



Consultation Response

By email to smartmetering@decc.gsi.gov.uk

Ref: URN 11D/868

24 November 2011

Smart Metering Implementation Programme – DCC Licensing Team

Department of Energy and Climate Change

3 Whitehall Place

London SW1A 2AW

Dear Sir/Madam

ELEXON's response to DECC's Smart Metering Implementation Programme: a consultation on the detailed policy design of the regulatory and commercial framework for DCC (September 2011).

I welcome the opportunity to provide ELEXON Limited's views on the design of the regulatory and commercial framework for the DCC. We remain totally committed to the success of the smart arrangements and are therefore keen to ensure that all the new smart roles, including that of the DCC, are delivered effectively, efficiently and economically. We do so for two principal reasons:

- The DCC and its services are critical to both industry and consumer experience and confidence. Their success is therefore central to realising the benefits of the Smart Programme; and
- The DCC will be delivering meter data for use in existing industry systems and processes. An ineffective DCC could fatally compromise the quality of the data used in settlement and other billing processes. ELEXON provides the electricity settlement processes on behalf of the industry.

ELEXON has provided detailed responses to the majority of the questions and these are provided in the attached document. Should the Programme wish to discuss any of our responses we would be very willing to do so. We have not provided a response to Section 6; we believe that these technical questions are better answered by providers of communication services.

I would like to draw out the following points from our response for your overall attention.

Incentive Regime

Whilst ELEXON has successfully delivered the electricity trading arrangements for over 10 years without a contract or explicit incentives, it has sometimes proved challenging to demonstrate to BSC Parties how we are focused on managing costs and improving services. Therefore we have been wholly transparent in our activities and costs and employed vehicles such as our Business Plan and monthly reports to demonstrate our value.

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Dependent on who is the eventual DCC, introducing an incentive regime may or may not of itself drive the right behaviours and outcomes. If well designed it could valuably distinguish the responsibilities of the DCC from those of its service providers, and help in monitoring and demonstrating the effectiveness and efficiency of the DCC.

The consultation discusses a wide range of tools that may form part of an incentive regime. From our experience of delivering key central services to the industry, techniques should not be considered in isolation, rather as part of an integrated incentive framework. We would also urge that the model should not be overly complex. An unduly complex model dilutes messages and risks driving perverse behaviours. It can also become a significant and disproportionate burden to deploy, monitor and manage for both those subjected to it and those applying it.

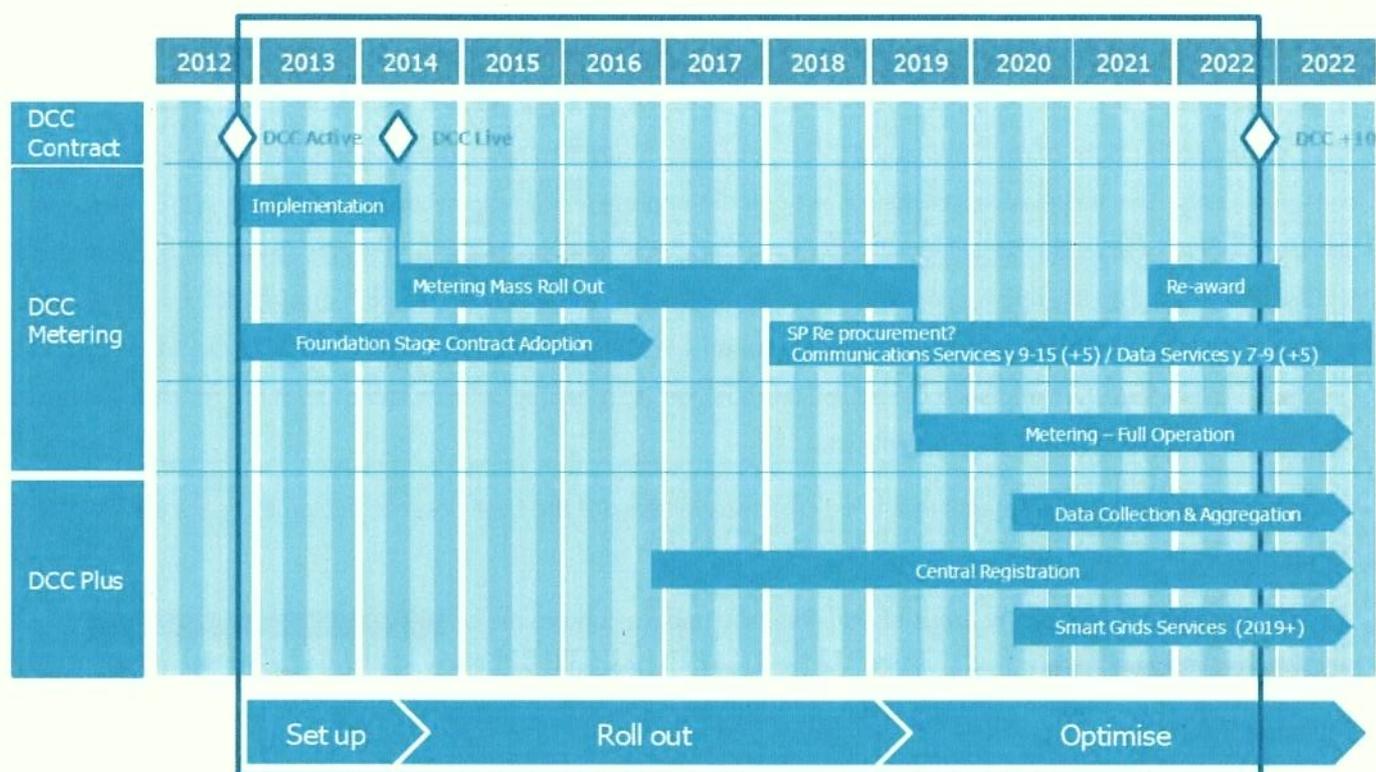
In setting the incentive regime we believe candidate areas should be assessed on two prime aspects:

- the extent to which the DCC can influence the successful outcomes from the activity; and
- the extent to which the DCC can predict the external inputs to the activity.



The challenges faced by the DCC across the first licence period are largely unique. We therefore believe that this needs to be recognised within any incentive regime and would recommend a model that allows differentiation between the distinct phases of implementation, rollout and service optimisation. The drivers and approximate timings are shown in the diagram overleaf:

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We would also suggest that the Programme uses the feedback from this consultation and provides further definition around the desired incentive regime prior to the start of the DCC award process. The alternative of allowing DCC licence applicants a totally free rein to propose their own incentive regimes will pose a substantial issue for the Programme in evaluating different offerings and could risk challenge on award.

We have discussed the Performance Incentive regime in more detail in an attachment to this response which forms our response to Question 83.

Licensing Process

We agree the content of the DCC licence outlined in the consultation and that the licence conditions are established as 'Special' Conditions.

Whilst recognising the need to establish the DCC in a timely fashion, the indicative timings of some of the stages are very tight and leave neither DECC nor bidders much flexibility. We are particularly concerned about the limited opportunity to assess the service provider contracts during the ITA stage. Dependent on the number of parties still in negotiation and the firmness of the contracts at this stage, this exercise could prove a significant burden and hence cost for applicants and the Programme. It may indeed serve only to prompt the introduction of cost reopeners for DCC, which will drive subsequent variations and escalating costs. We also urge the Programme to provide clarity on the likely start date of the award process. The current Q2 milestone for starting the award process is too broad and



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suggests either a 4 or 6 month lead time from now: such planning assumptions are key to allowing bidders to understand when to commence mobilisation, provide confidence in the process and drive costs.

We also urge early sight of the detailed DCC requirements in order to resolve the speculation and uncertainty that currently exists. This includes establishing clarity on the boundaries of responsibility between the DCC, its users, service providers and other bodies for all aspects of the end to end smart solution (e.g. security) and establishing the DCC service (e.g. the differing responsibilities of the SMIP, DCC and Service Providers during the key implementation phase). We believe that this could be achieved through DECC's suggestion of issuing a draft of the SEC in Q1 2012 (in plain English form). Taking such steps would greatly assist potential bidders and allow them to more fully assess and cost the opportunity and its inherent risks.

Communicating clear requirements in a timely manner will ensure the best possible outcome for the award process for both DECC and any bidders

If you would like to discuss any areas of our response, please contact me on [REDACTED]

[REDACTED]

Yours faithfully

[REDACTED]

[REDACTED]

A consultation on detailed policy design of the regulatory and commercial framework for DCC

Chapter 2: Proposed regulatory approach to DCC

The Prohibition Order

Question 1: Please provide views on the approach to basing the prohibition upon contracting with all licensed suppliers in respect of all domestic smart meters, and on the way in which the specific wording of the prohibition should be developed.

This reflects the primary purpose of the DCC and thus correctly targets the prohibition. Keeping the area narrow also limits the risk of inadvertent capture. We therefore support the suggested approach

Question 2: Do you think there will be any persons other than DCC who might inadvertently be captured by a definition structured in this way?

We see little scope for any other persons to be inadvertently captured by the drafting. We suggest however that the wording be checked against the role of Meter Operator /Installer. It is feasible that a Meter Operator/Installer may seek to contract to offer services to all licensable suppliers in relation to every Smart Metering System. If this were to occur the Meter Operator/Installer will be communicating information to the meter on behalf of a supplier when installing or physically working on the meter. To avoid this situation the definition could refer to 'remote' communication with the meter, as this will be limited to the DCC role.

Question 3: Do you have any other comments on the form of the licensable activity?

No

Consequential Changes to Legislation

Question 4: Please provide comments on the proposed changes to legislation identified in Table 2.1 and Table 2.2 and any other possible changes that you consider might be appropriate.

We have no comments in relation to the proposed changes to legislation in the consultation document.

In addition we believe the interaction with the Climate Change and Sustainability Act 2006 should be considered further. This Act imposes energy efficiency obligations on suppliers and distributors e.g. obligations regarding carbon reduction. If DECC intends to impose energy efficiency obligations on DCC then the Gas and Electricity Acts may require amendment to include DCC in the list of those obliged to comply with the Climate Change and Sustainability Act 2006.

licence Conditions - General

Question 5: Do you agree with the proposal to have a single document with a single set of licence conditions that apply to both licences?

Yes we believe that establishing a single set of licence conditions in a single document is the right approach. Doing this will ensure that the requirements on the DCC in relation to gas and electricity are the same and thereby contribute to the harmonising of gas and electricity processes which will ultimately benefit the consumer, particularly during the change of supplier process.

Question 6: Do you agree with, and have any comments on, the proposed approach to establish all of the DCC licence conditions as "special" conditions?

We support the proposed approach as appropriate for a single licensed body and recognising the draft regulation currently before parliament.

Question 7: Do you have any comments on the scope and nature of the consequential licence changes that we propose to make?

The proposed changes to condition 26 of the Electricity Supply licence and condition 10 of the Electricity Distribution licence state that the DCC licensee may be able to interrupt supply and therefore they may need to be provided with information regarding customers who require advance notice. We believe that the decision on whether to interrupt supply should sit with the supplier (or distributor in limited cases) and therefore responsibility for ensuring customers are provided with advance notice should also sit with the supplier. We agree that providing this information to the DCC could provide an additional safety check to prevent vulnerable customers losing their supply without sufficient notice. However we feel that if this information is provided to the DCC, it should be clear that this does not mean that the overall responsibility is shifted from the supplier.

From a settlement perspective, we have processes in place to ensure that changes to energisation status and disconnection activities are notified to the Supplier Meter Registration Service (SMRS) so that the consumption can be accurately reflected into settlement. Again it is important that the supplier or

distributor is aware if supply is likely to be interrupted for any significant length of time so they can make the required updates to the appropriate SMRS.

Question 8: Are there any other consequential licence changes that you consider might be necessary as a result of the creation of the new licensable activity?

No

Other Provisions to the Prohibition Order: Geographic Scope and Duration

Question 9: Please provide any comments on the proposed approach in relation to geographic scope of the DCC licence and provisions relating to its duration.

We agree that that the DCC licence should cover Great Britain as both the electricity and gas trading arrangements relate to Great Britain. Any misalignment between this or the coverage of the individual Supply and aggregate Distribution licences would necessitate dual arrangements and increase costs.

We agree that the duration of the licence should be specified in the licence itself and that any changes to the duration should be notified.

Chapter 3: DCC licence conditions

General Objectives of the DCC

Question 10: Do you agree with the proposed general objectives of DCC set out above?

Yes but see answers to Questions 13 and 14 below.

Question 11: Do you think it is necessary to include any statutory duties on DCC in the Gas and Electricity Acts or is it appropriate to address these issues in the DCC licence alone?

Yes, we believe it is appropriate to include appropriate statutory duties within the relevant Acts. Reference is made in chapter 2 (of the consultation) to a Prohibition Order and we assume that the requirements of such Order will be reflected in amendments to the Electricity Act 1989 and the Gas Act 1986. From a transparency and consistency perspective, we believe it would be helpful to include references to appropriate statutory duties in the respective Acts. The Electricity Act 1989 requires network licensees to develop and maintain an efficient, co-ordinated and economical system and to facilitate competition in the supply and generation of electricity and there are equivalent provisions in the Gas Act. The licences themselves reflect these duties as do the commercial and network codes associated with the licensed activities. The respective Acts also include provisions for modification of

licences and references to the Authority in the event of disputes. Since the DCC will provide comparable network services with similar objectives both in its licence and in the SEC licence then we can see no compelling reason why the DCC obligations and duties should not be given statutory force.

Question 12: Do you agree that any obligation to facilitate competition in the area of distribution should be considered as part of the implementation of any future smart grids related arrangements?

We believe it would be sensible to include an obligation to facilitate competition in the area of distribution for two reasons. First, the DCC's operation will directly or indirectly affect both distributors and consumers and the obligation should be explicitly referenced.

Second, work on the development of smart grids is progressing rapidly and by the time the DCC arrangements are in place the interactions between smart grids and smart metering will be further defined. Incorporating an obligation now will obviate the need to introduce the requirement in parallel with, or soon after DCC implementation and will enable the DCC to take account of smart grid related arrangements from the outset.

Question 13: Do you agree with the approach proposed in relation to the protection of consumers?

No, whilst we entirely agree that the DCC should be required to protect the interests of consumers, experience dictates that a more explicit reference within the objectives would be helpful in assisting the DCC, users of the DCC's systems and the SEC panel to operate effectively. Failing that a guidance note (similar to that DECC provides to Ofgem with regard to consumers and the environment http://www.decc.gov.uk/assets/decc/what%20we%20do/uk%20energy%20supply/energy%20markets/regulation/1_20100121172046_e_@@_guidancegaselecmarkets.pdf) should be provided.

Question 14: Do you think DCC should have a separate objective to promote (or facilitate) energy efficiency?

It is difficult to envisage what an explicit objective on the DCC to promote energy efficiency might achieve over and above the obligations to develop, maintain and operate [and procure] an efficient communications system and to promote or facilitate competition, particularly if the latter obligation is expanded to include energy efficiency services, metering services and other energy related services.

If DECC does conclude that energy efficiency should be explicitly referenced then we would suggest the obligation on the DCC should be to facilitate this rather than promote it since promoting energy

efficiency seems a more appropriate obligation for a regulator or supplier actively engaged in providing such services to consumers.

The Smart Energy Code licence Condition: The Scope of the SEC set out in the DCC licence

Question 15: Do you agree that SEC licence condition should be drafted so as to provide flexibility over the future scope of SEC, i.e. that the scope of the SEC in the DCC licence condition should be drafted in a permissive manner?

Yes. From our experience of managing the BSC we believe that licence conditions should be permissive. A robust change management process when coupled with appropriate and proportionate regulatory oversight can ensure that appropriate enhancements to the SEC and any consequential obligations on the DCC and others are properly evaluated without the need for redress to time-consuming and potentially costly legislative and licence changes.

Under all models consideration will also need to be given to how this is reflected in the commercial contracts that support delivery of the regulatory framework.

The Smart Energy Code licence Condition: SEC Applicable Objectives

Question 16: What are your views on the SEC Applicable Objectives set out above?

These seem appropriate as far as they go but please see the response to Questions 12 and 13 above – in our view a more specific reference to consumers and to distribution is required (the latter particularly if facilitating the implementation of smart grids is included in the DCC's responsibilities).

Generally, except where the objectives relate explicitly to obligations or services under the DCC's control, our strong preference would be for the objectives to refer to facilitation rather than promotion of a principle or service.

Question 17: Do you agree that the SEC should be designed to take into account consumers' interests by meeting its applicable objectives, rather than having an explicit objective related to the protection of the interests of consumers?

Please see our response to Question 13; an explicit reference to consumers would be desirable in our view.

Question 18: Should there be a SEC objective related to promoting (or facilitating) efficiency of energy networks?

Please see our response to Question 12. There will be interactions between the DCC's services and those of energy network operators who will have certain rights and obligations within SEC; where appropriate it seems sensible that the SEC and DCC services facilitate enhancement of these services. We would suggest that the objective should be to facilitate rather than promote since the primary obligation on providing efficient energy networks rests with network operators.

Question 19: Do you think the SEC should have a separate objective of promoting (or facilitating) energy efficiency?

No. Please see our response to Question 14 i.e. we do not believe a separate objective on promoting energy efficiency is appropriate; objective (f) (related to promoting or facilitating competition in energy efficiency, metering services etc) should suffice. In our view, where relevant, obligations on the DCC should also be reflected in the SEC's obligations.

The Smart Energy Code licence Condition: SEC Modification Arrangements:

Whilst there is no question on this section, we note that DECC intends to progress the SEC Modification Procedures as part of detailed drafting of the DCC licence conditions and in light of the parallel development of the DCC. We would remind DECC of the findings of Ofgem's Code Governance Review and, given that this recommended the broader adoption of the BSC model, that the BSC provides a good starting point for developing these arrangements.

Service Provision

Question 20: Do you agree with the definitions of the services that DCC should be required or permitted to provide?

Yes we agree the definitions are reasonable however we believe that one key element that must be stressed is the importance of ensuring the integrity of the DCC. Therefore the 'appropriate authorisation' and the compliance definitions must ensure that the DCC is not required to deliver services to smart meters and service users that might compromise the DCC, particularly as a result of having to support 'non-compliant' metering systems

In keeping with this it is also important to ensure that where the DCC is 'required' to deliver services it can levy appropriate charging. Where it is unable to exercise discretion it is inappropriate for it to bear the risk of delivering the service.

With regards to 'other wholly unrelated services' we believe that provided robust financial ring-fencing and accounting arrangements are in place, the extent of services should not, in our view, be limited to a

de-minimis level (instead services should be assessed to ensure that the delivery and integrity of the DCC is not compromised and that the competitive market is not adversely affected).

We recognise that the Authority's approval may be needed before additional services could be undertaken but in line with other provisions in the DCC licence and SEC, provisions should be permissive rather than restrictive; our own experience with the limitations in the BSC concerning what ELEXON, as BSCCo, is permitted to do bear this out. There will be circumstances where it is technically and commercially the right thing for the DCC to deliver a service itself. Such situations should be subject to an appropriate consents process rather than requiring expensive and time consuming removal of restrictions.

Question 21: In relation to which non-compliant metering systems should DCC be required to offer services?

The DCC should only be required to offer services to non compliant meters where it does not endanger the service and it does not carry an unreasonable cost to the industry. We suggest non compliant metering systems are subject to a dispensation authorised by the appropriate body (e.g. SEC Panel).

Question 22: In relation to which non-compliant metering systems associated with energy supply at consumer premises should DCC be permitted to offer services?

The DCC should only be required to offer services to non compliant meters where it does not endanger the service and it does not carry an unreasonable cost to the DCC (and therefore industry).

We need to ensure that metering systems meet the requirements for Settlement purposes under the BSC. As reliance may be placed on metering being compliant with the SEC for BSC purposes it is imperative that non compliant metering systems are not permitted where they do not meet Settlement requirements.

Question 23: What information should be made available to all users about:

- elective services;
- value-added services?

Should information be restricted to that required to assess the impact on other users of DCC services or should there be full transparency? Should DCC be required to make available the detailed commercial terms and conditions of such services?

There are several regulatory models which require service providers to set out a methodology which

allows those wishing to use those services to calculate the cost of doing so; such arrangements typically include non-discrimination provisions and the right of referral in case of a dispute. There are other models which require the purchaser to indicate the range of services required and then the provider can establish indicative prices around which contracts for providing those services can be struck.

We would note that the BSC and its subsidiary documents contain tables of charges for the provision of some services.

Any one of these models would work for elective services but for value added services we consider that these should be subject to a bilateral agreement between the DCC and the purchaser; whilst indicative pricing might be appropriate the DCC should not be required to make publicly available the commercial terms and conditions of such services which purchasers might see as being commercially sensitive (see Q24).

Question 24: Do you think the detailed terms and conditions for elective and value-added services should be set out in the SEC or included in bilateral agreements between DCC and persons to whom it is providing services?

We would suggest that there are three key elements to this:

1. The principles underpinning elective and value added services should be established and documented within the SEC, including the charging methodology;
2. The detailed terms and conditions should be within bilateral agreements thereby allowing for flexibility around such areas as named contacts, charges updates, etc.
 - For these services we would propose the use of standard Terms and Conditions reviewed by the SEC Panel but with commercial and contract administration variables as a 'template Schedule' to the contract thus giving appropriate certainty to service users and the Authority but avoiding an expensive and inefficient change process.
3. In addition we would suggest that the SEC has a disputes mechanism to ensure that service users are able to challenge and that criteria are established against which such disputes can be raised.

Question 25: Are there any other matters that we have not addressed related to the nature of services provided by DCC? (Note that provisions addressing independence and non-discrimination in the provision of DCC services are covered in paragraphs 3.119 to 3.120).

One element which has not been addressed as part of this suite is any credit arrangements for service

users. Within the energy industry it has been common to ask for credit (in letter or cash form) in advance of any provision of services to ensure that the service user can cover any accrued charges. Either payments will need to be made in advance or some arrangement of this nature will be necessary to protect the industry and DCC from the default of SEC signatories and should form part of the SEC.

Procurement: Resources to be Procured

Question 26: Do you agree that DCC should be required to externally procure specific services and have principles that determine what other services it should externally procure?

We agree that clarifying what must be procured, and principles around what other services should be procured, within the Legal Framework would be beneficial. However where it is possible for a service to be externally procured or delivered by the DCC itself, then subject to suitable permissions the latter should be permitted.

We therefore recommend that while the Data, Communications and compliance audit elements of the services must be designated for external procurement, all other services should be left to the discretion of the DCC with its overall mandate to deliver services economically and effectively. The SEC should ensure that DCC has this flexibility, with suitable controls in place.

Procurement: Procurement Objectives and Approach to Procurement

Question 27: Do you agree with the procurement objectives for DCC identified above?

Yes

Question 28: Do you agree that DCC should be required to produce a procurement and contract management approach document?

We believe that as part of the DCC Award process applicants should outline their procurement and contract management approach and identify how it fulfils the principles outlined in the licence.

We recognise that subsequently publishing a high level procurement and contract management document could promote transparency in how the DCC contracts and thereby encourage confidence and competition in its procurements. However it is important that this document is aimed at the principles and approach and does not expand into a manual on how each individual contract is to be or has been procured or managed - indeed timing issues mean that the bulk of the first set of principal procurements will have been undertaken by DECC.

We believe that there is a useful parallel with the Contract Principles and Tender Framework Statement that the BSCCo is required to produce under the BSC. These models have worked well and could be applied to the DCC.

Question 29: We seek your views as to whether the procurement and contract management approach document should be required to be submitted for approval by the Authority and/or the Secretary of State.

We believe that the submission of a Procurement and Contract Management Approach should form part of the DCC licence Award process. This should then translate into a published document.

The successful DCC applicant will have a contract and a licence and be bound by the provisions of the SEC which will be designated by the Secretary of State with subsequent changes subject to regulatory approval. Unless there are significant changes to the smart metering arrangements in future which have a substantive impact on the provision of DCC services we see no merit in resubmitting the procurement and contract management approach for regular regulatory approval. Instead we believe that once the DCC is appointed the SEC Panel should be the focus for any future review and amendment to the approach document. Where a change is suggested to the SEC, from whatever source, then the DCC should confirm that the change does not impact its approach document. If it does, the DCC should seek agreement to the changes as part of overall change assessment process. This could be complemented by a requirement to review the approach from time to time, but again this activity should be focused by the SEC Panel.

We note that under the BSC the BSCCo (ELEXON) is required to produce and the BSC Panel consult on a Contract Principles (E 2.3) and, prior to commencing procurement, must prepare a Tender Framework Statement (E 2.7) for the BSC Panel. These models have worked well and use the Panel to provide an appropriate level of scrutiny. We therefore do not support the suggestion that the DCC's procurement and contract management approach document be subject to approval by the Authority or Secretary of State (other than as part of the initial DCC award process).

Independence

Question 30: Is the scope of the proposed prohibition on discrimination, which is limited to undue discrimination between uses or classes of users, adequate?

Yes

Question 31: Are any specific provisions needed which require DCC not to discriminate

between service providers? Or is it sufficient to rely on obligations on DCC to maintain and develop an economic system and, in the procurement of DCC services, to promote competition in the provision of such services?

The latter. The DCC should provide an experienced procurement delivery function following a best practice approach.

Question 32: Do you agree that DCC should be independent of service providers? Do you agree that a de minimis level of affiliation between DCC and service providers should be permissible?

We do not believe that there should be any degree of affiliation between the DCC and its service providers as it jeopardises the perception of the independence of the DCC in its central activity. The definition of service provider and to which roles this applies should be clearly defined so as to avoid DCC being prohibited from managing its operational business most effectively (we refer you to our comments in Q26)

Question 33: What level of affiliation do you consider should be set for the maximum level of shareholding or control of any individual service provider may have in DCC?

See Q32

Question 34: Do you agree with the business separation between DCC and users that is proposed? More specifically, do you agree that no DCC user that operates in a competitive environment should be permitted to have more than a 20% shareholding or control in DCC, and that DCC and its subsidiaries should not be permitted to have any shareholdings in users or service providers?

It is our view that the composition of the business ownership is not as important as the degree of influence that service users have. For example a 2% shareholding that granted the ability to nominate a Director would potentially be more damaging than a 20% shareholding with restricted voting rights or appointment powers.

However in addition to this it is key that potential new market entrants have confidence that the DCC and its service providers support the market as a whole and are not unduly influenced by individual existing users. This may best be achieved through an explicitly independent DCC.

Question 35: Do you agree that it is not necessary to explicitly require business separation

between DCC users and DCC service providers?

We believe it would be inappropriate for the suppliers to provide services to other users through the DCC where they might be able to gain competitive advantage. As with DCC independence, it is not simply a question of actual anti-competitive behaviour but also perception.

We would suggest that this should be covered within the procurement principles and be under the DCC's discretion.

Question 36: Should DCC be prohibited from using confidential information for any purpose other than the licensed DCC activity? Should DCC be obliged to impose this restriction on service providers contractually?

DCC will be constrained in its use of data/information by the definition of the services it provides. We are not sure if this is referring to 'confidential' data or 'personal data'. The DCC should only use confidential or personal data for purposes it is permitted to do so.

This must also be applied contractually to the service providers. It is essential that consumer data and hence confidence is not put at risk by the DCC or its service providers.

For service procurements and when discussing the possible leveraging of its assets, the DCC must be able to use data relating to its services – notably data relating to requirements and volumetrics. The definition of what is confidential must recognise this requirement.

Financial Viability of the DCC, Business Continuity and Special Administration

Question 37: To what extent do you believe that the existing financial ring fencing provisions (and those proposed by Ofgem in its recent consultation on this issue) should be included in DCC's licence?

The proposed constraints are largely appropriate however the holding of the financial year's resources is not appropriate for a pass through cost and thin asset business.

Financial ring fencing in network licences is an important tool but if applied to the DCC it should be structured in such a way that it does not prevent the DCC accessing services from within its own broader business where this is most efficient e.g. some corporate functions such as HR and Finance will best be shared with other business units to get the best value; financial ring fencing must not prohibit this.

Question 38: Do you agree that a flexible approach to financial security should be adopted and, if a financial security is required, what level of financial security should be provided?