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Consultation

OPR Guidance Consultation January 2021			
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We are consulting on the guidance for the revised Operational Performance Regime (OPR). The regime financially incentivises DCC's performance in three main areas: system performance, customer engagement and contract management.

This consultation sets out our proposals relating to the OPR Guidance to enable implementation. This includes setting the performance levels and values for the system performance penalty mechanisms; and detailed processes for the customer engagement and contract management incentives. It also includes proposals for a transitional year to provide greater certainty to stakeholders around the implementation of the new regime.

To aid stakeholders in their response to our consultation, we have published the draft OPR Guidance, draft Terms of Reference and two draft directions to illustrate the implementation of our proposed options for the transitional year. We plan to publish the final version of these documents, taking account of stakeholder feedback, alongside the consultation decision in March 2021.

This document outlines the scope, purpose and questions of the consultation and how you can get involved. Once the consultation is closed, we will consider all responses. We want to be transparent in our consultations. We will publish the non-confidential responses we receive alongside a decision on next steps on our website at **Ofgem.gov.uk/consultations**. If you want your response – in whole or in part – to be considered confidential, please tell us in your response and explain why. Please clearly mark the parts of your response that you consider to be confidential, and if possible, put the confidential material in separate appendices to your response.

Any enquiries related to the text of this publication should be sent to Ofgem at:
10 South Colonnade, Canary Wharf, London, E14 4PU. Alternatively, please call Ofgem on 0207 901 7000.

Contents

Executive summary

The aim of the Operational Performance Regime (OPR) review is to optimise the financial incentives placed on Data Communications Company (DCC) to drive better performance. As a monopoly company it is important that DCC faces sufficient incentives to play its role well, delivering value for money and high quality services to support smart metering. This is key to ensure consumers are able to fully take advantage of the benefits of the smart meter rollout.

We became concerned, following DCC's submission of its performance under the OPR for the RY18/19 price control, that the OPR metrics may not be providing the best incentives to DCC. We asked stakeholders in our DCC Price Control RY18/19 consultation for their views on how the OPR could be modified and improved. All respondents, including DCC, agreed with our concerns and supported a review of the current OPR framework.

In May 2020 we published a consultation reviewing the OPR framework, setting out proposals to financially incentivise three areas: system performance, customer engagement and contract management. Respondents largely agreed with our proposals, and in October of that year we published our decision to implement the new OPR.

As part of our decision, we implemented a licence change to enable Ofgem to publish guidance, regarding the process, procedures and criteria of the OPR. This consultation sets out our proposals relating to the OPR Guidance to enable implementation. Accordingly, we have published a draft of the OPR Guidance alongside this consultation document[1].

Financial Incentive Areas

System Performance

We decided to financially incentivise DCC initially using three performance measures: service availability, prepayment and install and commission. Where relevant, these measures will be assessed by meter generation and region; and a new penalty mechanism applied for regional measures. In this consultation, we put forward proposals on setting the performance levels, as well as the X and Y values used in the penalty mechanisms.

[1] Draft OPR Guidance: www.ofgem.gov.uk/publications-and-updates/opr-guidance-consultation-january-2021

Customer Engagement

As part of the new OPR, we decided to implement a customer engagement incentive. This places a relatively small proportion of DCC's margin at risk against the quality of its customer engagement. Performance will be assessed based on qualitative submissions from both DCC and SEC panel, covering the timing and frequency of engagement; quality of information provided by DCC and the incorporation of customer views. This consultation proposes additional guidance around the criteria, as well as specific requirements upon the SEC Panel and DCC for preparing their submissions, including guidelines for the length and content.

Contract Management

As part of the new OPR, we decided to implement a contract management incentive. This places a relatively small proportion of DCC's margin at risk against the quality of its contract management and procurement activity. Performance will be assessed by an independent auditor using the National Audit Office Framework. This consultation proposes a detailed timeline and process for the audit, as well as our proposed scope. We have also published alongside this consultation the draft Terms of Reference[2] to be used to procure the auditor, on which we are seeking stakeholder views.

Transition Period

In our October decision, we set out our intention to consult on a transition period to provide greater certainty to stakeholders around the implementation of the new regime. This consultation sets out our proposals for two different approaches to a transitional year in RY21/22 for system performance; as well as as proposals to run a trial of the customer engagement and contract management incentives with no margin attached in RY20/21.

Next steps

This document sets out our detailed proposals in each of the above areas with consultation questions for each area. We welcome your views, and will consider them when we make our decision.

[2] Terms of Reference for an audit of DCC's contract management under the OPR: www.ofgem.gov.uk/publications-and-updates/opr-guidance-consultation-january-2021

Please send responses to smartmetering@ofgem.gov.uk by 11 February 2021. We will publish our decision in March 2021.

1. Introduction

1.1. DCC is the central communications body licensed to provide the communications, data transfer and management required to support smart metering. It is responsible for linking smart meters in homes and small businesses with energy suppliers, network operators and energy service companies. It is important that as a monopoly company DCC faces sufficient incentives to play its role well, delivering value for money and high quality services. This is key to ensure consumers are able to fully take advantage of the benefits of the smart meter rollout.

1.2. The Licence stipulates that DCC's Baseline Margin be put at risk each Regulatory Year under the relevant performance incentive regimes. These comprise the Baseline Margin Project Performance Schemes and the Operational Performance Regime (OPR). DCC's Baseline Margin is 100% at risk against these incentive regimes, with the majority at risk against the OPR. At present, the OPR focuses on a range of metrics measuring DCC's technical outputs to assess system performance.

1.3. In May 2020 we published a consultation reviewing the OPR framework, setting out proposals to financially incentivise three areas: system performance, customer engagement and contract management. Respondents largely agreed with our proposals, and in October of that year we published our decision to implement the new OPR.

What are we consulting on?

1.4. As part of our decision, we implemented a licence change to enable Ofgem to publish guidance, regarding the process, procedures and criteria of the OPR.

1.5. The OPR Guidance[3] is intended to be a comprehensive reference to the operation of the OPR, setting out the regime according to the licence, the direction and our October decision document. We have published the draft OPR Guidance alongside this consultation document.

[3] Draft OPR Guidance: www.ofgem.gov.uk/publications-and-updates/opr-guidance-consultation-january-2021

1.6. As highlighted in our October decision, there are some specific issues regarding implementation of the OPR that are set out in the OPR Guidance. This consultation sets out our proposals on these specific issues to seek stakeholder feedback.

Section 1: System Performance

1.7. The OPR Guidance sets out the formula to determine DCC's performance under each of the incentivised system performance measures, including the relevant penalty mechanism. We put forward proposals on setting the performance levels, as well as the X and Y values used in the penalty mechanisms.

Question 1: What are your views on our proposals for the level of MPL and TPL?

Question 2: What are your views on our proposals for the values of x and y?

Section 2: Customer Engagement

1.8. The OPR Guidance fully sets out the process and submission requirements for the customer engagement incentive. We propose additional guidance around the criteria, as well as specific requirements upon the SEC Panel and DCC for preparing their submissions, including guidelines for the length and content.

Question 3: Do you have any comments on the drafting of the OPR Guidance for the Customer Engagement Incentive?

Question 4: What are your views on the proposed submission requirements?

Section 3: Contract Management

1.9. The OPR Guidance fully sets out the process for the auditor assessment under the contract management incentive. We propose a detailed timeline, process and scope for the audit. We also invite views on the draft Terms of Reference[4] to be used to procure the auditor, which is published alongside this consultation.

Question 5: What are your views on the timeline and process for the auditor assessment?

Question 6: What are your views on the scope of the assessment?

Question 7: What are your views on the draft Terms of Reference?

Section 4: Transition Period

1.10. This section sets out our proposals for two different approaches to a transitional year for system performance in RY21/22. As part of these proposals, we are inviting views on the draft direction, which would be required to implement each respective option. In addition, we propose to run a trial of the customer engagement and contract management incentives with no margin attached in RY20/21.

Question 8: What are your views on the proposed 6 month grace period (option 1)?

Question 9: What are your views on the direction required to implement the 6 month grace period (option 1)?

Question 10: What are your views on the proposed 1 year grace period (option 2)?

Question 11: What are your views on the direction required to implement the 1 year grace period (option 2)?

Question 12: Which is your preferred approach to the system performance transition year, option 1 or option 2?

Question 13: What are your views on the customer engagemnt and contract management trial run?

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[4] Terms of Reference for an audit of DCC's contract management under the OPR: www.ofgem.gov.uk/publications-and-updates/opr-guidance-consultation-january-2021

Section 5: Impact Assessment

1.11. This section sets our assessment of the impacts of the revised OPR. It recaps our rationale and analysis that was set out in the 2016 consultation that first introduced the OPR, as well as our analysis for the revised regime set out in the May 2020 consultation. It draws together our assessment of expected and potential unintended impacts on DCC's performance; impacts on DCC's margin at risk; costs to DCC customers and the regulatory burden of our proposals.

Related Publications

Draft OPR Guidance January 2021: www.ofgem.gov.uk/publications-and-updates/opr-guidance-consultation-january-2021

Decision on DCC Operational Performance Regime Review October 2020: https://www.ofgem.gov.uk/system/files/docs/2020/10/dcc_operational_performance_regime_review_-_october_2020_decision.pdf

Consultation on DCC Operational Performance Regime Review May 2020: https://www.ofgem.gov.uk/system/files/docs/2020/05/opr_review_consultation.pdf

DCC Operational Performance Regime Working Paper March 2020: https://www.ofgem.gov.uk/publications-and-updates/dcc-operational-performance-regime-working-paper

Decision on increasing the revenue at risk against the OPR January 2021: www.ofgem.gov.uk/publications-and-updates/decision-increasing-dcc-s-revenue-risk-against-opr

Consultation on increasing the revenue at risk against the OPR October 2020: https://www.ofgem.gov.uk/publications-and-updates/consultation-increasing-dcc-s-revenue-risk-against-operational-performance-regime

2018/19 Price Control Decision: https://www.ofgem.gov.uk/publications-and-updates/dcc-price-control-decision-regulatory-year-201819

2018/19 Price Control Consultation: https://www.ofgem.gov.uk/system/files/docs/2019/10/dcc_price_control_consultation_-_regulatory_year_2018-19.pdf

Decision on DCC's Operational Performance Regime September 2017: https://www.ofgem.gov.uk/system/files/docs/2017/09/1._decision_on_dcc.pdf

Consultation on the implementation of the Operational Performance Regime June 2017: https://www.ofgem.gov.uk/system/files/docs/2017/06/consultation_on_the_implementation_of_the_operational_performance_regime.pdf

DCC Operational Performance Regime: Principles and Objectives March 2016: https://www.ofgem.gov.uk/system/files/docs/2016/03/dcc_operational_performance_regime_principles_and_processes.pdf

Consultation stages

1.12. The key dates of the consultation are set out below in figure 1.1.

Figure 1.1: Consultation stages

Consultation open	Consultation closes (awaiting decision). Deadline for responses	Responses reviewed and published	Consultation decision/policy statement
11/01/2021	**11/02/2021**	**February 2021**	**March 2021**

How to respond

1.13. We want to hear from anyone interested in this consultation, but in particular DCC's customers. Please send your response to the person or team named on this document's front page.

1.14. We've asked for your feedback in each of the questions throughout. Please respond to each one as fully as you can.

1.15. We will publish non-confidential responses on our website at www.ofgem.gov.uk/consultations.

Your response, data and confidentiality

1.16. You can ask us to keep your response, or parts of your response, confidential. We'll respect this, subject to obligations to disclose information, for example, under the Freedom of Information Act 2000, the Environmental Information Regulations 2004, statutory directions, court orders, government regulations or where you give us explicit permission to disclose. If you do want us to keep your response confidential, please clearly mark this on your response and explain why.

1.17. If you wish us to keep part of your response confidential, please clearly mark those parts of your response that you *do* wish to be kept confidential and those that you *do not* wish to be kept confidential. Please put the confidential material in a separate appendix to your response. If necessary, we'll get in touch with you to discuss which parts of the information in your response should be kept confidential, and which can be published. We might ask for reasons why.

1.18. If the information you give in your response contains personal data under the General Data Protection Regulation 2016/379 (GDPR) and domestic legislation on data protection, the Gas and Electricity Markets Authority will be the data controller for the purposes of GDPR. Ofgem uses the information in responses in performing its statutory functions and in accordance with section 105 of the Utilities Act 2000. Please refer to our Privacy Notice on consultations, see Appendix 4.

1.19. If you wish to respond confidentially, we'll keep your response itself confidential, but we will publish the number (but not the names) of confidential responses we receive. We won't link responses to respondents if we publish a summary of responses, and we will evaluate each response on its own merits without undermining your right to confidentiality.

General feedback

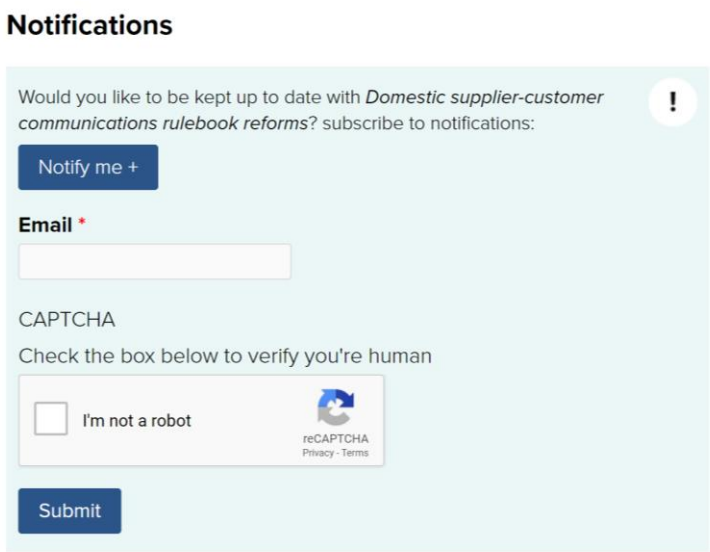
1.20. We believe that consultation is at the heart of good policy development. We welcome any comments about how we've run this consultation. We'd also like to get your answers to these questions:

1. Do you have any comments about the overall process of this consultation?
2. Do you have any comments about its tone and content?
3. Was it easy to read and understand? Or could it have been better written?
4. Were its conclusions balanced?
5. Did it make reasoned recommendations for improvement?
6. Any further comments?

Please send any general feedback comments to stakeholders@ofgem.gov.uk

How to track the progress of the consultation

You can track the progress of a consultation from upcoming to decision status using the 'notify me' function on a consultation page when published on our website. Ofgem.gov.uk/consultations.



Once subscribed to the notifications for a particular consultation, you will receive an email to notify you when it has changed status. Our consultation stages are:

Upcoming ▶ Open ▶ Closed (awaiting decision) ▶ Closed (with decision)

2. System Performance

Section summary

This section sets out our proposals for the OPR Guidance for the system performance incentives. It includes setting the levels of MPL and TPL, as well as the values of X and Y to be used in the penalty mechanisms.

Question 1: What are your views on our proposals for the level of MPL and TPL?

Question 2: What are your views on our proposals for the values of x and y?

Background

2.1. System performance measures the reliability of DCC systems, which is fundamental for the successful delivery of the smart meter rollout and business-as-usual operations.

2.2. In May 2020 we consulted on whether to financially incentivise four areas under system performance using the SEC performance measures, with each measure weighted 25% against the margin at risk. We also consulted on assessing the applicable metrics by meter type and region, as well as a new penalty mechanism. Stakeholders responded largely in favour of our proposals, and in October 2020 we published our decision to financially incentivise system performance.

2.3. We decided to incentivise five system performance measures: service availability, firmware management, install and commission, prepayment, and change of supplier. As of RY21/22, service availability, install and commission and prepayment will each hold a 33.3% weighting, while firmware management and change of supplier will hold a 0% weighting.

2.4. In addition, we decided to measure performance, where relevant, by meter generation (SMETS1, SMETS2) and assess performance separately across the three DCC communication service regions (north, central and south) for SMETS2 meters.

2.5. Finally, we decided to establish a new penalty mechanism, which would allow for poor performance in a single region to result in a penalty of 50% of the total margin.

2.6. In the OPR Guidance, we have set out more technical detail around the system performance measures, how they will be measured and the applicable penalty mechanisms. Below we have set out our rationale for the setting of the performance levels (MPL and TPL), as well as the values of X and Y to be applied in the penalty mechanisms.

Minimum and Target Performance levels

2.7. The Target Service Level (TSL) and Minimum Service Level (MSL) are both set by the SEC Panel in line with their expectations of the service required from DCC at the minimum and target level for the SEC performance measures.

2.8. The Target Performance Level (TPL) is where DCC retains 100% of its margin and the Minimum Performance Level (MPL) is where DCC retains a certain proportion of its margin (70% in the current OPR regime).

2.9. In the OPR Guidance, we propose to set the MPL equal to the MSL; and TPL equal to the TSL. This means that the MPL and TPL will be set at the same levels as the MSL and TSL as set out in the SEC.

2.10. This approach is consistent with the current OPR. We believe DCC's customers are best placed to determine the level of service that DCC should be incentivised to reach. In particular, as the costs of improvements to DCC's service will be passed on to DCC's customers, we consider it important to ensure the preferences of DCC's customers – and any trade-offs between performance and costs - are reflected in the OPR.

2.11. Table 2.1 shows the SEC Performance level values for TPL and MPL, aligned with the TSL and MSL as set out in section H13 of the SEC[5].

[5] The updated SEC section H - setting out the new performance measures - can be viewed on the SEC website: https://smartenergycodecompany.co.uk/modifications/operational-metrics/

Table 2.1: SEC Performance Level Values (TPL, MPL)

Performance measure	TPL	MPL
Service Availability	99.5%	98.0%
Firmware Management	99.0%	96.0%
Install & Commission	99.0%	96.0%
Prepayment	99.0%	96.0%
Change of Supplier	99.0%	96.0%

Setting the Value of Y

2.12. The value of Y determines the margin DCC retains at the MPL. In the previous OPR, this was set at 70%. Note the value of Y is consistent across all measures.

2.13. We are considering whether to maintain Y at 70% in the new OPR, or whether it would be more appropriate to decrease the value of Y to a minimum of 50%.

2.14. Maintaining Y at 70% would be consistent with the current OPR. This aims to provide a strong incentive for DCC to perform at least at the MPL.

2.15. Setting Y to 50% would reduce the amount margin retained at MPL. This would provide a lesser incentive for DCC to reach the MPL, while proving a stronger incentive to reach the TPL, or at least a greater marginal incentive on DCC to improve its performance from MPL to TPL.

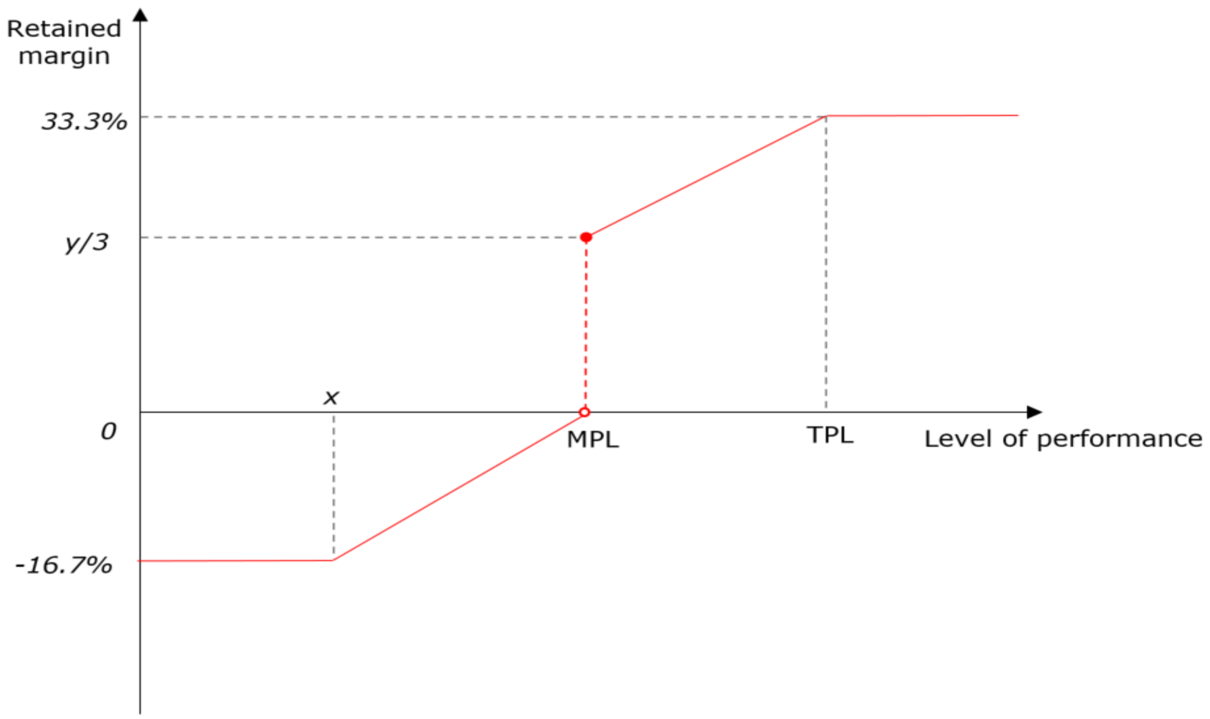
2.16. In our view, whether Y is best set at 70%, 50% or a value in between, depends on what the MPL and TPL represent (and by extension MSL and TSL). For instance, if MPL was intended to be the minimum acceptable level of performance, then we would consider that 50% may be the most appropriate value for Y. Whereas, if MPL represented what could still be considered as good performance, than 70% may be the more appropriate value. We are particularly keen to understand the views of DCC’s customers on this point.

Setting the Value of X

2.17. The value of X is only required in penalty mechanism B, which is used to determine retained margin for measures with a regional breakdown. As such, there is no precedent for the value of X in the old OPR.

2.18. The value of X determines the performance level at which DCC's retained margin in a region reaches its lowest negative point at -16.7%. This is demonstrated in figure 2.1.

Figure 2.1: Penalty Mechanism B: visualisation of the x value



2.19. We considered that we should set the distance between X and the MPL in proportion to the distance between the MPL and TPL. We therefore considered three main options:

2.19.1. Set X as half the distance between MPL and TPL;

2.19.2. Set X as equal to the distance from MPL and TPL;

2.19.3. Set X as double the distance between MPL and TPL.

2.20. Setting X at the half the distance between MPL and TPL results in a very steep gradient, and ensures DCC reaches the lowest negative point for the highest level of performance from the three possible options. This would serve to represent that performance below MPL is unacceptable. We consider that this is already represented by the vertical drop from the value of Y to 0.

2.21. Alternatively, setting X as double the distance between MPL and TPL would result in a shallower gradient, and ensures DCC reaches the lowest negative point at the lowest level of performance from the three possible options. We consider that this option has the primary benefit of ensuring a marginal incentive on DCC to improve its performance over the widest range of performance.

2.22. Setting X at equal to the distance between MPL and TPL would be a middle option. This would ensure DCC faced a marginal incentive to improve performance over a wider range of performance than if X was set at half the distance between MPL and TPL, but not as wide a range of performance compared to setting X at double the distance between MPL and TPL.

2.23. Given the benefits of the marginal incentive, our minded-to position is to set X as double the distance between MPL and TPL.

3. Customer Engagement

Section summary

This section sets out our proposals for the OPR Guidance on the Customer Engagement Incentive. It includes additional guidance for the assessment criteria and assessment process; specific requirements upon the SEC Panel and DCC in preparing their submissions; and guidance on the required format for the submission.

Question 3: Do you have any comments on the drafting of the OPR Guidance for the Customer Engagement Incentive?

Question 4: What are your views on the proposed submission requirements?

Background

3.1. We want to see DCC's decisions strongly informed by an understanding of its customers' needs, replicating the pressures a company would experience in a competitive market to drive better value for money. At the time of publishing this consultation - while DCC has demonstrated recent improvements in customer engagement - we continue to hear concerns from DCC customers that engagement around both its decision-making processes and wider informative engagement has not been sufficiently transparent, timely or relevant.

3.2. In May 2020 we consulted on whether it would be appropriate to financially incentivise DCC's customer engagement as part of the revised OPR regime. Stakeholders responded largely in favour of our proposals, and in October 2020 we published our decision to implement a financial incentive.

3.3. To assess DCC's customer engagement activity, we decided we would carry out a qualitative assessment process. This process requires DCC to prepare a submission setting out DCC's assessment of its performance during the previous Regulatory Year against a defined set of assessment criteria. The SEC Panel will also prepare a submission, ensuring that DCC customers can feed in views toward the submission's preparation. These submissions will then be provided to Ofgem for us to consult on, and subsequently make a decision.

3.4. We decided upon the final assessment criteria in our October Decision[6] following input from stakeholders. The assessment criteria cover three areas of DCC's customer engagement: 'Timing and frequency of engagement', 'Quality of information provided by DCC', and 'Taking account of customer views'. These criteria are included in full in the OPR Guidance.

3.5. Finally, we decided DCC would be assessed against a four-point scoring framework from 0-3 for each assessment question. A weighted average of the assessment question scores would then produce the final score. This scoring framework is contained within the OPR Guidance.

3.6. In the OPR Guidance, we have set out specific requirements upon the SEC Panel and DCC for preparing their submissions, and additional clarification on the evidence we may expect to see. We have set out our proposals for the requirements of the submission, including guidelines for the length and content. We have also provided further information on the types of supporting evidence that could be provided alongside the submission. We are seeking stakeholder views on these points as part of this consultation.

Additional Guidance

3.7. In addition to the assessment criteria that we have decided upon, we propose to include additional explanation within the OPR Guidance document. We consider that the assessment criteria is a suitably clear framework. However, we believe it would also be helpful to provide additional context to ensure the DCC, the SEC Panel and relevant stakeholders have as full a view as possible of our expectations.

3.8. The additional guidance is included in the OPR Guidance document published alongside this consultation and is intended to be read in conjunction with the assessment criteria.

[6] Decision on the Operational Performance Regime Review October 2020: https://www.ofgem.gov.uk/publications-and-updates/dcc-operational-performance-regime-review-october-2020-decision

We have provided the additional guidance in Appendix 1 of this consultation for reference and are seeking views on the level of detail provided.

Submission requirements

3.9. We are consulting on our proposals for the requirements of the submissions from DCC and the SEC Panel. In our May consultation we set out our expectation that each submission would consist of a main document, setting out a score with a descriptive rationale for each assessment criterion, and supporting evidence to justify the suggested score. The proposed OPR Guidance provides additional information about the requirements for each part of the submission.

3.10. We have drawn on Ofgem's wider experience in engagement incentives, from the RIIO-1 Stakeholder Engagement Incentive[7] and the Discretionary Recovery Mechanism[8] from the Switching programme financial incentives, as well as wider research, in order to determine the requirements for the submissions.

3.11. Figure 3.1 outlines the proposed main components of the submissions.

Figure 3.1: Submission requirements

Part 1: Main submission	Part 2: Supporting Evidence
• The main narrative of the submission, describing DCC's performance over the previous year. • It should contain the minimum requirements detailed in the guidance.	• Supporting evidence to complement the submission. • This will consist of a number of case studies, and any additional evidence of DCC's engagement as relevant.

[7] See Decision on the stakeholder engagement incentive 2019-2020: Transmission and Gas: https://www.ofgem.gov.uk/publications-and-updates/decision-stakeholder-engagement-incentive-2019-20-transmission-and-gas; and Decision on the Stakeholder Engagement and Consumer Vulnerability Incentive 2019-20: Electricity Distribution: ofgem.gov.uk/publications-and-updates/decision-stakeholder-engagement-and-consumer-vulnerability-incentive-2019-20-electricity-distribution
[8] See Guidance for the Discretionary Recovery Mechanism (DRM) for DCC under the Design, Build and Test Phase of the switching programme: https://www.ofgem.gov.uk/system/files/docs/2019/05/drm_guidance_document_1.pdf

3.12. We consider that we should not be overly prescriptive over the format of the submission to allow flexibility in how DCC and the SEC Panel choose to prepare their submissions. We have concerns that setting strict requirements for the submission format could result in the incentive becoming a 'tick-box' exercise, which does not appropriately incentivise real improvements. We have instead set out several guidelines to provide a common structure for DCC and the SEC Panel to follow. This aims to ensure the two submissions follow a similar basic structure and format to allow a consistent assessment approach to be taken for both submissions, without being too restrictive.

3.13. We propose that the main submission should consist of up to thirteen pages, and have provided suggested page counts for the answer to each criteria question. We consider that this would be an appropriate length to allow a comprehensive narrative against each criteria, but not produce an overly onerous burden upon DCC, the SEC Panel, Ofgem, and DCC customers in carrying out the submission preparation and assessment process.

3.14. We have suggested in the OPR Guidance that DCC and the SEC Panel should consider allocating no more than one page per criteria question for 'Timing and frequency of engagement' and 'Quality of information provided by DCC', and two pages per question for 'Taking account of customer views', due to their respective weighting. This will ensure the submissions do not limit the amount of detail, which could be provided for questions that carry greater weighting and therefore correspond to a greater percentage of DCC's margin.

3.15. We have also proposed that a number of case studies should be provided alongside the main submission. These case studies should provide the opportunity to follow DCC's engagement over a particular activity from start to finish, providing a more complete view of how DCC engages over an activity's progression. We propose to limit the number of case studies to five. We consider this will ensure enough cases can be chosen to demonstrate DCC's engagement over a range of activities, whilst not being excessive.

3.16. Finally, we have provided further information on the types of additional supporting evidence that could be provided alongside the main submission. We also propose to require that any additional evidence is referenced within the main submission or case studies. While we have not provided a restriction on the amount of evidence that could be provided, we propose that any additional evidence must be referred to either within the submission or the case studies. This will ensure that any additional evidence would be provided to support the arguments given in the submission, and its provision is justified. We believe this will enable an effective assessment to be made of the submissions overall.

3.17. We may make further amendments to the submission requirements as set out in the OPR Guidance if it becomes apparent that a more prescriptive approach is necessary following the trial of the customer engagement incentive.

Assessment Process

3.18. We set out in our May consultation that all aspects of DCC activity would be within scope of the Customer Engagement Incentive and we consider it is helpful to include this explicitly in the OPR Guidance. We have set out that we will take the type of activity into account, and any resulting constraints, when making our assessment. This is to ensure DCC is not unfairly penalised for circumstances outside of its control, whilst still ensuring customer engagement is embedded in DCC processes across the full breadth of its activity.

3.19. We have proposed that DCC and the SEC Panel must be transparent with one another and share drafts of their submissions when preparing them. This requirement will allow DCC to respond to points raised in the SEC Panel's submission, and vice versa, therefore helping to ensure the two submissions will be comparable. We consider that this will ensure balanced submissions are provided, and allow a consistent assessment approach to be taken.

3.20. Maintaining transparency will also ensure DCC has early sight of the submission from the SEC Panel and can make any necessary changes to its processes at an early stage of the next Regulatory Year. We are of the view that this will allow DCC to demonstrate continuous improvement.

4. Contract Management

Section summary

This section sets out our proposals for the OPR Guidance on the Contract Management Incentive. This includes setting out detailed proposals on the timeline and process for the contract management audit, as well as the scope of the assessment.

We also invite stakeholder views on the Terms of Reference, which has been published alongside this document.

Question 5: What are your views on the timeline and process for the auditor assessment?

Question 6: What are your views on the scope of the assessment?

Question 7: What are your views on the draft Terms of Reference?

Background

4.1. DCC was appointed using an outsourced service model, to manage contracted smart metering service providers. As such, external costs compose the largest proportion of DCC's costs, and it is critical that these contracts are entered into, managed and closed out effectively and efficiently. Proactive, best in class contract management and procurement have the potential to deliver real benefits to DCC customers and the consumer.

4.2. As of the publication of this consultation, not all of DCC's service providers are performing at the level expected by DCC. We outlined our concerns around DCC's contract management and procurement processes in both our 18/19 and 19/20 price control consultations[9]. Given the size and volume of DCC's contract portfolio, and that several

[9] See price control consultations for RY19/20 and RY18/19.

original service provider contracts will require extension, it is important that DCC increases focus on this area in the coming years.

4.3. In May 2020 we consulted on whether it would be appropriate to financially incentivise DCC's contract management and procurement as part of the revised OPR regime. Stakeholders responded largely in favour of our proposals, and in October 2020 we published our decision to incentivise this area.

4.4. We decided to use an independent auditor to carry out the assessment. An auditor will be able to provide the required expertise, time, and resources in order to thoroughly assess DCC's contract management processes, whilst respecting any required commercial confidentiality arrangements.

4.5. In addition, we decided to use an adapted version of National Audit Office (NAO) Contractual Relationships Framework[10] as the assessment criteria. This framework sets out seven domains of assessment, which are applicable to DCC. We decided to modify two supporting questions of the framework to ensure they captured the SEC modification change process in the assessment. We have published this version of the NAO framework alongside this document for reference.[11]

4.6. Finally, we decided to use the three levels of attainment as defined in the NAO Framework as the scoring framework. Each supporting question will be given an attainment level, according to the criteria set out in the NAO framework. An overall performance score would then be produced using a simple average across all supporting questions.

4.7. In the OPR Guidance, we set out more detail on the timelines and process for the audit, as well as the scope of the assessment. We have also published the draft terms of reference to be used to procure the auditor. We are seeking stakeholder views on these as part of this consultation.

[10] NAO Contractual relationships framework: https://www.nao.org.uk/wp-content/uploads/2016/11/Framework-for-publication.xlsx
[11] Modified NAO framework: www.ofgem.gov.uk/publications-and-updates/opr-guidance-consultation-january-2021

Timeline and Process

4.8. In the OPR Guidance, we set out the following timeline for the annual audit cycle, further developing the process we set out in our May consultation:

- ***Setting the Terms of Reference (TOR) (Jan-March):*** Ofgem to publish the draft TOR in January to gather feedback from DCC, SECAS and wider stakeholders. Ofgem will incorporate this feedback and publish the final TOR in March. SECAS will use the TOR to produce materials in preparation for the tender.

- ***Appointment of the auditor (March-May):*** SECAS will run a competitive tender process on behalf of Ofgem, with Ofgem's approval over the final selection of the auditor. We expect the auditor to be appointed by the end of May. Initially, the auditor will be contracted for a three year period. The budget for the auditor contract will be set by SECAS.

- ***Evaluation (June-July):*** The independent auditor will then evaluate DCC's contract management and procurement activity using the NAO framework and the agreed terms of reference. The auditor will work closely with DCC during this assessment to enable access to the required evidence as well as speaking to a number of DCC user representatives and the SEC Panel, the latter in particular in regards to the SEC change process. The auditor will need to provide an interim report for DCC to comment on by **9 July.**

- ***Reporting (July-August):*** The independent auditor will submit a draft report to Ofgem by **23 July**, taking account of DCC's comments**.** This report will include the auditor's assessment on the level of attainment that DCC has reached for each supporting question and domain. Ofgem will review the report, and may request further iteration to ensure the report meets the requirements set out in the scope/terms of reference. The final report must be issued to Ofgem by **20 August**. Once the final report has been issued, Ofgem will confirm to SECAS that the work is complete. The full report will then be issued to Ofgem, DCC and BEIS, and a non-commercially confidential version of this report will be circulated to the SEC Parties and the Panel.

- ***Consultation (Oct-Dec):*** Ofgem will incorporate a summary of the auditor's report as part of the price control consultation, setting out the audit scores as part of Ofgem's minded-to position on DCC's performance under the OPR. Ofgem will then publish the price control consultation to provide an opportunity for all stakeholders to respond. In particular, this will provide an opportunity for DCC users, the SEC Panel and DCC to submit additional evidence to appeal the auditor's scoring.

- ***Decision (Jan-Feb):*** Ofgem will then consider responses and any additional evidence submitted by stakeholders. This may include further clarification with the auditor around the scores. Ofgem will then determine whether to make any adjustments and publish the final decision.

4.9. This proposed timeline intends to balance the need to gather wide stakeholder feedback around the Terms of Reference; provide sufficient time for the auditor to run an in-depth assessment of DCC; and DCC's need to have early sight of the auditor's report to begin making improvements to their contract management processes for the next regulatory year. In future years, once the auditor is already in place, we may amend these timelines with a view to ensure the auditor submits its final report to Ofgem on 31st July in line with DCC's price control submission.

4.10. As set out in the above timeline, we consider it most efficient to contract the auditor on a three year basis. This ensures that the contract is more attractive to potential bidders than a 1 year procurement, and ensures a more efficient use of resources in the procurement for both SECAS and Ofgem. We would ensure the contract provides for amending the scope of the audit on an annual basis, in case there is a need for changes based on DCC's activities or emerging areas of concern.

4.11. Finally, the timeline sets out our intention to publish a summary of the auditor's report as part of the price control consultation. This would give DCC and other stakeholders the opportunity to respond and submit further evidence, which we would then consider when making our final decision. This would serve as an appeals process to the auditor assessment within the price control, ensuring the process remains fair and transparent to all parties.

Scope of assessment

4.12. The assessment criteria in the modified NAO Framework cover DCC's activities in contract management, procurement and re-procurment. We consider it is important to assess DCC's activities in all three areas, but that there could be a significant trade-off between the breadth and depth of the assessment. We are of the view that the audit would be most effective with some limitations on the scope to allow for a more in-depth assessment in key areas of DCC's operation.

Contract Management

4.13. DCC’s contract management of its SMETS2 service providers remain a key concern to DCC’s customers, and we consider this should be a key focus of the audit. The OPR Guidance sets out that the auditor will provide a detailed review of DCC’s contract management of DCC’s Communication Service Providers - Arqiva and Telefonica – and Data Service Provider – CGI.

4.14. As a main driver of the increases in DCC’s external costs, we believe that the audit should give visibility over DCC’s performance in managing its SMETS1 service providers. However, in order to keep the scope of the audit manageable and as we view the performance of SMETS1 service providers as a lesser area of concern relative to SMETS2, we propose that the auditor should only assess the top tier SMETS1 contracts. As such, the OPR Guidance sets out that the auditor will assess DCC’s contract management of the three SMETS1 service providers that incurred the highest costs over the Regulatory Year.

4.15. We considered whether we should narrow the scope of SMETS1 other than by the value of the contracts. For example, we could specify SMETS1 providers where we had particular concerns. However, as at this stage we do not have concerns over the performance of specific SMETS1 providers, we are of the view that cost is an appropriate indicator as to where the auditor should focus. If specific concerns did emerge in later years, we may choose to amend the scope through following the process to amend the OPR Guidance.

4.16. Finally, the auditor will also assess DCC’s contract management in terms of adherence to the SEC modification change process. Considering the volume of Change Request/Project Requests, we consider it would be overly burdensome to assess each of these individually. Instead, we propose that the auditor should assess the effectiveness of the change process as a whole, but may draw on a sample of the Change Requests/Project Requests as evidence if appropriate.

Procurement and re-procurement

4.17. DCC's procurement activities over the next year will be focussed on DCC's Network Evolution programme[12]. As such, the OPR Guidance sets out the procurement of 4G Comms Hubs and Networks; re-procurement of the Data Services Provider (DSP) and Smart Metering Key Infrastructure (SMKI) as within the scope of assessment.

Activities excluded from scope

4.18. The OPR Guidance sets out that activity covered by Baseline Margin Project Performance Adjustment Schemes (BMPPAS) - or where BEIS intend to put one in place for upcoming regulatory years - will be excluded from the assessment. This is to avoid potential double jeopardy from incentivising DCC's contract management activities under both the project performance schemes and the OPR.

4.19. For RY20/21, this means that activity relating to Release 2.0 will be out of scope from the assessment.

Terms of Reference

4.20. Alongside this consultation, we have published a draft Terms of Reference[13] to be used in the procurement of the auditor. This document aligns with the contents of the OPR Guidance, and sets out the background and aims of the procurement; the timings and process of the audit; the assessment framework; required outputs from the audit; and sets out the scope.

4.21. We are seeking stakeholder feedback on the drafting and content of the Terms of Reference as part of this consultation.

[12] See page 41 of DCC's Business and Development plan: https://www.smartdcc.co.uk/media/4144/20143-dcc_report-and-plan_v8.pdf
[13] Terms of Reference for assessment of DCC's Contract Management and Procurement activities under the Operational Performance Regime: www.ofgem.gov.uk/publications-and-updates/opr-guidance-consultation-january-2021

5. Transition Phase

Section summary

This section sets out our approach to the implementation of the new OPR, ensuring sufficient transitional arrangements are in place to offer certainty to DCC and other stakeholders.

We put forward two options to implement either a six month or 1 year grace period for the system performance incentives. We also propose to run a trial of the customer engagement and contract management incentives without margin attached during RY20/21.

Question 8: What are your views on the proposed 6 month grace period (option 1)?

Question 9: What are your views on the direction required to implement the 6 month grace period (option 1)?

Question 10: What are your views on the proposed 1 year grace period (option 2)?

Question 11: What are your views on the direction required to implement the 1 year grace period (option 2)?

Question 12: Which is your preferred approach to the system performance transition year, option 1 or option 2?

Question 13: What are your views on the customer engagemnt and contract management trial run?

Background

5.1. In the implementation of any incentive regime, it is important that there is a balance between ensuring that the regulated company has the chance to retain 100% of margin under that regime, while ensuring they are sufficiently challenged to achieve good outcomes.

5.2. During our May consultation, DCC raised their concerns that our timeline for implementation did not provide sufficient time to trial each area of the incentive to understand their performance, and have the opportunity to make improvements, before margin was put at risk against the incentive.

5.3. From our own observations, we believe running a trial of the different incentives would be beneficial to ensure stakeholders – both SEC Panel and DCC - have the chance to become familiar with the different processes, and allow us to consider improvements, ahead of margin being put at risk.

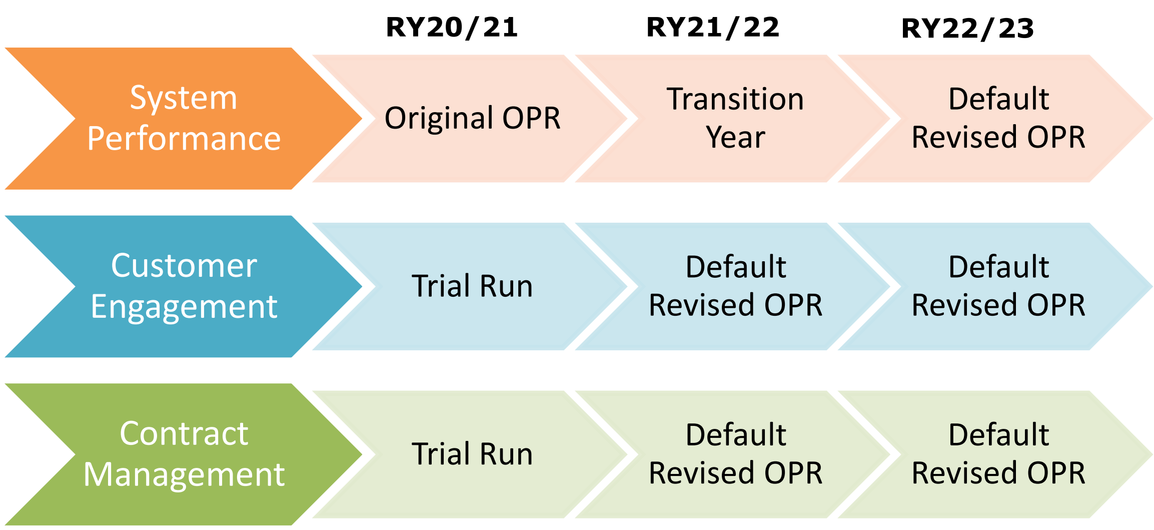
5.4. Therefore, in our October decision document, we set out our intention to consult on a transition phase to address DCC's concerns and provide greater certainty to stakeholders.

5.5. This section sets our proposals for potential transitional arrangements for each incentive area: system performance, customer engagement and contract management.

Overview

5.6. The OPR Guidance sets out that the nature of the Transition Phase will differ between System Performance, Customer Engagement and Contract Management. Figure 6.1 displays a timeline describing the transition phase for the three areas.

Figure 5.1: Transition Phase Timeline



5.7. We set out two options for the Transition Year for system performance in RY21/22; and our proposed approach to the Trial Run for customer engagement and contract management in RY20/21 below.

System Performance

5.8. The system performance measures to be used in the OPR are a subset of the SEC performance measures. In 2020, the SEC Operations Sub-Group (SEC Ops Group) reviewed the SEC performance measures to identify improvements and define new metrics that better measure system performance. The SEC modification bringing these measures into force was approved in October 2020[14].

5.9. DCC expect to be in a position to informally report on these measures using data generated by their Technical Operations Centre (TOC) by the end of April 2021, and intend to provide an annex to the Performance Measure Report on these measures to the SEC Ops Group in June. In order to report formally on these measures, DCC will need to consult on the Performance Measurement Methodology (PMM) with industry, which includes determining the approach to any exclusions. The exclusions are important to ensure that the measures only capture DCC's performance, excluding issues that are outside of DCC's responsibility, which may have a significant impact on whether DCC's performance would reach target performance levels. DCC expects to have fully completed this process by February 2022.

5.10. Given the long lead times to the implementation of the system performance measures, we expect DCC to have already begun to analyse their own performance and begin to implement improvements. This could include engagement with their service providers, and where necessary early scoping of negotiations for contract changes. In the case of contract changes, should these be judged necessary, on current timelines DCC anticipate that this would be completed mid-way through RY21/22.

5.11. Given the number of dependencies and level of uncertainty around the implementation of the system performance measures, we are of the view that it is reasonable to implement a transition period of up to a year, and propose in the OPR Guidance that the System

[14] A summary of this modification can be found on Smart Energy Code website: https://smartenergycodecompany.co.uk/modifications/operational-metrics/

Performance Transition Year would run in RY21/22. Note that the customer engagement and contract management incentives will run as normal in RY21/22 (we set out a trial run for these incentives in RY20/21 later in this chapter.)

5.12. We have set out two possible approaches below for this Transition Year for the system performance measures. We are keen to hear stakeholder views on both approaches, and the option they consider the most appropriate.

Option 1 - Six month grace period

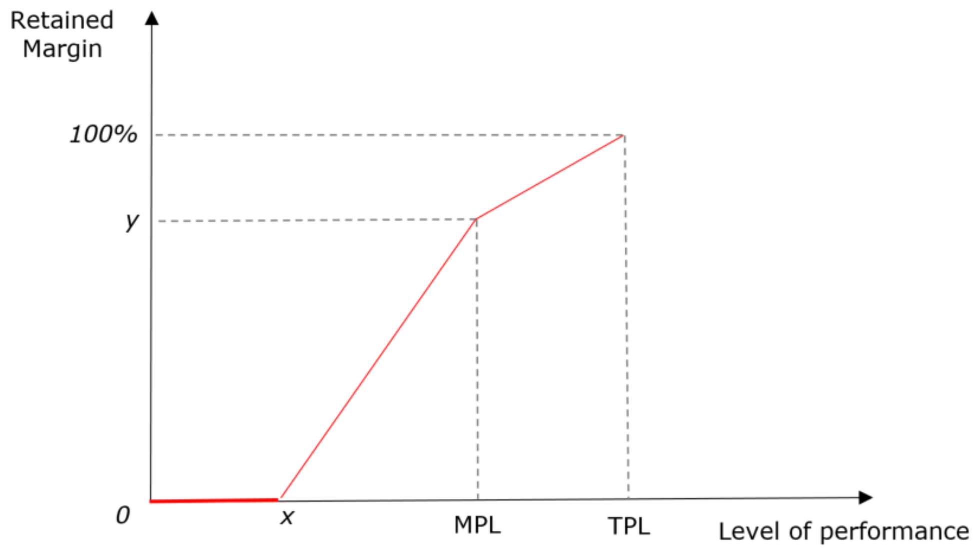
5.13. In this option, a grace period would be implemented for the first six months of the RY (April up to and including September). This would mean that DCC’s performance in any of the first six months would only contribute to its final RY21/22 performance, if the performance in that month improves DCC’s final RY21/22 performance score.

5.14. Effectively, this would mean DCC would not take on risk for the first six months of the RY. However, it increases the negative impact of below target performance in the second half of the year as 100% of the margin would be at risk for the remaining months (assuming DCC does not perform sufficiently in the first six months of the RY).

5.15. In addition, given that this will be the first year that DCC will be reporting on the new metrics, we consider it proportionate to adjust the penalty mechanisms to ensure DCC will not lose all margin for performance just below MPL, while still incentivising DCC to make improvements.

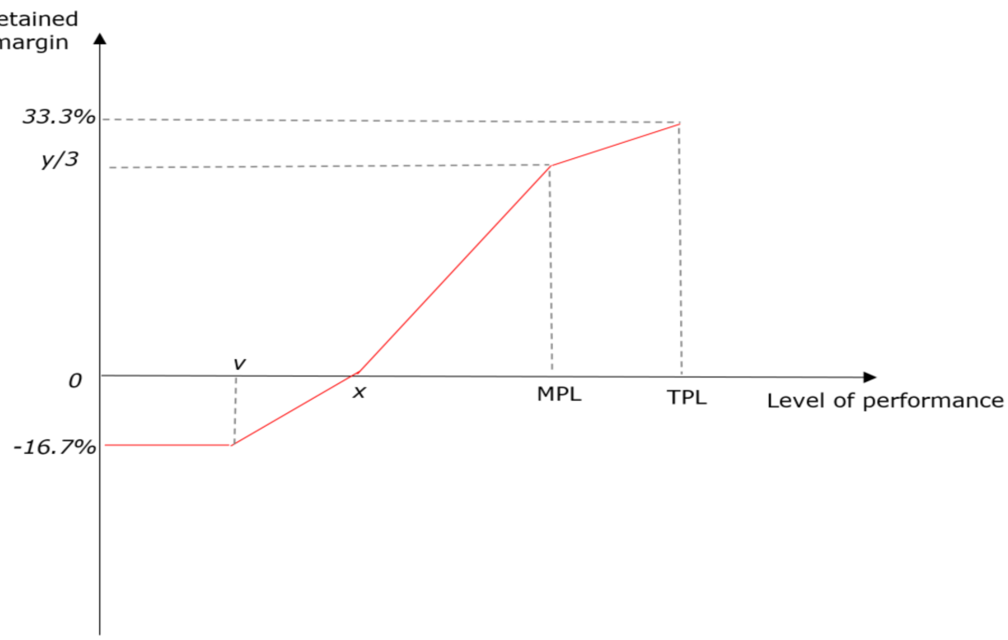
5.16. We have set out the adjusted penalty mechanisms for this approach in Figure 5.2 and 5.3.

Figure 5.2 – Adjusted Penalty Mechanism A



5.17. Penalty mechanism A – applicable to measures that are not reported by region – ensures that DCC will incrementally lose margin until DCC's performance reaches X, which is set at double the distance between MPL and TPL. For performance at or below X, DCC will retain 0% of margin.

Figure 5.3 – Adjusted Penalty Mechanism B



5.18. Penalty mechanism B – applicable to measures that are reported by region – ensures that DCC will incrementally lose margin for a given region until DCC reaches performance level X (set as in Penalty Mechanism A), where DCC will retain 0% of margin.

5.19. For performance below X, DCC's retained margin becomes incrementally negative until performance reaches level V, the value of which is also set at double the distance between MPL and TPL. The value of V determines the performance level at which DCC's retained margin in a region reaches its lowest negative point at -50%.

5.20. DCC expect to conclude their consultation process and agree the formal Performance Measure Methodology in February 2022. In this option, we would expect DCC to apply the formally agreed Performance Measure Methodology, including exclusions, retrospectively across their OPR reporting for RY21/22. DCC would then report on these measures to Ofgem at the end of July as part of the RY21/22 price control. As set out above, DCC's reporting in the first six months of the RY would only contribute to DCC's performance if it improves DCC's overall score.

5.21. The main advantage of this option is that it ensures DCC is incentivised under the new system performance measures in RY21/22. This would serve as a very strong incentive for DCC to make the improvements to their system performance that stakeholders wish to see as swiftly as possible.

5.22. It also gives the opportunity for DCC to view its performance and make improvements during the first half of the year, before being penalised for poor performance. DCC anticipates it would conclude contract changes mid-year in RY21/22, which approximately aligns with the end of the proposed grace period.

5.23. We consider that the main drawback of this approach is that, if DCC needed to make substantial changes to its performance to reach target levels, a six month grace period could be seen as relatively short.

5.24. If six months is not sufficient time for DCC to make any improvements needed to their performance to reach target levels, this has the potential to result in a large penalty to DCC during the first year of the new incentive regime. We have proposed the adjusted penalty mechanisms for the remaining six months to mitigate against the outcome that DCC loses 100% of its margin for performance just below MPL. Despite the softening of the penalty mechanisms, DCC will still face significant incentives to improve its performance over RY21/22 ahead of RY22/23.

5.25. In addition, this may result in DCC taking actions to implement rapid improvements to performance that could have been less costly if implemented over the course of a year. We are keen to hear from stakeholders whether they consider this a significant risk, and if so whether they consider it worthwhile to take on this risk.

Option 2 - One year grace period

5.26. An alternate option would be to provide DCC with a full year to report on the new performance measures without margin attached.

5.27. This would mean DCC would not be incentivised under the new measures for RY21/22, instead continuing to report and face incentives against the original OPR system performance measures for that year. The new system performance measures would come into force for RY22/23.

5.28. In this approach, 70% of DCC’s margin would be against the original OPR system performance measures for RY21/22, with the remaining 30% of DCC’s margin split evenly against the customer engagement and contract management incentives.

Table 5.1 – Performance measures and weightings for the one year grace period in RY21/22

Measure	Area of reporting	Metric	Weighting
SUM1	DCC service desk	Percentage of incidents resolved within Target Resolution Time	17.5%
SUM2a	Communication Hubs	Percentage of Communications Hubs delivered on time	8.75%
SUM2b		Percentage of Communications Hubs accepted by customers	4.375%
SUM2c		Percentage of Communications Hubs not faulty at installation	4.375%
SDM2	Core service requests	Percentage of service responses delivered within Target Response Time	17.5%
SDM3	Service/System Availability	Percentage availability of Data Service, User Gateway, Service Management System and Self Service Interface	17.5%
VMM1	Customer Engagement	Qualitative assessment of DCC's customer engagement based on submissions from DCC and SEC Panel	15%
VMM2	Contract Management	Auditor assessment of DCC's contract management and procurement activity based on the NAO Framework	15%

5.29. Note, we have dropped SDM1 – DCC WAN coverage - from the list of performance measures for the one year grace period, given that this measure was based on milestone dates in the CSP contracts, which have now expired. We propose spreading the margin that was against this measure across the other system performance measures for RY21/22.

5.30. We wish to hear from stakeholders whether they agree with the proposed list of measures for RY21/22, if there are any other measures we should consider removing, and whether stakeholders have any views on the proposed weightings between the measures.

5.31. In this approach, given that DCC will have already reported to the SEC Panel on the new system performance measures for a year without margin attached, we do not consider it necessary to make any adjustment to the penalty mechanisms for when the new performance measures will apply in RY22/23.

5.32. The main benefit of this approach is to allow DCC more time to assess the cost efficiency of improvements to their performance, through a full year of visibility over their performance ahead of margin being put at risk.

5.33. Our main concern with this approach is that DCC would face less incentive pressure during RY21/22, which could result in delays to DCC making improvements around its core operation. Outages and other network issues can have a real consumer impact, and as we expect high levels of consumers with SMETS2 meters in RY21/22, there is a risk of consumer detriment. This concern is in part mitigated by the fact DCC would still face incentives under the old OPR measures, as well as the new customer engagement and contract management incentives for RY21/22. We are keen to hear from stakeholders on the merits and risks of this proposal.

Directions for implementation of the transition period

5.34. In order to implement either approach, we would need to issue a new direction setting out the approach for RY21/22 and the approach for RY22/23 onwards.

5.35. For option 1, this would set out the formulae to implement the adjusted penalty mechanism for RY21/22. For option 2, this would set out the performance measures to be applied in RY21/22 and those for RY22/23 onwards.

5.36. We have published two draft directions alongside this consultation to illustrate how each option would be implemented. We have also set out the adjusted penalty mechanism formulas for option 1 in the draft OPR Guidance.

5.37. Note, as part of both draft directions, we have also made a small correction to note that the term XI is defined as part of the OPR Guidance.

Customer engagement & Contract management

5.38. In the OPR Guidance, we set out our proposal to implement a trial run of the customer engagement and contract management incentives during RY20/21. We intend both trial runs to replicate the process of the assessment as set out in the OPR Guidance.

5.39. For customer engagement, this would involve DCC and SEC Panel preparing a qualitative submission in line with the prescribed assessment criteria on DCC's customer engagement over RY20/21 to be sent to Ofgem by 31 July 2021. Ofgem would assess both submissions according to the scoring framework, and provide an indicative score and feedback on both submissions. Ofgem would report on this process as part of the price control consultation for that year, but margin would not be at risk.

5.40. For contract management, an auditor would assess DCC using the NAO Framework from May to July 2021. DCC would be provided with the auditor's interim report in July, followed by the final report in August. Ofgem would report on this process as part of the price control consultation for that year, but margin would not be at risk.

5.41. The main benefit of this approach is that it provides early visibility to DCC on their performance under each incentive, while ensuring full implementation for RY21/22. This means that DCC have the opportunity to make early improvements and will face financial incentives to make these improvements for RY21/22. This approach also provides certainty to DCC, SEC Panel and Ofgem on the processes for both incentives, and gives the opportunity for Ofgem to improve those processes before margin is at risk.

5.42. We considered whether it would be appropriate to run a trial period for customer engagement and contract management in RY20/21, but then only implement the incentives with margin attached for RY22/23. This would provide DCC with a full RY to make improvements following sight of their indicative scoring. However, as both customer engagement and contract management are priority areas of concern for both Ofgem and DCC's customers, we consider it important that DCC faces strong incentives to make improvements in this area as swiftly as possible. We consider pushing back implementation of these incentives another year would risk DCC delaying actions that would improve their performance.

6. Impact Assessment

Section summary

This section sets our assessment of the impacts of the revised OPR. It recaps our rationale and analysis that was set out in the 2016 consultation that first introduced the OPR, as well as our analysis for the revised regime set out in the May 2020 consultation and the October 2020 decision.

It draws together our assessment of expected and potential unintended impacts on DCC's performance; impacts on DCC's margin at risk; costs to DCC customers and energy consumers; and the regulatory burden of our proposals on DCC and SEC Panel.

Introduction of the OPR

6.1. In 2016, we published two consultations[15][16] to populate - through a direction - the OPR framework that had been set out by BEIS in the licence[17].

6.2. When drafting the DCC licence, BEIS recognised the need for incentives. As a monopoly, DCC is not subject to competitive pressures, which drive effective performance for a high quality service. In the absence of these competitive pressures, incentive-based regulation can be used to ensure that DCC is responsive to the needs of its users and delivers good consumer outcomes.

6.3. As such, the licence stipulates – since it was awarded in 2013 - that the amount at risk against these incentives each regulatory year should not be less in total than 100% of the value of DCC's Baseline Margin. DCC's Baseline Margin was agreed as part of Licence

[15] DCC Operational Performance Regime: Principles and objectives: https://www.ofgem.gov.uk/system/files/docs/2016/03/dcc_operational_performance_regime_principles_and_processes.pdf
[16] DCC Operational Performance Regime: final proposals: https://www.ofgem.gov.uk/system/files/docs/2016/11/dcc_opr_final_proposals_0.pdf
[17] See licence condition 38 of the Smart Meter Communications licence: https://epr.ofgem.gov.uk/Content/Documents/Smart%20DCC%20Limited%20-%20Smart%20Meter%20Communication%20Consolidated%20Licence%20Conditions%20-%20Current%20Version.pdf

Application process, but can be adjusted via an annual application submitted by DCC as part of the annual price control process. In RY18/19 – the first year of the OPR – the amount of Baseline Margin at risk was £5m, compared to £67m of internal costs.

6.4. Following consultation, we decided to introduce a regime that incentivised DCC's system performance. This measured the reliability of DCC's network through five groups of quantitative metrics: DCC Service Desk, Communication Hubs, DCC WAN Coverage, Core Service Requests, and System Availability.

6.5. As a downside only incentive scheme, if DCC reached the target performance levels for a metric, then DCC would retain all margin that was at risk against that metric. If DCC's performance would be below the target level, then DCC would lose margin incrementally until its performance was below the defined minimum level at which point all margin would be lost for a given metric.

6.6. In our 2016 consultation, we considered the need for the number of OPR incentives to be relatively few in number to create meaningful incentives on DCC. The greater the number of performance metrics in the regime, the lower the reward for DCC for achieving the desired behaviours for each performance metric. Therefore, we recommended a targeted approach for the incentive to apply to DCC's core smart metering activities, focussing on facilitating the rollout and system stability.

6.7. We considered the incentive structure for the five groups of system performance measures we decided to incentivise, taking into account that the OPR is a downside only incentive regime. As such, we considered the balance between ensuring it was possible for DCC to retain 100% of their margin and making sure they are sufficiently challenged to achieve good outcomes. This led to an approach where we placed sharper incentives on DCC to deliver target performance levels – to retain 100% of margin - while also giving DCC a strong incentive to ensure they reach minimum levels to retain 70% of margin.

6.8. We also took account of the regulatory burden on DCC of the incentive regime. We minimised regulatory burden by ensuring the proposed measures were based on metrics already established and reported on by DCC under the SEC or Service Provider reporting requirements.

6.9. Finally, we set out our intention that the OPR remained flexible so that incentives can be adjusted or amended to reflect operational experience and users' evolving needs.

The review of the OPR

6.10. Following DCC's submission of its performance under the current OPR for the RY18/19 price control, we became concerned that the OPR metrics may not have been providing the best incentives to DCC. In particular, based on feedback from DCC's customers (see the RY18/19 Price Control Consultation[18]), we were concerned that the system performance measures were not sufficiently reflective of customer experiences. In addition, the scope of the OPR was limited to system performance, while other areas of DCC's performance also have the potential for high customer impact.

6.11. We asked stakeholders in our DCC Price Control RY18/19 consultation for their views on how the OPR could be modified and improved. All respondents, including DCC, agreed with our concerns and supported a review of the OPR framework.

6.12. In March 2020 we published a working paper[19] setting out our initial thinking on how to financially incentivise three areas through a revised OPR. This would mean only 70% of margin would be at risk against system performance, due to the introduction of two new incentive areas, each with 15% of margin attached. The feedback we received largely welcomed the paper, while highlighting the key trade-off between widening the scope and diluting the margin attached to each incentive.

6.13. In May 2020 we published a statutory consultation setting out why the intervention was necessary, our policy objectives, our detailed proposals on each of the three incentive areas and the impacts of those proposals, which we have set out below. We published our decision on these proposals in October 2020.

Impacts on DCC's performance

6.14. Well-designed financial incentives have the impact of encouraging swift improvements to performance. As such, the aim of the OPR review was to optimise the financial incentives placed on DCC to drive improvements to DCC's quality of service and provide better value for

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[18] DCC Price Control Consultation: https://www.ofgem.gov.uk/publications-and-updates/dcc-price-control-consultation-regulatory-year-201819
[19] Operational Performance Regime Review: Working Paper: https://www.ofgem.gov.uk/system/files/docs/2020/03/2020.02_dcc_opr_working_paper_0.pdf

money. This was partly through improvements to the metrics used to measure system performance, and partly via the incentivisation of two new areas: customer engagement and contract management. Each of the three areas we proposed incentivising would have the potential for high consumer impact as a result of poor performance from DCC.

6.15. On system performance, we decided to move from metrics based on a set of technical outputs to a set of outcomes based measures, driven by the work of the SEC Ops Group in this area. This ensured the metrics were more strongly correlated with customer experiences; ensured the measures were a better reflection of DCC's performance; and serve as a stronger incentive on DCC to make improvements to their service, to the benefit of industry and energy consumers.

6.16. Following stakeholder feedback, we identified customer engagement and contract management as two priority areas not covered by the current OPR, where DCC customers would like to see rapid improvements in DCC's service. We expected that financially incentivising these areas would cause DCC to focus more resources on improving these areas further and faster than DCC otherwise would without incentives, again to the benefit of both industry and energy consumers.

Mitigating unintended impacts on DCC performance

6.17. As part of our consultation, we assessed potential unintended consequences on DCC's performance to ensure the design of our incentive regime was effective.

6.18. By introducing two new incentive areas, as well as system performance measures reported by region and meter generation, there was a risk that the incentive pot became too fragmented. This could mean the financial incentive DCC faced in a single area would not be sufficient to make it financially more attractive for DCC to make improvements to their service. To counteract this risk, we decided to only financially incentivise three system performance measures initially to ensure sufficient margin was at risk against each component of the regime.

Figure 7.1 – Indicative margin attached to OPR incentives based on RY19/20 Baseline Margin – old OPR

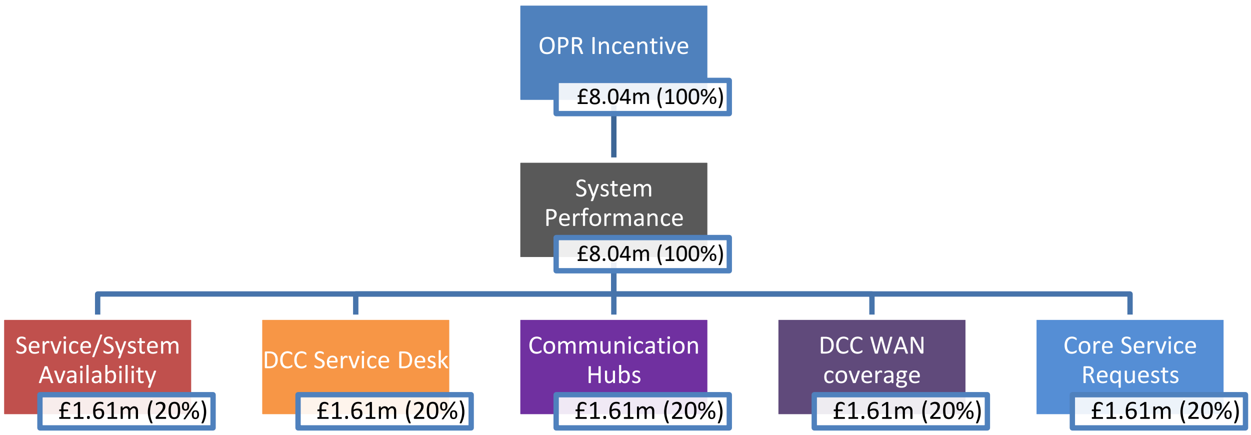
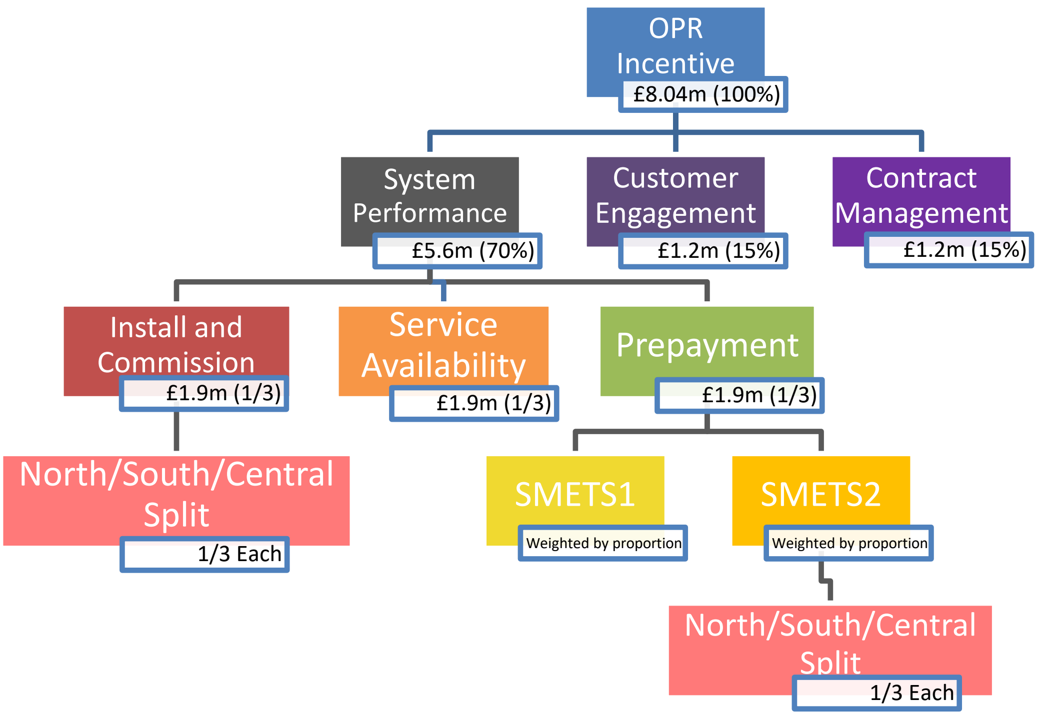


Figure 7.2 – Indicative margin attached to OPR incentives based on RY19/20 Baseline Margin – revised OPR



6.19. We considered the weighting between the three incentives to ensure DCC's behaviour was appropriately incentivised in each area. We gave system performance the highest weighting (70%) in line with the views of DCC's customers that this was most business critical area – and due to the quantitative nature of the assessment - while still ensuring that customer engagement and contract management have sufficient margin attached, based on our observations of DCC's previous response to incentives, to motivate improvements (15%).

6.20. Equally, we identified the risk that making the scope of the incentives too narrow could result in DCC making only limited improvements - or performance worsening - in areas not captured by the regime. For example, we decided not to incentivise the change of supplier measure, despite the fact that if there is a failure in the change of supplier process – that can be due to the actions of an energy supplier or DCC - this can result in consumer detriment, as the consumer will be unable to switch supplier. Based on our monitoring of this process to date, we are not concerned by DCC's performance in this area relative to the role played by energy suppliers, though there remains a risk that poor performance from DCC in this area could result in consumer detriment.

6.21. To mitigate this risk, we included change of supplier within the scope of the regime, as well as other measures that relate to areas of potential consumer detriment, with a 0% weighting. If these areas become a concern, we have the flexibility to include these measures by amending the weighting through the OPR Guidance.

6.22. There is also a potential risk that we set performance levels that are not reflective of customer requirements, driving up costs beyond what is efficient based on customer needs. We mitigated this risk by continuing to use performance levels as set by industry as part of the SEC, and by engaging with industry to understand what should be considered good performance for customer engagement and contract management.

6.23. DCC's performance for customer engagement and contract management will be measured via an assessment based on a set of qualitative criteria. With such an assessment, if the criteria are designed too narrowly and do not capture the breadth of DCC's performance, there is a risk that DCC makes changes to meet the criteria of the assessment, but that these changes do not drive real improvements to the customer experience.

6.24. To mitigate against this risk, we decided to use a tried and tested framework to assess DCC's contract management using the NAO framework. This framework is well established and the criteria sufficiently broad to avoid its use becoming a "tick box exercise". In addition, we will draw on the expertise provided by an auditor to carry out an in-depth assessment of DCC.

6.25. To assess customer engagement, we have established our own assessment framework, based on Ofgem's experience of implementing stakeholder engagement incentives. Initially we designed the assessment criteria to measure six areas, but following feedback from DCC and other stakeholders, we streamlined this proposal to three core areas. We have also set out high-level requirements for the submission to mitigate against the assessment becoming too prescriptive.

Impacts of the revised OPR on DCC's margin

6.26. Licence Condition 38.10(b) states:

6.27. "[The OPR] Must not allow the amount of the Licensee's revenues that are at risk under that regime in Regulatory Year t to be less, in total, than 100% of the value of BMt; excluding any Project Baseline Margin"

6.28. In accordance with the licence, DCC's Baseline Margin is currently 100% at risk against the regime, excluding margin attached to project scheme incentives.

6.29. Given that the amount at risk against the OPR is set to the value of DCC's Baseline Margin, DCC is protected from making a financial loss under this incentive regime. In our May consultation, we did not propose any change to the amount of margin at risk against the OPR.

6.30. To give an indication of the value at risk against each of the three incentive areas, the total Baseline Margin at risk against the OPR for RY19/20 was £8.04m. If we split this margin in line with our proposed weighting, the margin at risk for the system performance category would be £5.628m and £1.206m for both customer engagement and contract management. When the OPR comes into effect in RY21/22, we expect the margin at risk to be greater than the RY19/20 margin, due to anticipated increases in DCC's Baseline Margin.

6.31. In our RY18/19 price control decision, DCC's margin was reduced by £1.305m under the OPR, due to DCC's performance in the North region. In our 19/20 consultation, we proposed that DCC's margin should be reduced by up to £1.608m under the OPR. This margin will be passed back to DCC's customers and by extension energy consumers.

6.32. DCC has stated their concerns that altering the system performance measures, and incorporating customer engagement and contract management under the OPR, will cause DCC to lose a greater share of their margin than previous years. To an extent, we view this as a given consequence of amending the OPR to capture areas where we and stakeholders are concerned by DCC's performance levels; and consider it DCC's responsibility to make the improvements to its service to mitigate this risk.

6.33. Given stakeholders' and our own concerns around fragmenting incentives, we published a further consultation[20] in October on increasing the incentive pot at risk against the OPR. In this consultation, we considered the policy options and impacts for adding the value of DCC's External Contract Gain Share as part of the margin at risk against the OPR. We have published the decision[21] for this consultation alongside this document.

Costs to DCC's Customers and Energy Consumers

6.34. The revised OPR does not create any new expectations as to DCC's performance. We have set clear expectations through our previous price control consultations that DCC should provide reliable system performance; as well as high standards of customer engagement and contract management.

6.35. However, DCC may be performing below those levels, which would be assessed through the revised OPR. If this was the case, DCC would be incentivised to make improvements to its service, which may result in additional incurred costs that will be passed on to DCC's customers and energy consumers. These costs would be scrutinised as to whether they were economic and efficient under the price control.

6.36. Throughout the OPR review, we have received feedback from DCC's customers in strong support of improvements across all three areas of the OPR: system performance, customer engagement and contract management. In system performance, to ensure that the performance levels included in the OPR are in line with customer expectations, we have proposed in this consultation to set target and minimum service levels as equal to the target

[20] Consultation on increasing DCC's revenue at risk against the OPR: https://www.ofgem.gov.uk/publications-and-updates/consultation-increasing-dcc-s-revenue-risk-against-operational-performance-regime
[21] Decision on on increasing DCC's revenue at risk against the OPR: www.ofgem.gov.uk/publications-and-updates/decision-increasing-dcc-s-revenue-risk-against-opr

and minimum performance levels set out in the SEC, consistent with the approach in the original OPR.

6.37. We do not consider DCC spend in this area to be a negative impact of the new OPR - we expect DCC to incur some costs to make improvements that will benefit their customers - providing the spend is incurred economically and efficiently. However, given the amount of margin at risk against these incentives and the implementation timeline, DCC have raised the concern that they may implement changes to rapidly achieve the performance levels under the new regime, which could have been more cost efficient if implemented over a longer timeframe.

6.38. To mitigate this risk, we have proposed arrangements for a transitional year to give DCC the opportunity to understand their performance, and have the opportunity to make improvements, as well as provide more certainty to stakeholders over the implementation of the new regime (see Chapter 5).

Regulatory Burden

6.39. When developing the revised OPR, we considered the regulatory impact of our proposals. Note, as the OPR is intended to improve competition in the energy market, this falls outside of the scope of Ofgem's Business Impact Target[22].

6.40. In terms of system performance, we continue to use measures that have been developed and will be reported to the SEC. As this is unchanged from our approach under the old OPR, we expect any additional regulatory burden in this area to be minimal.

6.41. For customer engagement, we will be asking DCC and SEC Panel to provide a qualitative submission as part of the annual price control submission. This will comprise a 13 page submission with supporting evidence. We recognise that this will increase the regulatory burden of the OPR, and have therefore taken steps to mitigate this burden by placing guidelines on the submission format to help restrict its length whilst allowing sufficient detail to be provided. It is likely that the process will become less burdensome in subsequent years

[22] See Business Impact Target (2019) – Final Report: https://www.ofgem.gov.uk/publications-and-updates/business-impact-target-2019-final-report

as processes are embedded. Considering this is a priority area for DCC customers, we consider this proportionate to deliver improvements we wish to see.

6.42. Finally, for contract management, we acknowledge that there will be an increase in regulatory burden from completing an annual audit as part of the OPR. However, given the size and volume of DCC's contract portfolio, and that this is a priority area for DCC's customers, we view this additional regulatory burden as proportionate.

Conclusion

6.43. The aim of the OPR review is to improve the effectiveness of the incentive regime to drive improvements in DCC's performance for the benefits of DCC's customers and energy consumers.

6.44. We intend to deliver this aim by moving to a set of outcomes based metrics to more effectively measure system performance, and by increasing the scope of the regime by introducing two new incentive areas: customer engagememt and system performance.

6.45. Once the new regime is implemented, this will result either in positive behaviour change from DCC to meet the incentive targets, providing benefits for DCC's customers and energy consumers, as well as allowing DCC to retain 100% of their margin. Alternatively, DCC will not change their behaviour, perform poorly against the regime and lose margin as a result. At this stage, it is difficult to quantify the impact on DCC without making assumptions about their future performance. This uncertainty underpins our rationale for introducing a Transition Phase as set out in Chapter 5 of this consultation.

6.46. Throughout our review of the OPR, we have gathered stakeholder feedback across multiple consultations and engagements to inform our policy making, and ensure that the revised OPR is effective in delivering the objective of positive change in DCC's performance.

6.47. This further consultation on the OPR Guidance provides stakeholders a further chance to share their views on the impacts discussed in this consultation.

Appendices

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Appendix 1 – Additional Guidance for Customer Engagement

We have produced additional guidance for the assessment criteria provided in the OPR Guidance document. This additional information is intended to be read in conjunction with the assessment criteria provided in the OPR Guidance; we have provided it below for your reference. We are seeking views on the level of detail provided.

Additional guidance - Timing and Frequency of engagement

6.48. Expected timelines and frequencies for engagement should be set out clearly for DCC customers across projects and decision-making cycles, ensuring appropriate lead times for DCC customers to engage effectively. We would expect DCC to review these with its customers to ensure its processes are working and revise timeframes if necessary.

6.49. The submission should provide specific evidence demonstrating when and how frequently DCC has allowed customers to feed in their views, as well as covering the frequency and timeliness of broader informative engagement.

6.50. We would expect DCC to seek greater input, supported by appropriately detailed information, where decisions have greater potential impact on customers.

Additional guidance - Quality of information provided by DCC

6.51. When assessing the quality of the information, we will consider customers' ease of access to the information, the readability/comprehensibility of the information, and the level of detail and precision in the content.

6.52. We would expect DCC to provide sufficient rationale for different options, providing where possible sufficient information around the expected costs of options in order for customers to give informed feedback.

6.53. We would expect to see evidence that DCC has considered its audience when providing information and that the engagement is tailored appropriately, such as through the format of the information, level of technical detail, and the forums DCC chooses to engage.

6.54. We would expect to see evidence covering engagement around change and project requests, as well as DCC's broader informative engagement.

Additional guidance - Taking account of customer views

6.55. The submission should evidence that DCC has been clear when communicating to its customers, which issues they can provide views on, and ensure that DCC has provided avenues for customers to seek clarification if needed.

6.56. DCC demonstrating that it followed the recommendations of its customers in its decision-making processes would be strong evidence of high performance. However, DCC would also be able to demonstrate high performance by clearly communicating to its customers the rationale behind why, in certain instances, DCC made a decision that diverged from the views of its customers.

6.57. DCC should evidence that it has closed the ‘feedback loop’, ensuring stakeholders have been informed of the outcomes as a result of their engagement. This should be carried out regardless of whether the recommendations of customers have been followed, with a strong rationale provided for DCC’s decisions.

Appendix 2 – Glossary

A

Authority

The Gas and Electricity Markets Authority.

B

Baseline Margin

An amount of additional revenue in each regulatory year, over and above the sum of the Licensee's Internal Costs and External Costs, that the Secretary of State has agreed shall be included (subject to the performance of the Baseline Margin Performance Adjustment) in the Licensee's Allowed Revenue, and is determined in accordance with the provisions of Part C of Condition 36.

C

Communications hub

A Device which complies with the requirements of Communications Hubs Technical Specifications (CHTS) and which contains two, logically separate Devices; the Communications Hub Function and the Gas Proxy Function.

Communications Service Provider (CSP)

Bodies awarded a contract to be a service provider of DCC's communications services. Arqiva Limited and Telefónica UK Limited have been appointed to provide these services.

D

Data Communications Company (DCC)

The company that manages the data and communications to and from domestic consumers' smart meters.

Data Services Provider (DSP)

Body awarded the contract to deliver systems integration, application management and IT hosting services to DCC. CGI IT UK Limited has been appointed to provide these services.

Department for Business, Energy and Industrial Strategy (BEIS)

The UK government department responsible for business, industrial strategy, science, innovation, energy, and climate change.

N

National Audit Office (NAO)

The National Audit Office is an independent Parliamentary body in the United Kingdom which is responsible for auditing central government departments, government agencies and non-departmental public bodies.

O

Ofgem

Office of Gas and Electricity Markets.

Operational Performance Regime (OPR)

The Operational Performance Regime (OPR) is the incentive regime which incentivises DCC to perform against a set of performance measures, placing the majority of DCC's margin at risk. This is provided for under Schedule 4 of the Smart Meter Communication Licence.

S

Smart Energy Code (SEC)

The SEC is an industry code which is a multiparty agreement that defines the rights and obligations between the Data Communications Company (DCC), Suppliers, Network Operators and other users of DCC's services. All parties must comply with the Code.

Smart Meter Communication Licence

The Smart Meter Communication Licences granted pursuant to Sections 7AB(2) and (4) of the Electricity Act 1989 and Sections 6(1A) and (1C) of the Gas Act 1986.

Smart Metering Key Infrastructure (SMKI)

Smart Metering Key Infrastructure (SMKI) means the public key infrastructure established by DCC for the purpose, among other things, of providing secure communications between Devices and Users.

SEC Operations Sub-Group (SEC Ops Group)

The SEC Operations Sub-Group is sub-group of the SEC responsible for the operational matters that relate to the services provided under the Smart Energy Code, including DCC Services, and to enable close co-operation between the DCC and DCC users for monitoring DCC's performance.

Service Request Variant (SRV)

Service Request Variants (SRVs) are the messages that are sent between Smart DCC Customers and the Smart Metering System in the home/business.

SEC Release

SEC Release is a package of one or more approved Modification Proposals which is implemented in accordance with the SEC Release Management Policy.

U

User

User is a Party that has completed the User Entry Process (and, in respect of Services available in accordance with this Code to Users acting only in one or more User Roles, a Party that has completed the User Entry Process for that User Role).

Appendix 3 – Privacy notice on consultations

Personal data

The following explains your rights and gives you the information you are entitled to under the General Data Protection Regulation (GDPR).

Note that this section only refers to your personal data (your name address and anything that could be used to identify you personally), not the content of your response to the consultation.

1. The identity of the controller and contact details of our Data Protection Officer

The Gas and Electricity Markets Authority is the controller (for ease of reference, "Ofgem"). The Data Protection Officer can be contacted at dpo@ofgem.gov.uk

2. Why we are collecting your personal data

Your personal data is being collected as an essential part of the consultation process, so that we can contact you regarding your response and for statistical purposes. We may also use it to contact you about related matters.

3. Our legal basis for processing your personal data

As a public authority, the GDPR makes provision for Ofgem to process personal data as necessary for the effective performance of a task carried out in the public interest. I.e. a consultation.

3. With whom we will be sharing your personal data

We are not intending to share your personal data with other organisations. We are intending to publish non-confidential consultation responses, including any personal data that may be contained within them.

4. For how long we will keep your personal data, or criteria used to determine the retention period

Your personal data will be held for six months after the consultation closes.

5. Your rights

The data we are collecting is your personal data, and you have considerable say over what happens to it. You have the right to:

- know how we use your personal data
- access your personal data
- have personal data corrected if it is inaccurate or incomplete
- ask us to delete personal data when we no longer need it
- ask us to restrict how we process your data
- get your data from us and re-use it across other services
- object to certain ways we use your data
- be safeguarded against risks where decisions based on your data are taken entirely automatically
- tell us if we can share your information with 3rd parties
- tell us your preferred frequency, content and format of our communications with you
- to lodge a complaint with the independent Information Commissioner (ICO) if you think we are not handling your data fairly or in accordance with the law. You can contact the ICO at https://ico.org.uk/, or telephone 030 3123 1113.

6. Your personal data will not be sent overseas

7. Your personal data will not be used for any automated decision making

8. Your personal data will be stored in a secure government IT system

9. More information

For more information on how Ofgem processes your data, click on the link to our "Ofgem privacy promise