

# Incentives: - our performance and an overview of proposals for RIIO-2

Tuesday 1<sup>st</sup> October 2019

nationalgrid



# Who we are...



**Mike  
Wassell**

RIIO-2 Incentives  
Manager



**Carol  
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GSO RIIO-2 Commercial  
Strategy Manager



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Head of  
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**Jenny  
Pemberton**

RIIO 2 Stakeholder  
Engagement Manager

# Logistics

Should last for approximately an hour

Polling via Webex

Your questions are welcomed throughout via chat function

All callers will be placed on mute

Slides will be circulated after the call

# Quick Poll – Getting to know you

1. Please tell us your name

2. Which of the following best describes you / your organisation?

3. On a scale of A to E, where A is know nothing and E is know a great deal, how much would you say you know about National Grid Gas Transmission's operational activities?

- A. Know nothing
- B.
- C.
- D.
- E. Know a great deal

# Quick Poll – Impact and Interest

**On a scale of A to E, where A is not impacted at all and E is impacted a great deal, how impacted are you or those you represent) by Incentives?**

- A. Not impacted at all
- B.
- C.
- D.
- E. Impacted a great deal

**On a scale of A to E, where A is not interested at all and E is interested a great deal, how interested are you (or those you represent) by Incentives?**

- A. Not interested at all
- B.
- C.
- D.
- E. Interested a great deal

# The need for incentives and their purpose

Delivering desirable consumer outcomes through a regulatory framework

## Need

Improve information discovery properties

Enable efficient delivery of outcomes that matter to consumers

Identify outcomes that mimic those of a competitive market

## Purpose

Focusing on unlocking consumer value in the short and long term

Encourage to anticipate the future needs of consumers and network users

Focusing on what is delivered rather than how it is delivered

# Key principles of incentives

An incentive must...

- ...have a robust baseline
- ...be measurable and quantifiable
- ...recognise the changing landscape
- ...promote investment and innovation to unlock additional consumer value, both now and into the future (financial or otherwise)
- ...be supported by stakeholders and aligned to stakeholder priorities

To deliver...

- ...additional consumer value in the short or long term
- ...improved performance in areas above and beyond business as usual obligations

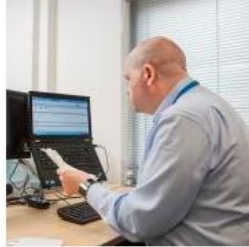
# RIIO-1 Incentives



Constraint management



Residual balancing



NTS shrinkage



Customer/Stakeholder Satisfaction



Demand forecasting



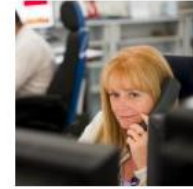
Maintenance



Greenhouse gas (GHG) emissions



Stakeholder Engagement Incentive Scheme (SEIS)



Information provision



Operating Margins (OM)



Unaccounted for Gas (UAG)



Transportation support services (TSS)

Incentive ceased from October 2018

Reputational



# RIO-1 Incentive performance to date

	Incentive Year Performance (£m)					
Incentive	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19
Constraint management	12.6	12.6	12.6	13.3	14.2	13.8
Shrinkage	5.1	4.8	6.3	2.5	4.2	7.0
Demand forecasting	2.5	3.7	3.2	2.5	2.5	-0.7
Maintenance	1.1	0.9	0.4	0.7	0.7	0.7
Greenhouse gas	-0.5	0.0	-0.2	-1.0	-1.4	0.0
Residual balancing	1.0	1.1	1.2	1.1	0.6	1.0
Customer Satisfaction	0.7	2.0	2.0	3.5	2.5	2.7
Stakeholder Satisfaction	-	-	-	0.8	0.9	0.9
Stakeholder Engagement	1.1	1.5	1.5	1.8	0.2	0.6

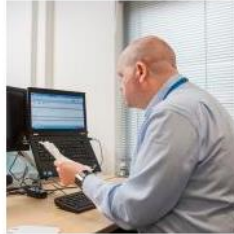
# RIIO-2 Incentives proposals



Constraint management



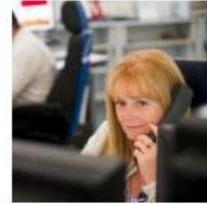
Residual balancing



NTS shrinkage



Environmental



Information provision



Stakeholder Satisfaction



Demand forecasting



Maintenance



Customer Satisfaction



Greenhouse gas (GHG) emissions



Unaccounted for Gas (UAG)



Community Engagement

Reputational

# QUESTIONS



# RIIO-2 Incentives - at a glance



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# Capacity Constraint Management

We are obligated to release Entry and Exit capacity at around double peak demand (top down regime). Flows of gas at these levels cannot be physically accommodated concurrently meaning there is an inherent risk to be managed.

## RIIO-1 Incentive

- Target cost (Revenue – Costs) of £22m (in 09/10 prices) based on expected constraint costs
- Cap and Collar on incentive reward +£20m/-£60m (in 2009/10 prices)
- Encourages us to take on risk, minimise commercial actions and ensure investment decisions are balanced against risk

## RIIO-2 Initial position

- Retain scheme, design to be reviewed after completion of network capability review
- Review scheme with regards to the high impact/low probability nature of scheme
- Potentially introduce a new element that removes revenue from the scheme where we scale back interruptible / off-peak capacity

No Incentive (BAU)	Incentive (exceeding BAU)	Value for Consumers
<ul style="list-style-type: none"> <li>• Less likely to release non-obligated capacity</li> <li>• Tend towards more risk aversion in NGG decision making</li> <li>• More likely that commercial decisions are made closer to real time and more frequent actions (more risk averse)</li> </ul>	<ul style="list-style-type: none"> <li>• More likely to take on risk in releasing capacity over and above obligations</li> <li>• Realigning outages at cost to NGG to mitigate / manage potential constraints</li> <li>• More likely to take on risk in key investment decisions</li> <li>• Less risk averse in carrying out constraint management actions</li> </ul>	<ul style="list-style-type: none"> <li>• Facilitates customers being able to bring gas on and off the network when and where they want, meaning the cheapest gas can be sourced with minimal disruption:               <ul style="list-style-type: none"> <li>• Improved quality of service</li> <li>• Lower consumer bills</li> <li>• Improved safety and reliability</li> </ul> </li> </ul>

## Quick poll

Should we retain a Capacity Constraint Management incentive?

Yes

Unsure

No

Do you agree with our RII0-2 initial position?

Yes

Somewhat

No

# Residual Balancing

We, as residual balancer, can enter the market and undertake trades to resolve any residual imbalance on the system. The net costs or revenues from our market balancing actions are ‘smeared’ back to shippers via balancing neutrality. The incentive is integral to the residual balancing role and framework.

## RIIO-1 Incentive

The incentive comprises of:

- Linepack Performance Measure (LPM): drives us to balance closing to opening linepack ( $\pm 2.8$  mcm/d)
- Price Performance Measure (PPM): drives us to minimise the price spread of our trades by measuring the price range of our trading actions compared to the System Average Price (SAP) ( $\pm 1.5\%$ )
- Cap and Collar +£2/-£3.5m

## RIIO-2 Initial position

- Tougher to achieve due to reducing the performance gradient, against a backdrop of a changing and more challenging energy landscape
- Amend LPM for shoulder months to 5.6 mcm/d to drive the right behaviour during seasonal transitions between winter and summer and vice versa
- 20% reduction in cap and collar

No Incentive (BAU)	Incentive (exceeding BAU)	Value for Consumers
<ul style="list-style-type: none"> <li>• Increased likelihood of trading more often to minimise risk (risk averse) with less focus of cost and effect on market of residual balancing actions</li> <li>• Trading strategies less likely to evolve and keep pace with a changing market</li> </ul>	<ul style="list-style-type: none"> <li>• Trading activity is more strategic (less risk averse) and more likely to keep pace with a changing market</li> <li>• Invest and innovate in commercial insight, analysis and supporting tools</li> <li>• Less market intervention (we currently avoid entering the market roughly 250 days per year)</li> </ul>	<ul style="list-style-type: none"> <li>• We enter the market in a measured way to avoid incurring unnecessary costs for consumers</li> <li>• More efficient, transparent and predictable management of linepack – more informed market</li> </ul>

## Quick poll

**Should we be incentivised to balance linepack and minimise the price spread of our actions?**

Yes

Unsure

No

**Do you agree with our RII0-2 initial position?**

Yes

Somewhat

No



# Maintenance

We must periodically carry out maintenance on the NTS and publish a planned maintenance schedule. Where the work requires customers to cease or reduce offtake flows, we may ‘call’ one or more ‘maintenance days’.

## RIIO-1 Incentive

- Changes scheme – target maximum number of planned maintenance changes we initiate each year. Earned reward £50,000 per change below target number. Penalty £50k per change over target. Cap and collar +/-£0.5m p.a.
- Use of days scheme - target of 11 maintenance days called for Remote valve Operations (RVOs). If maintenance days used is less than target, tiered reward to NGG between £15k and £25k per day, capped £0.215m. If maintenance days used exceeds the target, NGG penalty of £20k per day, collar of £0.5m

## RIIO-2 Initial position

- Retain existing scheme and add target no. of “maintenance days” (10% of plan) for asset replacement and reinforcement works
- +/-£20k per day variance against target, capped & collar £0.5m.

No Incentive (BAU)	Incentive (exceeding BAU)	Value for Consumers
<ul style="list-style-type: none"> <li>• More likely to focus on UNC obligations (e.g. use our entitled maintenance days)</li> <li>• More likely to reschedule planned maintenance activities as we focus on operational requirements</li> </ul>	<ul style="list-style-type: none"> <li>• Volume of maintenance in RIIO-2 likely to increase from RIIO-1 levels. requiring increased focus on customer impacts and alignment of plans</li> <li>• We continue to perform beyond our regulatory obligations</li> </ul>	<ul style="list-style-type: none"> <li>• Less customer outages benefits operational costs and markets (e.g. CCGTs able to generate)</li> </ul>

## Quick poll

Should we be incentivised to minimise our impact of maintenance activities on customers?

Yes

Unsure

No

Do you agree with our RIIO-2 initial position?

Yes

Somewhat

No

# Demand Forecast

We provide NTS demand forecasts over a range of timescales to help the industry make informed physical and commercial decisions.

## RIIO-1 Incentive

- D-1 incentive has an annual average absolute error forecasting accuracy target of 8.5 mcm/d in 2018/19
- D-2 to D-5 the target is 13.7 mcm/d
- Cap & collar
  - D-1 +£10/-£1.5m
  - D-2 to D-5 +£10/-£1m



## RIIO-2 Initial position

- Retain scheme
- Make incentive tougher to achieve by reducing the performance gradient, recognising that demand forecasting is becoming increasingly challenging
- Caps for each scheme reduced to £8m, collars as-is

No Incentive (BAU)	Incentive (exceeding BAU)	Value for Consumers
<ul style="list-style-type: none"> <li>• Less likely to evolve and invest in our demand forecasting tools and processes</li> <li>• Increasing demand volatility more likely to impact forecast accuracy</li> </ul>	<ul style="list-style-type: none"> <li>• Invest in our demand forecasting models, processes, intelligence, tools and procured services</li> <li>• Increased focus on forecasting demand volatility</li> </ul>	<ul style="list-style-type: none"> <li>• Industry can make informed decisions enabling savings to be passed on to consumers</li> <li>• Reduces barrier to entry for smaller industry participants</li> <li>• Increased forecast accuracy likely to benefit wholesale market prices</li> </ul>

## Quick poll

**Do you use our demand forecasts?**

Yes

Unsure

No

**Should we be incentivised to improve our demand forecasts?**

Yes

Unsure

No

**Do you agree with our RIIO-2 initial position?**

Yes

Somewhat

No

# Greenhouse Gas

**Methane gas is vented as part of normal operation of compressor fleet from depressurisation for maintenance and stand-down, or natural loss while the compressor is pressurised (running and standby)**

## RIIO-1 Incentive

- Currently penalised for each tonne of methane emitted per annum over a target of 2,897t (CO2 equivalent)
- The current scheme has an unlimited financial downside, and no financial upside for emitting less than target



## RIIO-2 Initial position

- Retain scheme with more penal rates but include an upside and cap/collar to encourage investment and innovation to further reduce emissions
- Potentially include within a broader environmental incentive package

No Incentive (BAU)	Incentive (exceeding BAU)	Value for Consumers
<ul style="list-style-type: none"> <li>• Venting levels driven primarily by operational requirement</li> <li>• Environmental consideration becomes more focussed on compliance</li> </ul>	<ul style="list-style-type: none"> <li>• Continual review of GHG impacts of our maintenance planning and compressor strategies to focus on evolving and adapting to changing requirements</li> <li>• Investing in innovation of processes and technology to reduce frequency of maintenance based depressurisation</li> </ul>	<ul style="list-style-type: none"> <li>• Reduced environmental impact</li> </ul>

## Quick poll

**Should we be incentivised on GHG?**

Yes

Unsure

No

**Do you agree with our RII0-2 initial position?**

Yes

Somewhat

No

# Shrinkage

As NTS Shrinkage Provider, NGG is responsible for managing the end-to-end service of forecasting, accounting for, procuring, and supplying energy to satisfy the daily NTS shrinkage components. The associated costs are collected from shippers via the commodity charge

## RIIO-1 Incentive

- We are incentivised to deliver shrinkage energy at a cost lower than an agreed annual Target Shrinkage Cost
- There is a financial reward for delivering below target cost and penalty for exceeding
- There is a cap and collar of +/-£7m p.a.



## RIIO-2 Initial position

- Retain the scheme
- Add seasonal products to trading options to reduce trading costs (increased liquidity)
- Review Shrinkage Methodology
- Reduce cap and collar to +/-£5m

No Incentive (BAU)	Incentive (exceeding BAU)	Value for Consumers
<ul style="list-style-type: none"> <li>• Greater focus on delivery of UNC obligations and less focus on delivery of Shrinkage below target cost</li> </ul>	<ul style="list-style-type: none"> <li>• Procure shrinkage energy at prices better than the target price through innovative trading strategies</li> <li>• Manage price risk by buying energy using forward contracts</li> <li>• Minimise TNUoS charges by developing compressor running strategies, whilst still meeting customer needs</li> <li>• Invest in market analysis to inform trading strategies</li> </ul>	<ul style="list-style-type: none"> <li>• Reduced cost of shrinkage passed through to customers and ultimately consumers</li> </ul>

## Quick poll

Should we be incentivised on Shrinkage energy procurement?

Yes

Unsure

No

Do you agree with our RIIO-2 initial position?

Yes

Somewhat

No



# Customer satisfaction

How we operate our day to day services has an impact on our customers time, effort and ability to make informed decisions which in turn impacts their operating costs.

## RIO-1 Incentive

- Customers are asked at least once a year, when taking all services into consideration - how satisfied they were with National Grid Gas Transmission on a scale of 1-10
- The average score across the year is compared to a sliding scale reward cap of 8.50 and penalty collar of 5.30 where 6.90 is the threshold between reward and penalty
- The incentive is calculated from +/-1% of revenue

## RIO-2 Initial position

- Retain existing scheme
- Ensuring all customer contacts passing through all core customer touchpoints have an opportunity to score and feedback on the quality of their experience throughout the year

No Incentive (BAU)	Incentive (exceeding BAU)	Value for Consumers
<ul style="list-style-type: none"> <li>• More likely to focus on <u>what</u> is delivered by <u>when</u> and less on developing <u>how</u> to meet the change in demand, variety of needs and expectations across all our service areas</li> <li>• Focus on developing systems and processes which deliver single service proposition</li> </ul>	<ul style="list-style-type: none"> <li>• Re invest in necessary continual improvement to meet change in demand –people, systems etc</li> <li>• Re invest in adapting service proposition based on varying customer segment needs</li> <li>• Continue to perform beyond our regulatory obligations</li> </ul>	<ul style="list-style-type: none"> <li>• Positive impact on the operating costs of the businesses directly serving consumers</li> </ul>

## Quick poll

**Should we be incentivised to continually improve the experience we provide our broad spectrum of customers?**

Yes

Unsure

No

**Do you agree with our RIIO-2 initial position?**

Yes

Somewhat

No

# Stakeholder satisfaction

We recognise that how we proactively or reactively engage and interact and with all stakeholders is as important as what the interaction is about

## RIIO-1 Incentive

- Stakeholders are asked the same satisfaction questions as customers
- With a reward cap of 9.00 and penalty collar of 5.80 and 7.40 being the threshold between reward and penalty

## RIIO-2 Initial position

- Retain existing approach without incentive reward
- All contacts passing through all core interactions and engagement touchpoints have an opportunity to score and feedback on the quality of their experience throughout the year

### Reputation Measure

- Ensuring all our touchpoints with customers, stakeholders and communities are measured in a similar way so that we can have a holistic view of where we need to prioritise efforts
- Recognises that the experience we provide is vitally important

### Value for Consumers

- Listening to all stakeholders, including customers and communities helps us to streamline our processes and communications so that they deliver what is needed, first time
- This in turn helps us to keep our costs as low as possible in future

# Community engagement

We recognise that how we proactively or reactively engage with those affected by our construction work – the communities and their representatives, before during and after the work has completed is extremely important to those involved in terms of care and transparency

## RIIO-1 Incentive

- Part embedded in Stakeholder Satisfaction



## RIIO-2 Initial position

- Replacing current local manual survey process with existing stakeholder approach
- Aimed at local consumers not just their representatives and following the communication path before, during and after to ensure quality is there throughout and continual improvement made

### Reputation Measure

- Ensuring all our touchpoints with customers, stakeholders and communities are measured in a similar way so that we can have a holistic view of where we need to prioritise efforts
- Recognises that the experience we provide is vitally important

### Value for Consumers

- Listening to all stakeholders, including customers and communities helps us to streamline our processes and communications so that they deliver what is needed, first time
- This in turn helps us to keep our costs as low as possible in future

# Which of these areas is important to you that we go above and beyond?

**Greenhouse Gas**

**Demand forecasting**

**Capacity constraint management**

**Shrinkage**

**Residual balancing**

**Maintenance**

Please select all that apply

# QUESTIONS



# Upcoming Webinars

**Network capability baseline capacity review**

**7<sup>th</sup> & 14<sup>th</sup> October**

**Incentives: Our proposals for RII0-2**

**8<sup>th</sup> October**

**Understanding the capability of the network in an uncertain world**

**16<sup>th</sup> October**

To register, please contact  
[Jennifer.Pemberton@nationalgrid.com](mailto:Jennifer.Pemberton@nationalgrid.com)

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Thank You



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