Scottish & Southern Electricity Networks

T2BP-DD-SHE-001

SSEN Transmission

SSEN Transmission – Consumer Value Proposition

Approach to Consumer Value Proposition (CVP)

This short paper outlines the approach we took to developing our CVP as the Ofgem Business Plan Guidance developed.

CVPs were introduced in June 2019, when the first draft of our Business Plan had already been completed. Nonetheless, what remained consistent in the June 2019 Guidance with the Framework Decision was that there would be an incentive on companies to submit high quality business plans1; demonstrating ambition and added value was always at the forefront of Business Plan.

In submitting our final Business Plan, we took a five-stage approach to our CVP proposal development:

Stage 1: Minimum requirements	• How do we meet Ofgem BP Guidance minimum requirements, made a step change from RIIO-1 to RIIO-2 and compare to benchmarks? • *First compulsory, other two strengthen proposal*
Stage 2: Stakeholder support	• Is there evidence that this is something consumers value? • *Key evidence that proposal incorporates what consumers and stakeholders value*
Stage 3: Monetisation	• Can the proposed CVP be monetised? If so, how? • *Demonstrate a reasonable approach, setting out workings and assumptions that results in a net value*
Stage 4: Qualitative CVPs	• If it can't be monetised or the net benefit is small, add to qualitative CVP provided Stage 1 and 2 are satisfied • *Qualitative proposals still add value*
Stage 5: Return commitment	• How will we hold ourselves to account for delivering additional value to consumers? • *Qualitative assessment through Enhanced Reproting Framework with final judgement at close out*

[1] Framework Decision 2018 ruled out fast-tracking but identified a need to for alternative incentives on companies to submit "high quality" business plans. Sector Specific Methodology Decision 24 May 2019 –references the four-stage Business Plan Incentive assessment with limited detail on stage 1 (minimum requirements) and stage 2 (ultimately the CVP). The term CVP did not exist. Key: refers to a qualitative assessment and that the Business Plan Guidance will set out how that qualitative assessment will be undertaken. Business Plan Guidance – 3 June 2019 – first publication with detail of the CVP including monetisation (updated 9 September and 31 October).

Stage 1: Minimum requirements

In identifying the minimum requirements our approach was first to be clear what CVP was not. It was not the by-product of the majority of minimum requirement/core funded activity in the business plan (e.g. connecting renewable generation through load related allowances or GVA we generated), even if that activity was ambitious.[2]

Next, we identified areas that we believed were above minimum requirements. For us, the minimum requirement test was threefold:

1. incremental to the Ofgem minimum requirements set out in stage 1 of the Business Plan Guidance;
2. making a step change from T1 to T2 (i.e. not BAU); and
3. demonstrably ambitious compared to appropriate benchmarks.

A strict interpretation of the updated Business Plan Guidance (paragraphs 5.12 and 5.13 in particular) would consider that only Point 1 is required, however, we did not feel that it was likely Ofgem would seek to limit the scope in such a way, potentially disregarding wider benefits supported by consumer and stakeholder feedback. Our view was that Point 1 was a mandatory requirement which could be further augmented and thereby strengthened by providing evidence of Points 2 and/or 3. We have sought to develop our CVPs in line with this interpretation, supporting the proposition that our Business Plan offers additional benefits and value for money to consumers beyond minimum requirements and BAU activities.

Stage 2: Stakeholder Support

The second step for us, like all elements of our plan, was to demonstrate if and how our proposals for CVP had stakeholder support. This aligned with Ofgem's key requirement that Business Plans should be informed by stakeholders, focusing on their key priorities in detailing network activities and outputs to be delivered in the price control period. In our Business Plan, we have provided evidence that our CVP proposal incorporates consumers expectations, priorities and values (paragraph 5.21 of the Guidance).

Stage 3: Monetisation

The third stage was to determine if a monetised value could be calculated for the CVP.

Ofgem was consistent, from the SSMD through to each iteration of the Business Plan Guidance, that the quality assessment part of the BPI assessment would be qualitative, however, it did state in the June 2019 version of the Guidance that companies "*should seek to provide a monetised value to consumers for each proposal forming part of the CVP*" noting *"where a company is unable to propose a robust methodology for calculating a monetised value … it may be unable to determine an appropriate size of reward for that proposal".* This additional wording did not replace the qualitative assessment and Ofgem did not rule out the possibility of

[2] Note: minimum requirements or minimum activity does not mean unambitious activity. There are lots of examples where moving from RIIO-1 to RIIO-2 required a step change under Ofgem minimum requirements.

a reward where monetisation isn't possible or difficult which we consider is consistent with the approach to deliver a Business Plan developed through enhanced stakeholder engagement and which focuses on stakeholder priorities and not just easily measured activities.

In its June and then September Guidance, Ofgem provided that companies should use a **reasonable**[3] methodology in the absence of explicit guidance and models for valuing specific CVPs

Based on the above, we sought to identify reasonable monetisation methodologies in the limited timeframe. While there was no detailed step-by-step guidance, there were three requirements when monetising the value which we were careful to comply with. To:

- clearly set out the methodology and associated data used in calculations;
- ensure that the benefits were net of costs; and
- ensure that the benefits were net of the company's totex efficiency incentive rate.

While we believe our approaches were reasonable, we understand other approaches may also have been adopted; in some cases, we noted the alternatives. We also clearly set out our assumptions as we understand that alternative assumptions may also have been made.

Through our approach, we have sought to demonstrate that there is a substantive net benefit to consumers as a result of our CVP proposals. Due to the qualitative nature of some of our CVP proposals, that exact value is open to debate, however our approach has been to be as transparent as possible in our methodologies to facilitate that debate.

Stage 4: Qualitative CVPs

Where it was difficult to monetise, due to limited data or time constraints, or where the net benefits were small (e.g. for science based targets) we chose to report as a qualitative CVP so as not to distract from the other CVPs which had a larger monetised net benefits.

It does not follow that these areas are without value; simply that they were difficult to monetise. These qualitative CVPs were subject to the same level of scrutiny in Stage 1 and Stage 2 to identify whether they were above minimum requirements and if they were supported by stakeholders, respectively.

Stage 5: Return Commitment

Finally, our commitment to deliver our CVP proposal formed part of our Output Commitment; if we don't undertake the activities that deliver any rewarded CVP value, we have committed to return an equivalent and proportionate CVP value to consumers, being held to account through our Enhanced Reporting Framework (ERF).[4]

[3] Bullet 4 of paragraph 5.21, RIIO-2 Business Plan Guidance, 9 September 2019
[4] Page 36-37 of Regulatory Framework: Outputs, Incentives, CVP & Innovation

The process for assessing the CVPs was recognised by Ofgem as qualitative; and we consider it is appropriate that the process for assessing CVP output delivery must also be qualitative.

The monetisation presents a value to inform the overall assessment, it does not present a baseline target on which to track deliverability. Of note:

- **Not all CVPs require the company to deliver something** within a price control e.g. CVP 1a and CVP 1b, so there is no scope for "clawback" based on deliverability.
- Even if the proposal relates to a commitment to deliver something in RIIO-2, **a baseline for any mechanistic return is not appropriate** where a range of metrics inform the value or when it is changes from the original proposition to deliver something different that could result in great value.

For example, we demonstrated that our package of Commercial and Connections services can result in value stretching across displaced carbon, reduced constraints and cost savings through avoided distribution costs and reduced wholesale prices. To shoe-horn into one element and set a baseline target would be a crude mechanism of measurement potentially undervaluing key stakeholder priorities. Rather it would be more appropriate to undertake impact assessment(s) of the activities completed, which may change and evolve from those originally proposed in line with stakeholder expectations and an evolving industry.

- Any **assessment should be judged through close out mechanisms** as the CVP commitments are typically for a value created over the full price control period and not, for example, an annual benefit. That is not to say progress towards demonstrating that value can't be made at incremental stages throughout the price control (e.g. mid-period report), but the full impact can only be judged at the end.

These bullets are particularly important in distinguishing a CVP/BPI from ODIs, where quantitative baseline targets can be set and can be monitored annually.

Further detail on how this qualitative assessment process to track CVP performance could work is provided below.

Accountability from an independent group: Our RIIO-T2 User Group has strongly influenced the development of our RIIO-T2 Business Plan, including challenging us on the aspects that formed our CVPs. We are committed to continue an enhanced engagement approach during the implementation of our Plan and throughout the period. Our initial thoughts are that this Group may retain some of the existing members to provide a degree of continuity and expertise in that ongoing challenge, however, the majority of members will be new to enhance the legitimate independent challenge that we a) continue to meet the needs of our stakeholders and b) we meet the commitments of our Plan. It is this independent challenging function we found invaluable during the development of our Business Plan. We propose reporting progress against all our outputs and incentives, including CVP, should form part of this Group's remit,

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including the delivery of an independent annual report to the Board. For the Group to make judgements the onus will be on us to provide the evidence.

Transparent and accessible reporting using our Enhanced Reporting Framework: As part of our Stakeholder Engagement Strategy and Stakeholder Engagement Action Plan we worked with Citizens Advice to develop a new ERF for RIIO-T2. Feedback from Citizens Advice and stakeholders demonstrated a desire for transparency in the performance and activities of energy networks, noting existing performance reports are technical and financially focused. Our new ERF is split into three parts: Service Performance, Financial Performance and Performance for Society. The purpose of the Performance for Society section is to ensure customers and stakeholders can see the **contribution that we are making to society** through the delivery of an essential public service. Any CVP reward and demonstrated benefits will be reported qualitatively in this section as well as quantitatively in the Financial Performance section on an annual basis, published on our website. We will proactively engage with stakeholders throughout the period to provide feedback on our report including Ofgem.

Precedent for this approach: The above accountability and transparent reporting will ensure consumers and wider stakeholders can see the contribution we are making to society and delivering the benefits we outlined in our CVP. This type of reporting is not unprecedented. For example, in RIIO-ED1 DNOs report on their wider connections engagement under the Incentive on Connections Engagement. While we are proposing to report wider benefits rather than benefits to a particular customer segment (large generation customers) similar principles apply. Parallels can also be drawn with the public facing report of the Environmental Discretionary Reward in RIIO-T1, albeit the detail and depth of CVP reporting is unlikely to be like the EDR, similar gathering of the types of evidence is envisaged.