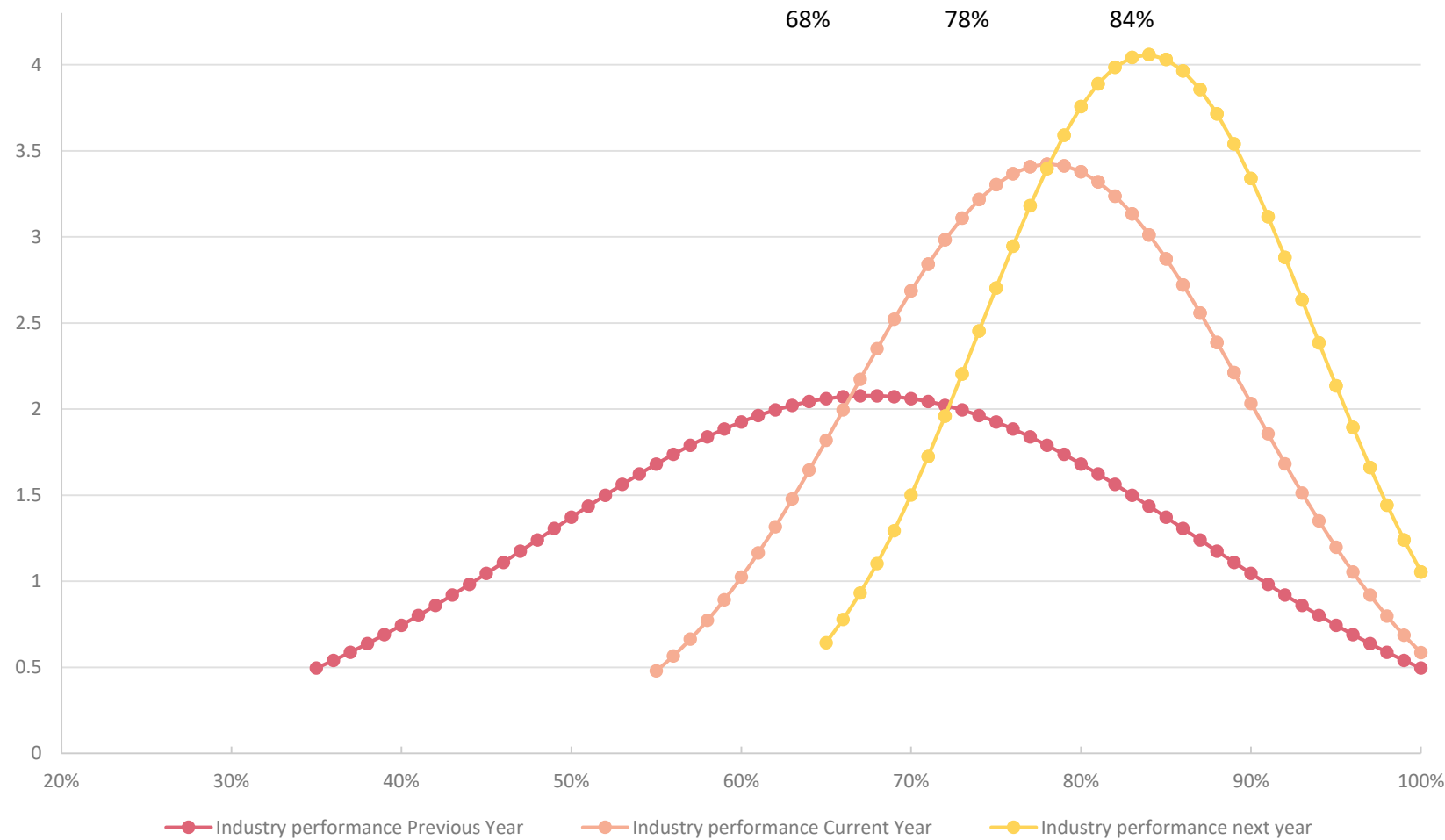# Incentives

26 September 2018

Gemserv

# "a good settlement regime"

Industry performance



**Previous Year**
Understand inherent industry performance
Monitor performance
**Current Year**
Understand current industry performance
Areas of focus
Link performance measures to obligations
Monitor performance
Implement incentives for better behaviour
**Next Year**
Understand forward plan for industry performance
Areas of focus
Amend obligations for greater standards
Monitor performance
Implement incentives for better behaviour

68%    78%    84%

Industry performance Previous Year    Industry performance Current Year    Industry performance next year

# Incentive types

- SOFT
  - Random monitoring
  - Regular monitoring
  - Performance enquiries
  - Education and engagement
  - Letter to offending party – 'poor performance notification'

- MEDIUM
  - Letter to offending party
  - Interview/call in senior management (PAC or UNCC)
  - Name/publish stats
  - Agreed performance plan
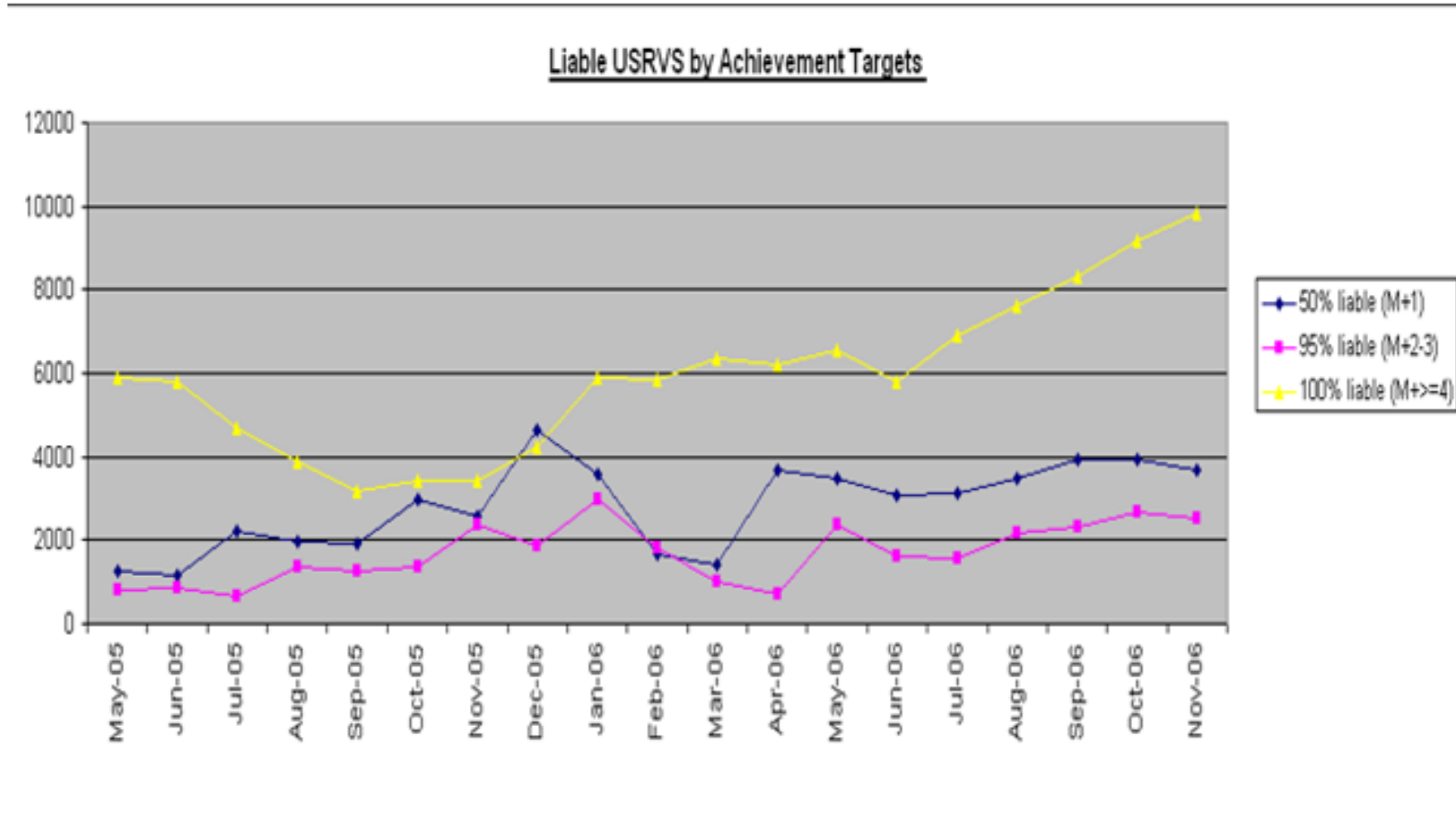
- HARD
  - Liquidated damages
  - Code sanctions
  - Escalate to Ofgem

# Case Study: USRV (User Suppressed Reconciliation Value)

- Filter failure regime:
  - Financial penalty charged per meter point per month for offending LSPs
  - Liabilities capped (initially at £100,000, later increased to £300,000) to prevent excessive charging
  - Shippers given performance targets, penalty charge increases with time taken to resolve issues (historic issues £30/month, 95% resolved within 2 months – outstanding penalty £20/month, 100% resolved within 4months – outstanding penalty £30/month)
  - Revenue spread back to RbD community
  - Invoiced monthly to LSP shippers based on performance

# USRV incentive regime



Liable USRVS by Achievement Targets

Legend:
- 50% liable (M+1)
- 95% liable (M+2-3)
- 100% liable (M+>=4)

# Criteria for Incentives

- Does the liability represent the value of risk?
  - How would this be quantified?

- Who pays who?
  - How would cash flow be managed and redistributed?

- What happens if a Party doesn't pay?
  - Escalation actions?

- What value should the penalty be?
  - Avoided costs?
  - Value of benefit received?
  - Or both?
  - Should a punitive element be added?

- Are incentives fit for legal scrutiny?

# Potential incentives

Can 'one size fit all?'

# Scenarios:

**Assumptions party A:**

- Annual throughput = much lower than party B
- Obligation to submit reads within 5 days
- Portfolio static within the month
- Read submission data provided on the agreed day per month
- Market participant agrees to the PAF obligations
- Performance obligation is the minimum requirement
- Due each calendar month

**Assumptions party B:**

- Annual throughput = much higher than party A
- Obligation to submit reads within 5 days
- Portfolio static within the month
- Read submission data provided on the agreed day per month
- Market participant agrees to the PAF obligations
- Performance obligation is the minimum requirement
- Due each calendar month

# Example 1 – Party A charge for missed reads

- 300 sites in total – lower throughput than party B

- Obligation to submit 300 reads per day

- Charge per day per missed read - £300

- Charges start at D+5

- Day 0 – 150 reads not submitted

- Day 30 – 60 reads not submitted
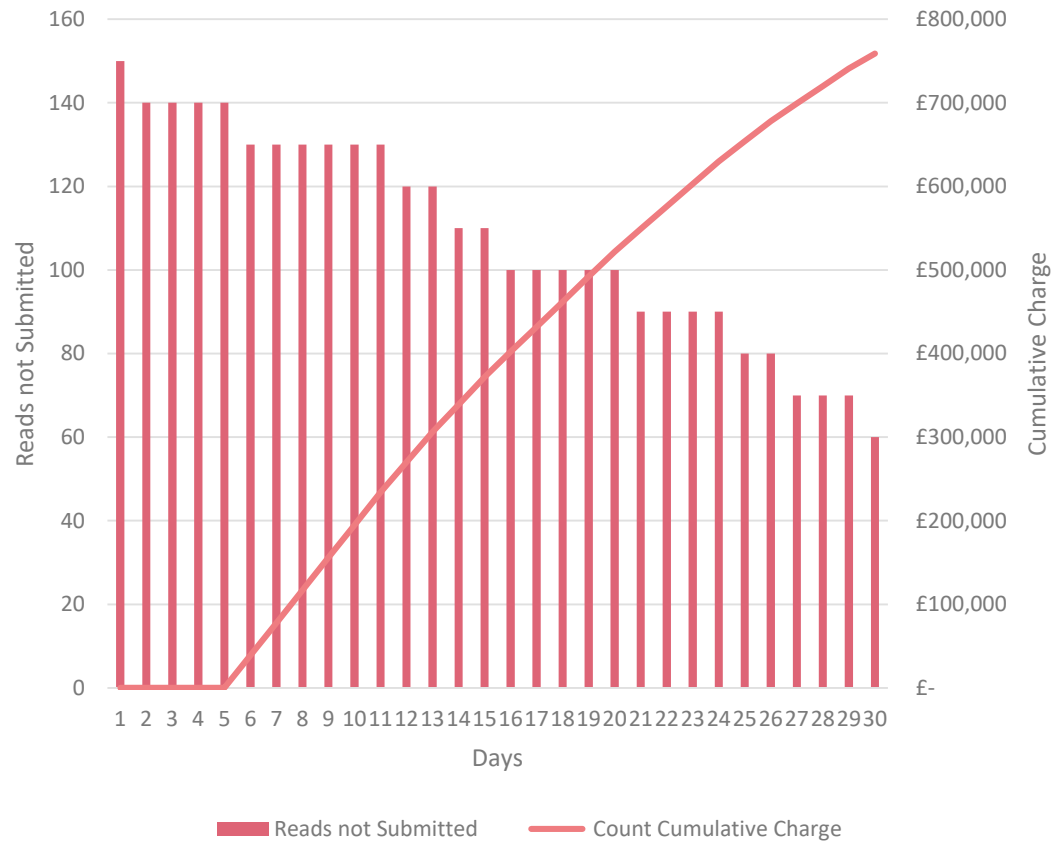
- Cumulative charges for month - £759,000

- Cumulative charges for month for 0 reads submitted - £2,250,000

### Cumulative charge per day based on count of reads not submitted - Smaller Shipper size



Reads not Submitted     Count Cumulative Charge
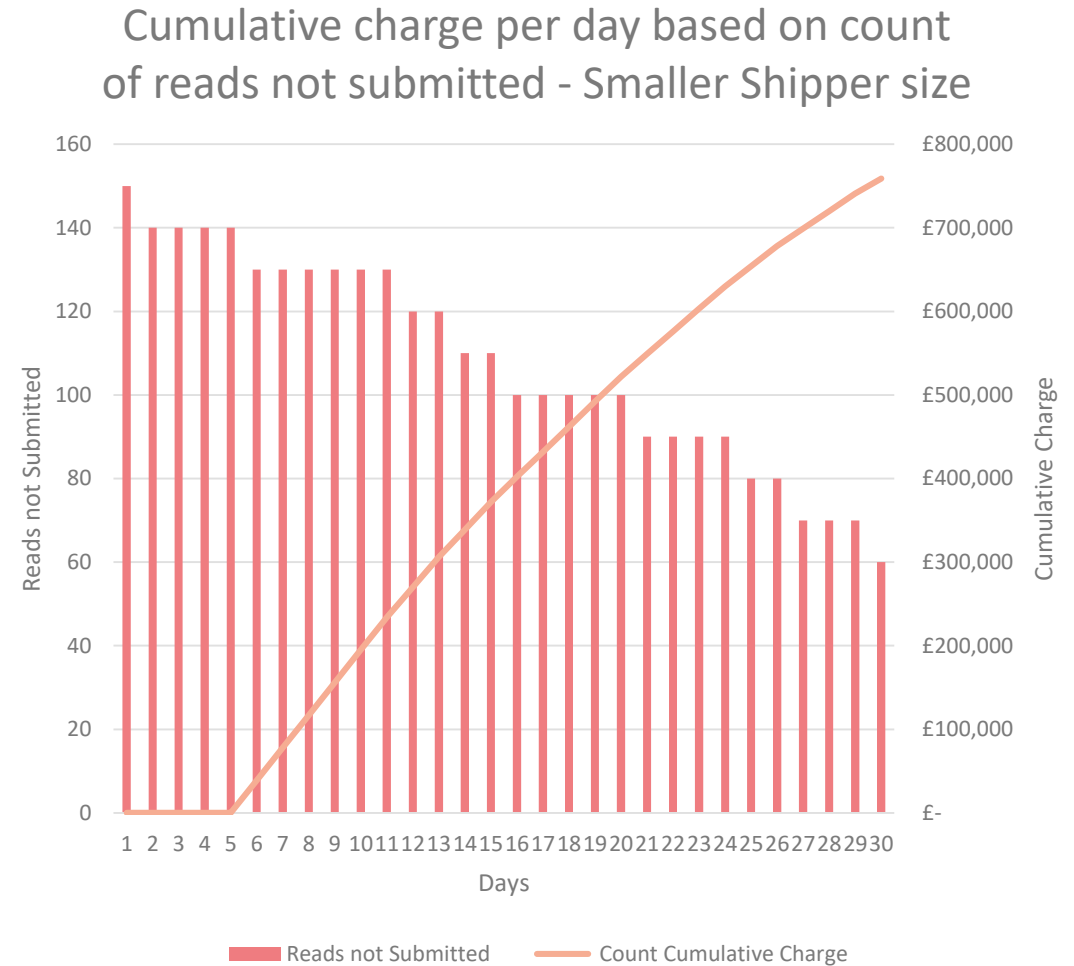
# Example 1 – Party B daily charge for missed reads

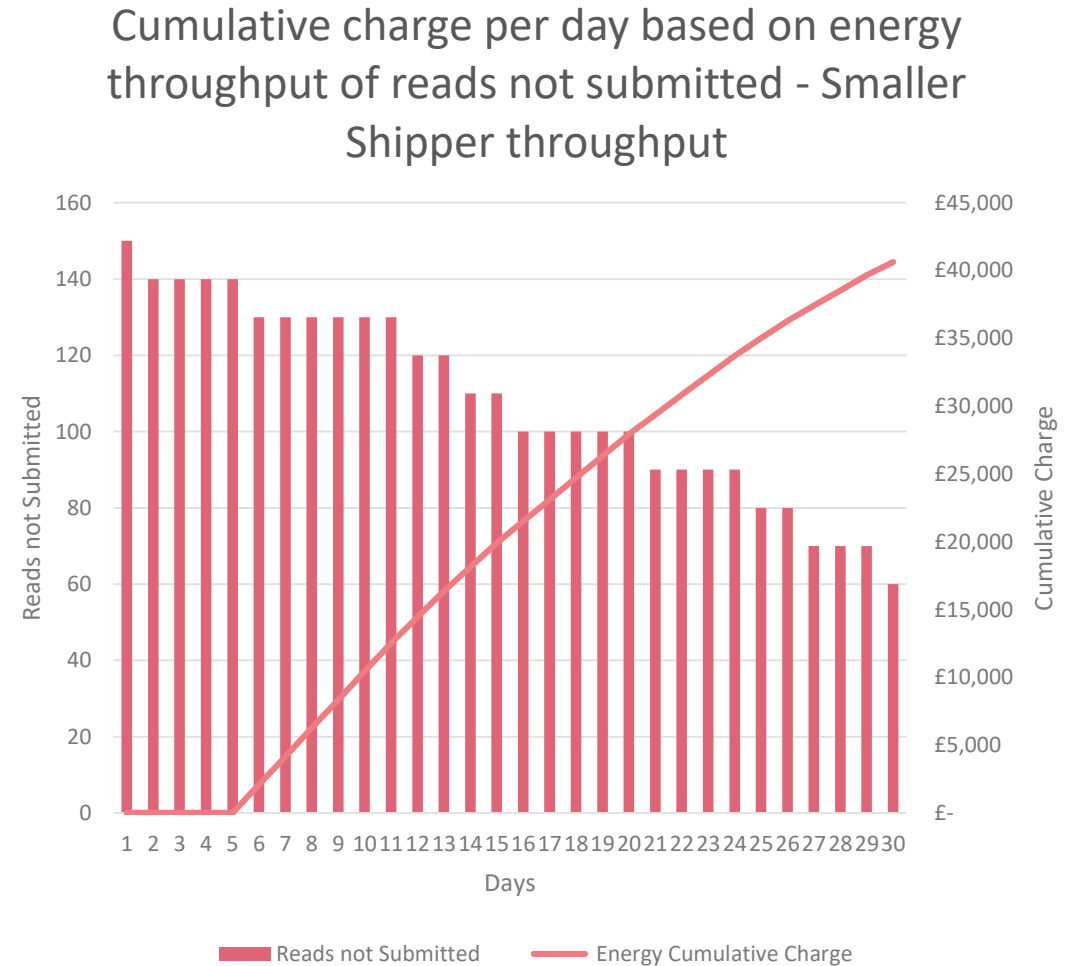Cumulative charge per day based on count of reads not submitted - Larger Shipper size



- 300 sites in total – higher throughput than party A
- Obligation to submit 300 reads per day
- Charge per day per missed read - £300
- Charges start at D+5
- Day 0 – 150 reads not submitted
- Day 30 – 60 reads not submitted
- Cumulative charges for month - £759,000

- Cumulative charges for month for 0 reads submitted - £2,250,000

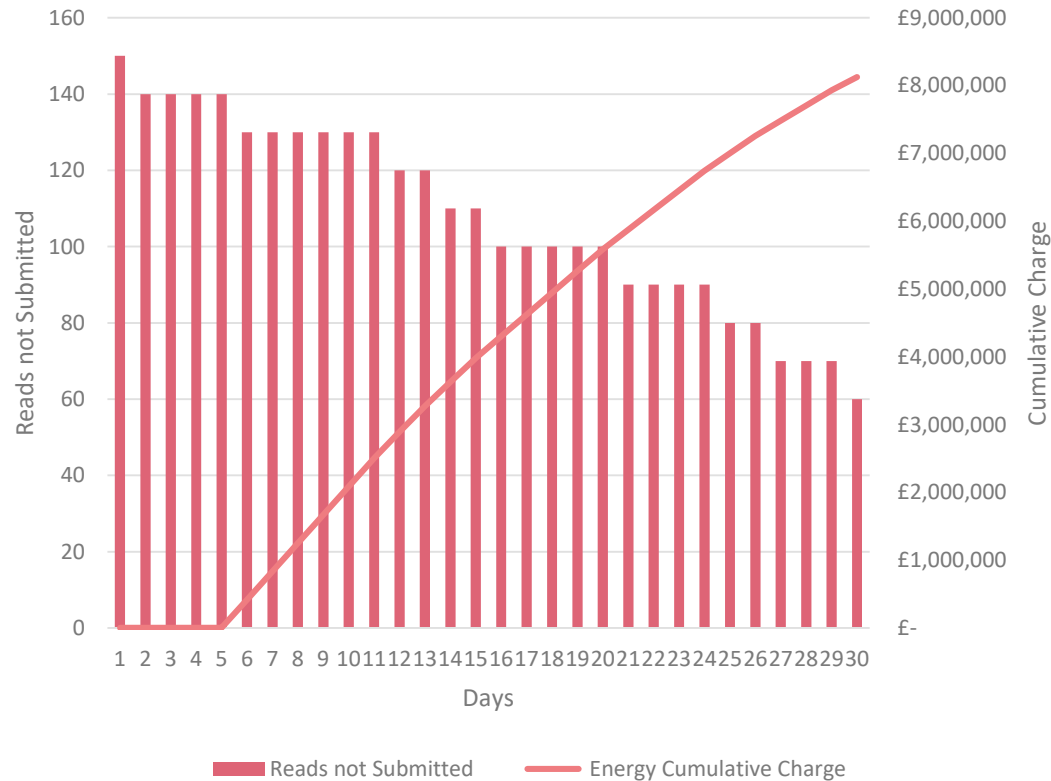# Example 2 – Party A daily estimated throughput charge

- 300 sites in total – lower throughput than party B

- Obligation to submit 300 reads per day

- Charge per day per missed read - £16.05
  - Average site AQ (293,000 kWh)
  - Price - £0.02

- Charges start at D+5

- Day 0 – 150 reads not submitted

- Day 30 – 60 reads not submitted

- Cumulative charges for month - £40,619

- Cumulative charges for month for 0 reads submitted - £120,411

Cumulative charge per day based on energy throughput of reads not submitted - Smaller Shipper throughput



Legend: Reads not Submitted | Energy Cumulative Charge

# Example 2 – Party B daily estimated throughput charge

### Cumulative charge per day based on energy throughput of reads not submitted - Larger Shipper throughput
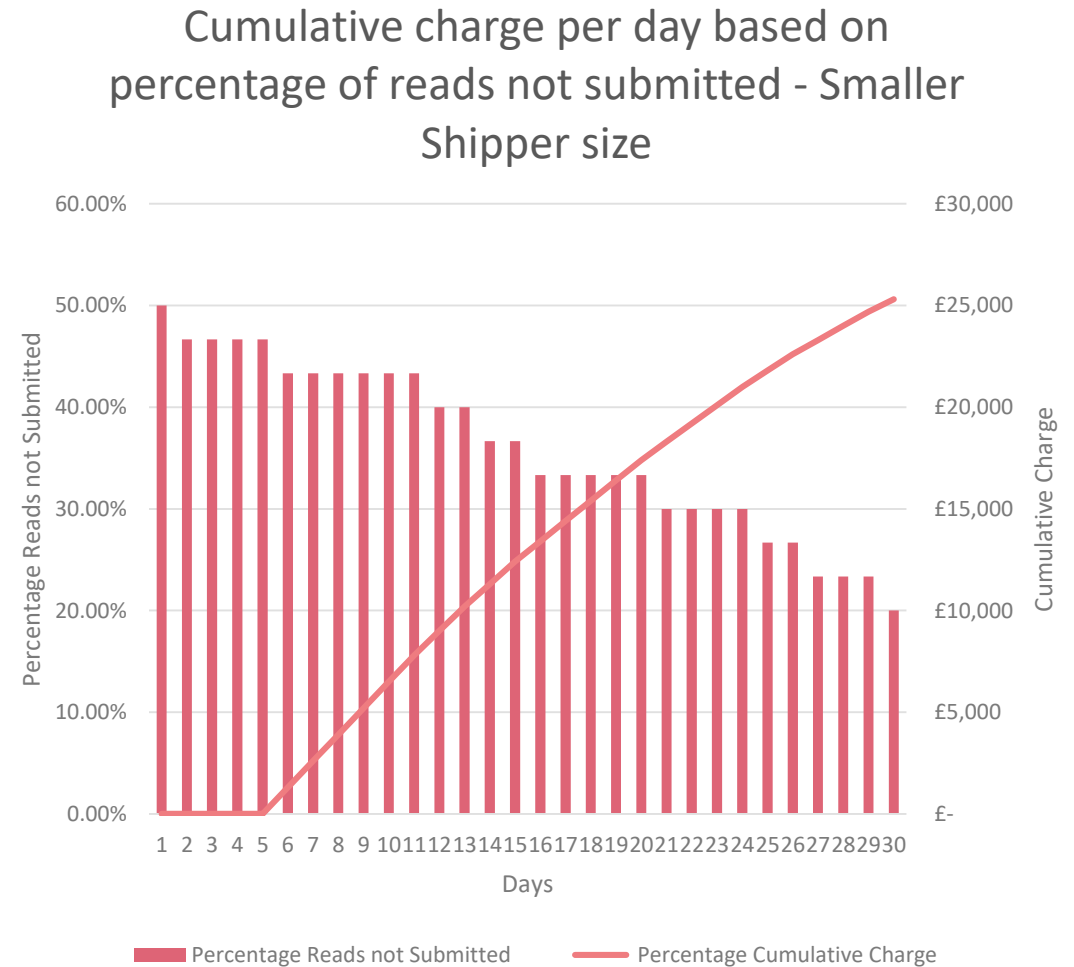


- 300 sites in total – higher throughput than party A
- Obligation to submit 300 reads per day
- Charge per day per missed read - £3,210.96
  - Average AQ of sites (58,600,000 kWh)
  - Price - £0.02
- Charges start at D+5
- Day 0 – 150 reads not submitted
- Day 30 – 60 reads not submitted
- Cumulative charges for month - £8,123,726
- Cumulative charges for month for 0 reads submitted - £24,082,192

# Example 3 – Party A Percentage of reads achieved

- 3,000 sites in total – lower throughput than party B

- Obligation to submit 100% reads per

- Charge per day per missed percentage - £3,000

- Charges start at D+5

- Day 0 – 150 reads not submitted

- Day 30 – 60 reads not submitted

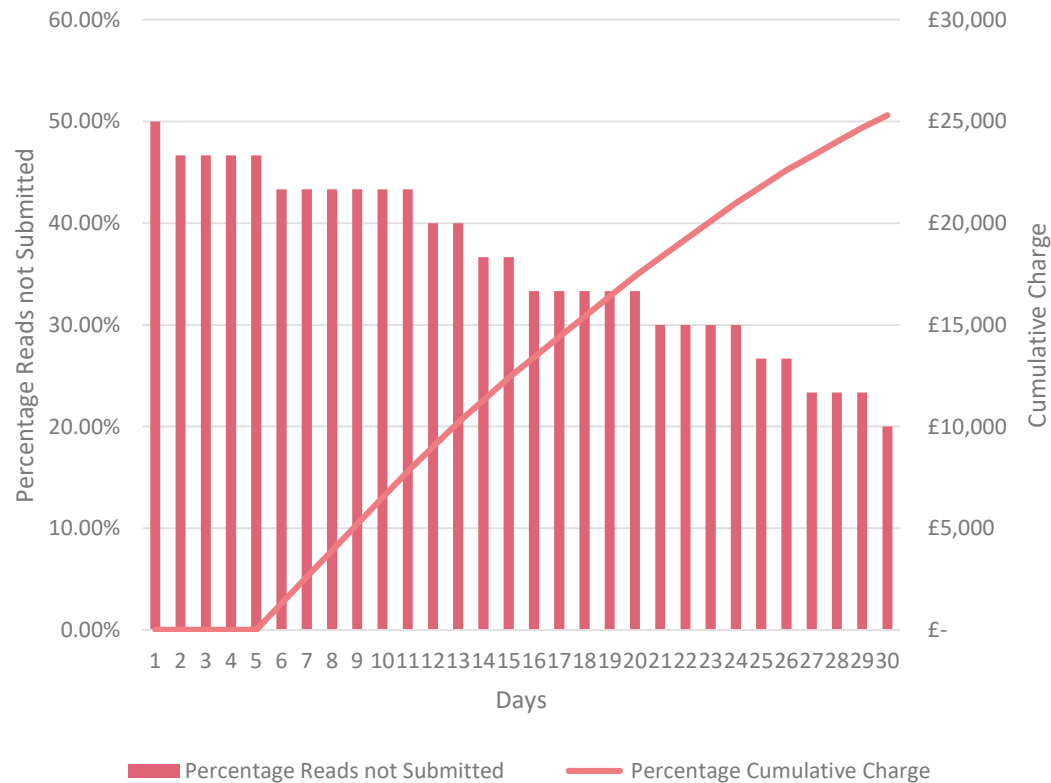- Cumulative charges for month - £25,300

- Cumulative charges for month for 0 reads submitted - £75,000



Cumulative charge per day based on percentage of reads not submitted - Smaller Shipper size

# Example 3 – Party B Percentage of reads achieved

## Cumulative charge per day based on percentage of reads not submitted - Larger Shipper size
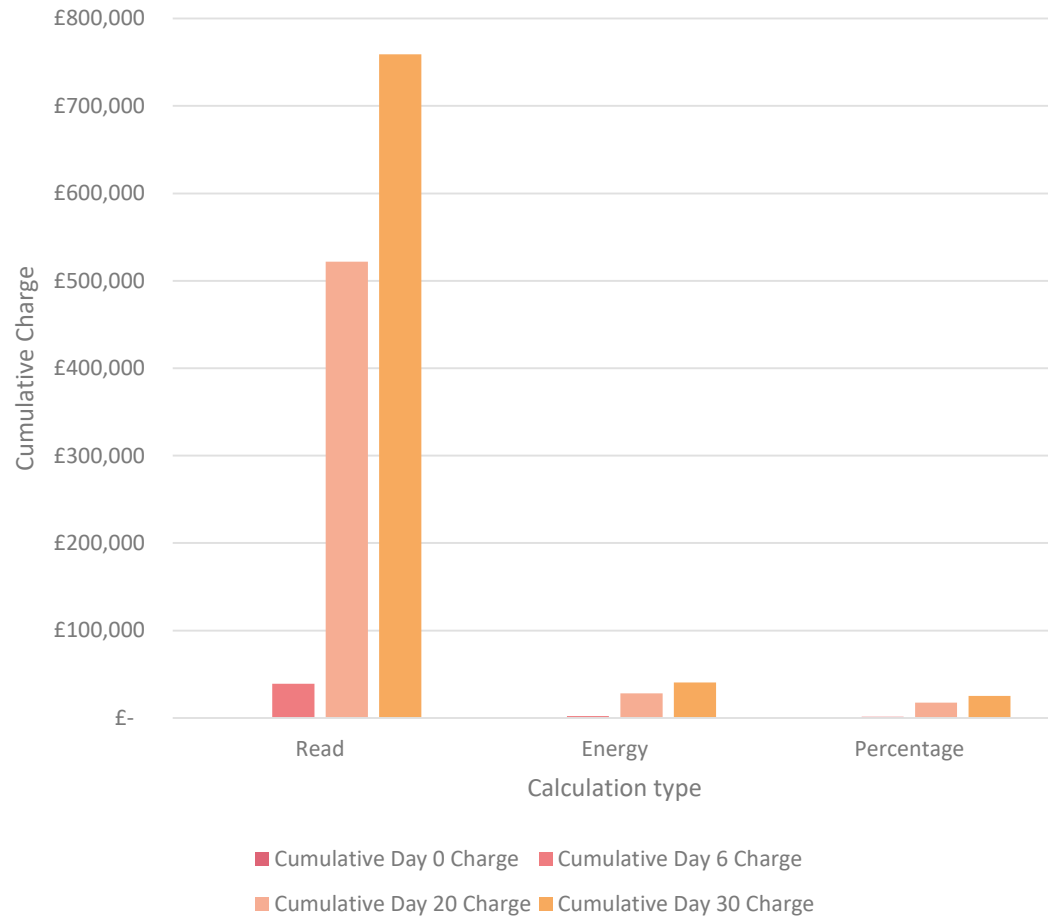


- 300,000 sites in total – higher throughput than party A

- Obligation to submit 100% reads per day

- Charge per day per missed percentage - £3,000

- Charges start at D+5

- Day 0 – 150 reads not submitted

- Day 30 – 60 reads not submitted

- Cumulative charges for month - £25,300

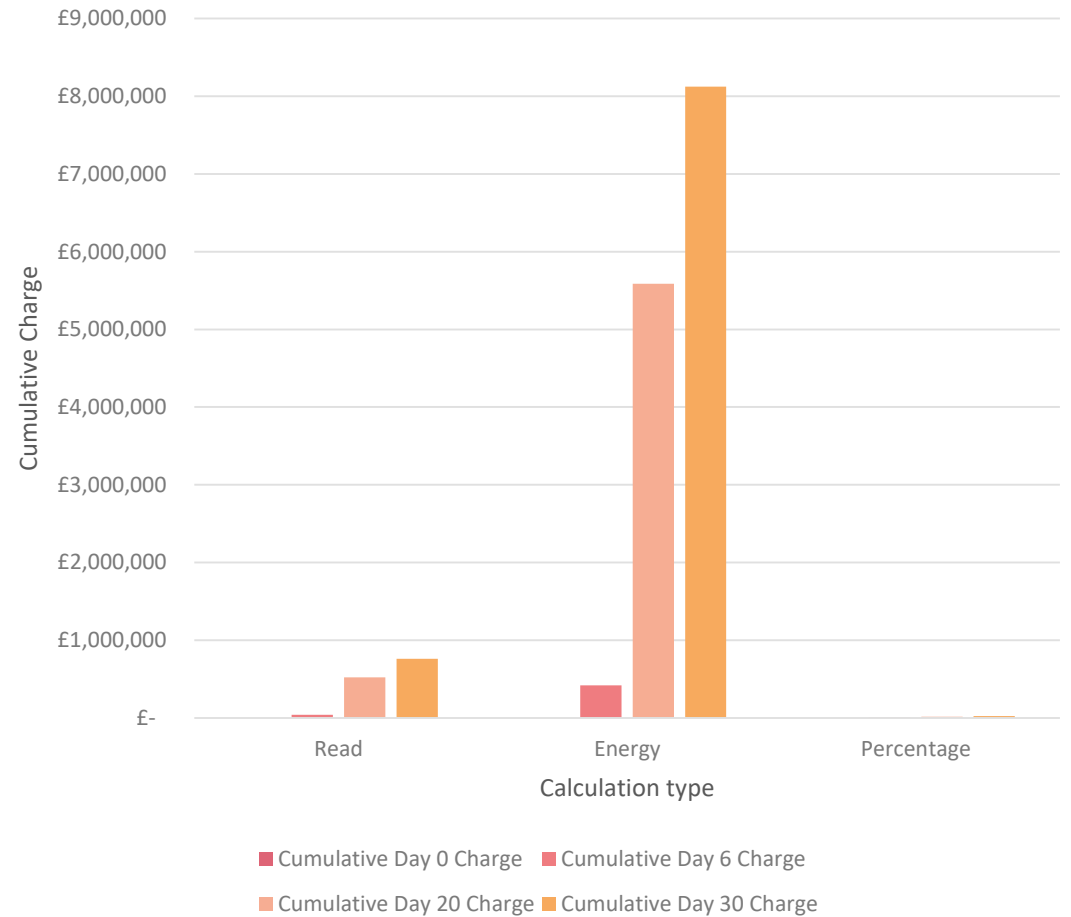- Cumulative charges for month for 0 reads submitted - £75,000

# Summary



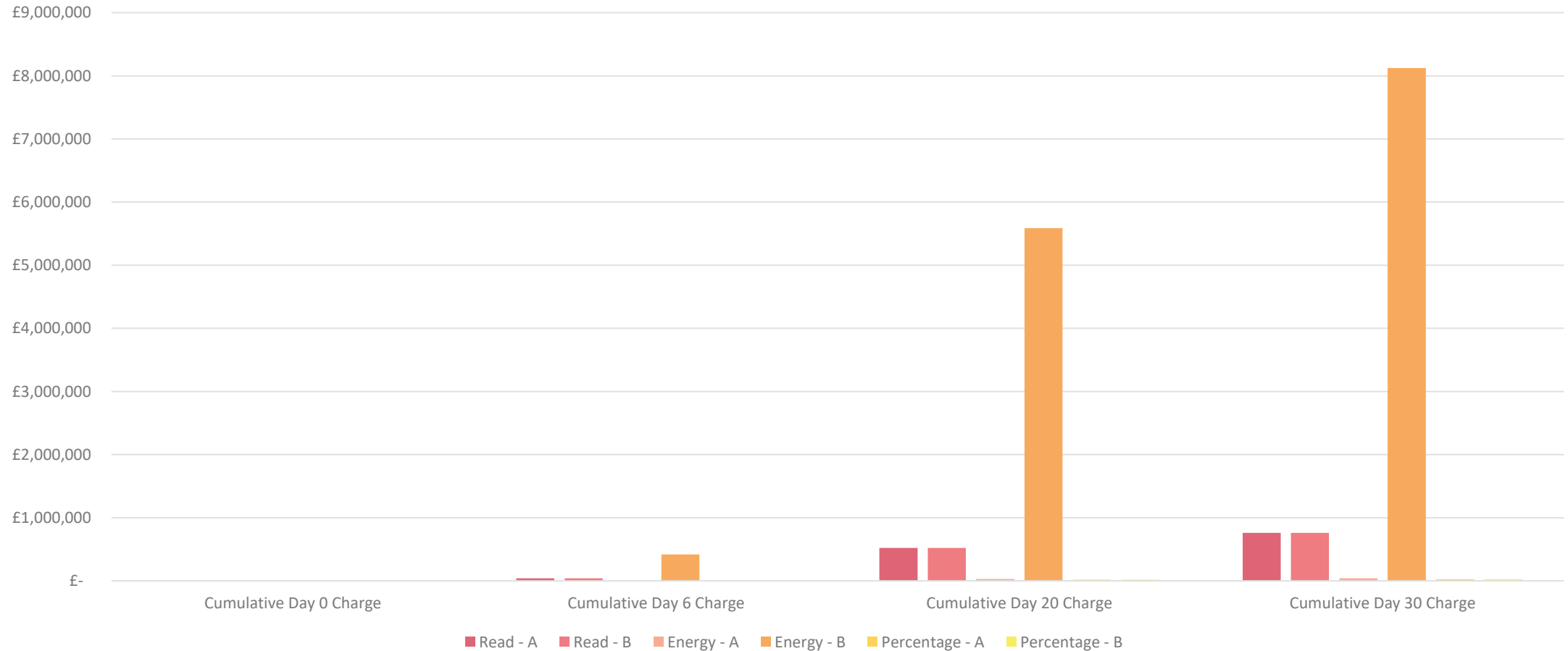Cumulative charge based on Party A

Cumulative charge based on Party B

# Summary – throughput and Calculation type

Cumulative charge across 30 days based on Smaller and Larger Shipper size and calculation type

# Summary table

| Calculation Type | A | | | B | | |
|---|---|---|---|---|---|---|
| | Read | Energy | Percentage | Read | Energy | Percentage |
| **Cumulative Day 0 Charge** | £ - | £ - | £ - | £ - | £ - | £ - |
| **Cumulative Day 6 Charge** | £ 39,000 | £ 2,087 | £ 1,300 | £ 39,000 | £ 417,425 | £ 1,300 |
| **Cumulative Day 20 Charge** | £ 522,000 | £ 27,935 | £ 17,400 | £ 522,000 | £ 5,587,068 | £ 17,400 |
| **Cumulative Day 30 Charge** | £ 759,000 | £ 40,619 | £ 25,300 | £ 759,000 | £ 8,123,726 | £ 25,300 |

# Suggestions for use of incentive calculation for PARR reports

| PARR | Read | Energy | Percentage |
|---|---|---|---|
| 2B.1 Estimated & Check Reads | Read | Energy | |
| 2B.2 No Meter Recorded in SP | Read | | Percentage |
| 2B.3 No Meter Recorded and data | | | Percentage |
| 2B.4 Shipper Transfer Read Performance | Read | Energy | Percentage |
| 2B.5 Read Performance | Read | Energy | Percentage |
| 2B.6 Meter Read Validity Monitoring | Read | Energy | Percentage |
| 2B.7 No Read Class 1,2,3 or 4 | Read | Energy | Percentage |
| 2B.8 AQ Correct by Reason Code | | Energy | Percentage |
| 2B-9 Standard CF AQ > 732,000 kWh | | Energy | Percentage |
| 2B.10 Replaced Meter Reads | Read | Energy | Percentage |

# Conclusions and next steps
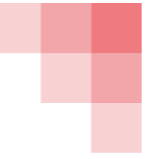
- One size does not fit all

- Each risk needs to have the settlement risk and risk to consumers assessed to determine the appropriate incentive regime

- Further work will need to be done to determine appropriate financial levels of avoidance costs and benefits

- Supporting analysis will be needed to evidence the best approach

- Any proposals for UNC modifications will need PAC support

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