would expect companies actions to reflect this. Some form of reporting requirements would help shine a light on their performance in this area which consumers increasingly care about.

Discretionary Reward Scheme

As noted above we are concerned about the loss of the environmental aspects of this incentive (while noting that the vulnerability aspects are to be covered by at least a reputational incentive).

As indicated above we believe that there would be real benefits in some sort of reputational incentive to encourage ambition and sharing of best practice in an area of increasing concern to consumers. Ideally this would be linked to cross-sector reporting as proposed for ET/GT.

Other environmental outputs

Although not mentioned in Ofgem's consultation, we note from previous Ofgem RIIO GD1 reports that there were other environmental outputs included in GD1 around land contamination, use of virgin aggregate and spoil to landfill. While we understand that Ofgem is looking to simplify the arrangements going forwards and that these may well not justify being considered outputs in future they remain potentially important and are examples of the sorts of things that could be included in an annual environmental report as proposed above.

Q30: Relevance of ET/GT proposals

One solution as envisaged for ET (and probably GT) is for the Business Plan Incentive to reflect the extent to which companies' plans are ambitious in this area with companies then having to produce annual environmental reports to show how their approach is evolving and what actions they are taking (including BCF reporting). If this is seen as the right approach for ET/GT we can see no reason

why it should not also apply to the GDNs with real merit in there being a standard approach across sectors to help stakeholders get a full picture.

While Ofgem seems concerned that reputational incentives through reporting have had limited impact to date, the answer would seem to be to work out how to improve them rather than simply to drop them. Similarly we recognise the concerns with discretionary reward schemes like the DRS but are aware that incentives of some form are needed to get companies to invest. Ofgem are proposing getting rid of the DRS and replacing it for vulnerable customer activity with a 'use it or lose it' allowance but with nothing replacing it on the environmental side.

There is a real opportunity here for creative approaches to how best to incentivise outcomes that are harder to quantify and / or not wholly under the companies' control. It is not clear that bespoke arrangements are the right answer given that the ability to compare and contrast across GDNs is likely to be important in getting them to push the boundaries. As such we would encourage Ofgem to put in place some sort of over-arching incentive in this area as planned for ET /GT.

Q31 – De-carbonisation of heat

Evidence to support government's decision

We agree with Ofgem's approach of supporting innovation projects to provide evidence to support a major decision on the future of heat in the 2020s.

It is right that there is network funding for this as evidence is needed on the impacts on the networks. Wider innovation activity should be funded through taxation rather than consumer bills given the regressive nature of bill funding.

We do have a concern however around how to ensure the objectivity of the evidence from GDN led trials when what is at stake is their core business (rather than how to run it more efficiently). Involving academic partners can help but is not a panacea. We encourage Ofgem to ensure suitable arrangements are in place to address this.

Handling uncertainty

In talking about low or no regrets options Ofgem seems to particularly have in mind additional expenditure that would "future proof" the network, where the costs are limited or the expenditure would be required in a range of futures. We agree such expenditure should be considered depending on the costs involved and the overall business case.

However what we are also challenging in relation to SGN's thinking, but does not seem to feature in Ofgem's consultation, is how GDNs should assess ongoing asset management options in the face of this uncertainty. In many cases GDNs will have choices between repairing and replacing assets, where a repair may have a shorter life and be less cost effective in the long term but avoids the risk of asset stranding. We understand that in GD1 Ofgem specified a payback period as a way of dealing with that uncertainty – and we would welcome any guidance from Ofgem on whether it considers that still to be appropriate for GD2. We are also keen to understand whether – in the event it was a viable option – it would be acceptable for GDNs to invest in energy efficiency as an alternative to reinforcement for example.

Chapter 5: Maintain a Safe and Resilient Network

Q33 – Overall package

The CEG is comfortable that a monetarised risk approach is, in principle, the right track to go down. However, we have concerns that companies may not yet be ready to fully deploy this approach, where data is weak, inconsistent, or uncomprehensive. We expect an element of judgement will continue to be necessary during the next period in undertaking works to keep the network safe.

Our main concern is that companies develop an approach to cost benefit analysis which fully embraces benefits to the customer and community. We are not convinced that there is yet a 'level playing field' in comparing different types of service or repair/replacement project, which would demand a more robust CBA for each asset type. While we understand Ofgem's rationale for setting a payback period (eg the 16-year calculation regarding replacement) – it is unclear if this one-size-fits-all approach is really helpful. In reality there are different life cycles and different options available for different assets and services.

The approach taken to CBA is central to which projects get included in the Business Plan and we would like to see further guidance from Ofgem as soon as possible on any requirements they may have about how this should be carried out. As noted below this is particularly important given the uncertainty around the future of the gas networks and the implications this has for tradeoffs between repairing and replacing assets.

In general, the CEG does not see itself (or consumers / stakeholders generally) as best placed to judge the merits of safety driven changes – or cyber / physical security issues. The standards should be set by the relevant authorities (eg HSE, BEIS). However we will challenge SGN where it has options for how these standards are met which can bring in other considerations including, for example, levels of customer disruption and the risks of asset stranding.

On a separate point we would like to see OFGEM recommending community benefit clauses in procurement processes and ensuing contracts, and adopting similar considerations in internally commissioned work.

(Q38) In terms of incentivization, we are happy to see priority given to service replacement of non-PE pipes given these are often in close proximity to properties and hence create a safety risk.

Q43 – GDN Record Keeping

We also think incentives should encourage better record-keeping and an open data approach which enables meaningful access for communities to information about services and properties. In particular we see an issue about data on mid and high-rise properties (6 and above storeys) which would benefit from renewed attention by companies, again with a commitment to meaningful data sharing with communities and partners.

General Comments on the CEG Role

We can see the value of the CEG 'system' and approach and think the creation and positioning of CEG structures are genuinely helpful in bringing customer voice into the planning by companies.

Throughout this document and the framework document Ofgem makes various references to areas where it expects the CEGs to challenge the GDNs thinking. As you are aware the make-up of our CEG includes strong consumer advocates as well as a number of us who have broader skills and experience. We see our primary role as ensuring the needs of consumers are reflected in SGN's business plan. As such we see ourselves as well placed to comment on any bespoke ODIs proposed (q6 of the framework consultation) and also to help in understanding how the interests of different groups of consumers and of current v future consumers might be weighed (q97/98 of the framework consultation).

Although no specific questions are asked in relation to our role in the GD consultation we would note that we feel we are best able to contribute in relation to how SGN are delivering against the three consumer outcomes that Ofgem has proposed (where we can test that what SGN is proposing is supported by the consumer and stakeholder evidence). On broader questions around innovation, competition, efficiency etc we will of course probe what SGN is doing (and for example are probing around their handling of uncertainty as highlighted above) but remain dependent on Ofgem's greater resources and ability to compare across the companies to provide a full challenge in these areas.

In addition to these roles, we also see a gap in relation to how strategic and policy issues are considered at an industry level. Going forward Ofgem should consider the merits of a customer/stakeholder forum at a higher, more strategic level. We are aware, of course, of the CCG and CEG Chairs' group, but having a largely process-driven agenda (to date) we do not as yet see these fulfilling the type of role that is needed on a more ongoing basis. We would be happy to discuss this further.

Yours faithfully

Maxine Frerk

SGN CEG Chair