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Dear Ian

Consultation on legal drafting for Stage 1 of the Smart Energy Code

1. In our response to the government's last consultation on the Smart Energy Code (SEC), British Gas set out a number of principles against which we would assess the governance framework proposed for this important new industry code. It is worth re-stating a number of these principles, as they provide the context for our answers to your recent consultation questions (provided in Appendix 1).
2. We are generally satisfied with the general progress that has been made in the SEC drafting and appreciate the clarity that the full legal drafting provides at this stage.
3. We are encouraged by the collaborative approach that DECC have taken in developing elements of the SEC, and by the convergence of some proposals towards the principles we have previously set out. But we also look forward to contributing to further refinements, in particular in the areas of efficient governance and charging mechanisms, where we believe additional and ongoing review is warranted as the SEC is established.

Principles of SEC governance

4. In May we stated that our guiding principle is that British Gas assets, operations, costs or customer service delivery cannot be unduly or unfairly influenced by other industry parties by means of SEC governance. This has not changed.
5. The SEC will govern smart metering services provided to British Gas which will allow us to serve all of our domestic and small business customers, and potentially many of our larger business customers. This could amount to as many as ten million premises.
6. The SEC will cover a broader set of industry arrangements than any other industry code and will be fundamental to the operation of our business. Therefore the SEC Panel, or the SEC governance

model as a whole, must not be able to deliver decisions and outcomes that are skewed in the favour of a collective, of competitors or any particular industry constituency.

Representation must reflect customer impact and investment

7. Our previous response was quite clear on this:

As the major financial contributor to the DCC, the largest user of DCC services, having over 16 million future smart meter installations, 10 million customers and having the largest investment programme dependant on the DCC's success, it is imperative that we play a leading role in the SEC governance arrangements. Any arrangements that do not provide this are unacceptable.

8. The current consultation proposes two models for Panel membership, neither of which in our view provides for adequate representation of the large suppliers. We are however mindful of the need for a balance between broad membership and cumbersome administration.
9. So, as a general principle we question whether smaller organisations have the ability, acting as a collective, to routinely exercise disproportionate control over the change process. Together, these Parties are likely to contribute relatively little financially towards the operation of the DCC, and represent small numbers of DCC-serviced customers, therefore we believe it would be wholly inappropriate and unacceptable for them to have a greater combined voice or power than a single larger entity.
10. Although difficult to deliver, we believe such an outcome is achievable, by considering the makeup of the Panel, and the role that panel is asked to perform in the wider governance framework. In the current drafting, these elements require some further consideration.

This is an opportunity to design efficient governance from day one

11. Previously we underlined the importance for Parties to be able to bring about change. The ability to stall or filibuster should be prevented. At the same time it should not be possible to railroad change through in a manner that damages not just day to day operations but confidence in the regime.
12. We called for standard minimum implementation time-frames. These may vary dependent on the impact of the change on affected Parties and could be tailored by change type given the broad scope of the SEC (industry processes, meter functionality, etc).
13. Detail on these aspects is currently limited. But these are important principles which have a bearing on our attitude towards appeals, Panel and Change Board constitution and remit, and overall 'value for money' of the SEC arrangements.

Cost allocation must be carefully considered and remain under review

14. We have always thought that it is essential that costs are allocated among Parties in proportion to the cost burden that they place upon the DCC. Suppliers should not effectively be penalised for proactive participation in Foundation and in the early years of the mass-rollout stage.

15. Whilst we remain encouraged that the Government recognises this in its current proposals, we believe there is still a potential for perverse incentives, during early rollout, and at the close of the mandate. Without further industry engagement it will not be obvious whether this is in fact the case. We explore this in our response to consultation question 2.

Transition arrangements are key

16. Last time we highlighted the importance of the transitional arrangements. We now have much more information about how these arrangements will work. There are two significant outcomes to ensure:
- i. That Foundation and adoption/enrolment are facilitated – designed into SEC operation as a matter of course to make the adoption process straightforward and commercially attractive. We understand that proposals here will be informed by the output from the Foundation consultation currently underway. The requirements and mechanisms for an efficient adoption process, and the expected timetable to go with it, are absolutely critical for suppliers to gain early sight of. Current drafting does not provide this detail.
 - ii. That the role and membership of the Panel is adequately defined at day one, with complete transparency of how early governance functions will migrate to enduring functions. Current SEC drafting does not distinguish sufficiently the role of transitional and enduring Panel; and prohibits a transitional Change Board, which we think could play a useful role given sufficient flexibility in remit.
17. If you require any further information or wish to discuss any element of this response then please do not hesitate to contact us.

Yours sincerely

Appendix 1 – Responses to consultation questions

Question 1: Do you agree that the Government conclusions are appropriately reflected in the SEC Stage 1 legal drafting? Please provide a rationale for your views, and any further comments on the draft legal text.

- 1.1 We have no further general comments on the draft legal text that have not already been addressed in discussion with DECC. We note that instances have been identified where the legal drafting seems to be at odds with the sentiment of the consultation document. In such cases we have interpreted the legal drafting as the master document.

Question 2: Do you have any comments on format of the DCC's Charging Statement for Service Charges?

- 2.1 We have no comments on the format of the charging statement. We would expect that the governance of the statement is sufficient to allow for changes to be made to its format and content, should we identify a requirement for increased transparency or clarity.

Go-early suppliers may be penalised during rollout, depending on allocation of DSP and CSP costs

- 2.2 The methodology for charging costs to DCC Users is clear and in our view sensible, however we are still left with continued uncertainty about the split of fixed and variable costs of the DCC's service providers. When will we get the visibility that we need to understand our potential exposure to such costs for DCC go-live and beyond?
- 2.3 A large number of British Gas customers will have a SMETSv1 meter (or meters) installed by the time the DCC service is available. Services to these meters will be provided in-house or third party SMSO. We have no objection in principle to sharing costs on the basis of mandated meter points for the Market Proving and Mass Rollout (MPMR) period, but we are concerned that the subsequent allocation of fixed and variable costs by the DCC service providers must be done appropriately. We expect a large proportion of DSP and CSP start-up costs to be recovered as soon as DCC goes live by means of a fixed charge (i.e. guaranteed recovery) element. This inevitable weighting - heavily towards DCC fixed cost recovery from Users - will act as a disincentive to install any meters before DCC is capable of providing a service.
- 2.4 If, as in the example above, CSP and DSP start-up and development costs are recovered by means of fixed charges in the early years of DCC, suppliers who use DCC as their only SMSO will pay once. BG will be paying twice to service its existing smart meters - through its own SMSO and through DCC - until such a point as DCC is ready to adopt those meters. We are not yet clear about how fast this may happen.
- 2.5 The allocation of cost to fixed and variable charges by the DCC service providers must be keenly considered so as to encourage take-up of DCC services at a manageable rate, but not penalise suppliers who have supported the government's strategy for early rollout. As a guiding principle it should be the DCC implementation timetable, rather than cost of use implications that should

influence suppliers' plans for rollout. To help realise this, we would expect that the large setup costs of the DSP and CSP will be recovered well beyond the MPMR period.

The switch from MPMR to enduring charging model may have a perverse impact on the distribution of charges

- 2.6 One further point that needs consideration clarification is the impact of mandated supply points from 2020 onwards that have not yet had a smart meter installed. We anticipate large numbers of mandated premises where suppliers have, for whatever reason, been unable to install a smart meter before the deadline set by licence. It would be very undesirable for non-compliance to the rollout mandate to result in the benefit of a 'windfall' gain in reduced DCC fixed charges to any supplier that has failed to meet targets. An overnight switch on 1 Jan 2020 to charging in accordance with enrolled supply points means this could happen.
- 2.7 We expect that certain common services will be required and procured by DCC for residual non-smart mandated supply points, and we believe that these supply points must remain visible and part of a mandated set indefinitely, with periodic repeat attempts to install a smart meter. There should be an incentive for all suppliers to do this, and treatment by DCC of this population of meters will incur some level of fixed cost, to be shared by the supplier community. So we can't exclude them from the pricing model, unless these services are dealt with by a separate and appropriately shared charge.

Question 3: Do you agree with the thresholds applied to the 'first comer / second comer' principle (Five Year Rule for costs over £20,000)? If you disagree please set out the reasons for your preferred approach.

Investment decisions will be made on the basis of no second-comer

- 3.1 British Gas agrees that there should be a facility for the redistribution of investment cost where subsequent parties benefit from the development of an elective service. But we are clear that any investment we make will be appraised on the assumption that no subsequent users will take up the service; or alternatively the development will be undertaken in collaboration with other DCC Users from the outset.

Flexibility in exclusivity period may be appropriate

- 3.2 We are concerned at the difficulty in specifying a 'one size fits all' solution, in particular for certain elective developments of high financial value. Here we believe there is merit in considering some flexibility in the exclusivity period, where it is anticipated that services may take some time to develop or bed in. We think that the incentive to develop an elective service comes entirely from the ability to gain competitive advantage following delivery of that service, and that the provision to claw back development costs is no more than peripheral to the investment decision.
- 3.3 So we are far more interested the ability to secure a longer exclusivity period, particularly for complex developments where DCC and supplier intellectual capital is as great an input as initial development costs. To be able to distinguish such elective services is likely to require some kind of

measure of complexity. We note that DCC costs may well be the best proxy here, whereby discussions to extend exclusivity beyond the currently proposed six months would be triggered at a certain threshold.

The administration of the process must not be a burden

- 3.4 We would be concerned if the Code Admin and Secretariat services become over-burdened by payment arrangements to redistribute small sums of money. It is likely that certain elective services will be taken up by numerous other users after the initial exclusivity period, possibly all at once. Costs for the redistribution of monies to the original investor will be borne by all code parties, not just those taking the elective services. For this reason, we think that a sum of £50,000 may be a more appropriate trigger for the application of the second-comer principle.

Question 4: Do you think the members of the Panel nominated by industry should be drawn from and elected in equal numbers by Party category OR be elected by all Parties (as set out in the legal drafting). Please give reasons for your answer.

Option A is the only viable option presented

- 4.1 The consultation presents two options. Of these options, only Option A is acceptable to British Gas. Option B allows for the potential for a Panel with no large supplier representation and as such must be dismissed outright. We do not believe that there is a material difference between options A and B in terms of whether sufficient experience and expertise is delivered to each post. But we do think that Panel members drawn from DCC parties will be far more effective than independent experts, which option B permits.
- 4.2 In our experience, whilst a panel of independent experts may offer expert guidance and a 'purist's' approach, they may not have sufficient insight into the practical and operational considerations of delivering smart metering. Members drawn from SEC Parties, by contrast, will tend to practise a level of pragmatism that is necessary to minimise frustration in change governance.

All Party categories must be guaranteed a voice...

- 4.3 We believe it makes for good governance to bring all Party categories to the table. Option A should guarantee this in the enduring regime, whereas Option B will not.

... but it should be proportionate to financial commitment and customer numbers

- 4.4 The large energy suppliers ('Big Six') have a critical and absolute interest in ensuring the success in operation of the DCC. They will pay the vast majority of its costs and will be heavily impacted by almost all changes that are proposed to SEC. Most importantly, they represent the overwhelming majority of energy consumers impacted by smart metering, and they do this forcefully, considerably and in support of the consumer's best interests.
- 4.5 British Gas absolutely believes in its right to a proportionate voice, and is fully committed to supporting the establishment of a successful transitional and enduring governance regime for smart metering. It would be unacceptable to design a governance regime for DCC users which allowed

minority voices representing a fraction of the overall marketplace to frustrate progress for the overwhelming majority. We will strongly resist any regime that is unable to appropriately recognise the validity of our views.

- 4.6 Whilst neither option for Panel constitution goes far enough to recognise adequately the role that the large suppliers have accepted in the success of the smart metering in the UK, we believe there is scope to increase representation for the benefit of the panel as a whole. We consider this further below.

Initial Panel membership should make the most of industry resource

- 4.7 During the initial months, in the absence of a universal requirement to accede to SEC, Panel representation in some Party categories may be limited. It is feasible that only suppliers and network operators are involved in the Panel's early activities. (Although DECC will appoint initial Panel members, they can only do so among Parties guaranteed to accede to SEC in BG's preferred model.)
- 4.8 There is an opportunity to consider whether for this initial period, it would be sensible to assign more than one Panel seat to large suppliers, and perhaps network operators, to reflect the difficult task they have in bringing stability to a new regime still in a period of significant ongoing development. Such a task will be made more difficult if the burden of DCC User representation falls to only two or three individuals.
- 4.9 We suggest that it would be appropriate to appoint two or three large supplier representatives for the initial DCC set-up stage. It is crucial that the Panel provides solid support and leadership, since even in the run up to DCC go-live there will be varying attitudes to the practicalities of bringing the full DCC service on-line.
- 4.10 Furthermore, BG strongly advocates initial Panel membership not just from SEC Parties, but from Parties who are also using (or intending to use) DCC services from day one. The most effective Panel will be made up of SEC Parties that are visibly committed to working with DCC from the very start.

An initial Change Board could be useful

- 4.11 It may also be helpful to review the current position that the establishment of a Change Board is not permitted in the initial phase of SEC. The Panel should have this option available, as there are a number of useful functions that a Change Board as a broad discussion forum could perform on the Panel's behalf. Furthermore, DECC should be confident of a general willingness to provide resource to such a forum, as is already evident at existing programme meetings.

Panel member is not an easy job – at any time

- 4.12 We have suggested that room should be made for additional large supplier (and possibly network operator) Panel membership in the initial period up to and beyond DCC go-live. However, may we also make it clear that even on an enduring basis, our preferred option (A) does not give sufficient large supplier representation, since it practically limits large supplier Panel membership to one.

- 4.13 We have always supported the transfer of duties from Panel to a more representative Change Board, in order to limit the requirement for Panel members to balance conflicting constituency requirements.
- 4.14 As drafted, the Panel remit is still very broad, and we anticipate an intense interest in Panel business. So we expect that any Panel representative will have a lot work to do. This will be an incredibly difficult job, in particular for a single large supplier representative, since they will be expected to voice the concerns of those DCC users on whom the impact of any changes is massive, both in terms of financial impacts and number of customers affected.
- 4.15 We fully expect that much of the development of DCC services will be driven by large suppliers, and acknowledge that large supplier parties are best placed to provide ongoing resource to support this. It would therefore be appropriate to broaden the enduring Panel membership to at least two members for the large supplier category. An alternative to this would be to allow the Chair to nominate a further large supplier to the Panel for the overall benefit of sharing the workload and providing further support and expertise where required.

Question 5: Do you support the proposed composition of the Change Board and its decision making arrangements?

The remit of the Change Board should be broader

- 5.1 British Gas has always supported the need for a separate Change Board. This will relieve pressure from the more resource-limited Panel, and provides an appropriate forum for wide and inclusive DCC User representation. We are heartened by its inclusion in the Stage 1 legal drafting.
- 5.2 Nevertheless, we still believe that there is scope to give further duties to the Change Board as a matter of course. We agree that a where an industry recommendation is required (the need for which we remain unconvinced of), it should be the Change Board that provides this. But as currently proposed this seems to be its sole function.
- 5.3 British Gas is convinced that far better use can and should be made of the industry resource that the Change Board will provide. Rather than acting only at the very end of the change process, the Panel should hand all change management activity over to the Change Board. It is here that the operational expertise to consider code (and system) changes will sit. The Panel will retain the responsibility for ensuring due process, but can remain somewhat distanced from the detailed discussion and development. This will reinforce the split between the Panel's 'executive' function, and the Change Board's delivery of industry developments.

Recommendation determined by affected Parties is right ...

- 5.4 We are pleased to see an improvement in the proposed voting arrangements, whereby a majority view is required in affected Party categories.

... but the right to vote should be self-determined

- 5.5 But we do not support the power of the Panel to determine which parties are affected. We fully understand why this has been proposed, but in practice we feel that it is unnecessary. Self-declaration of interest in any matter should be sufficient, otherwise time is wasted in debate at Panel and Change Board level, with viewpoints likely to be just as polarised once any such debate is over.
- 5.6 We do not support any provision which does little but increase the likelihood of appeals; and any feeling of exclusion will always be unhelpful to the governance model as a whole.

Quoracy arrangements for the Change Board need further consideration

- 5.7 We believe that quoracy arrangements for small suppliers and other DCC users need further consideration. Under the current drafting, we anticipate that even travel disruption may render the Change Board unable to conduct its business. We would suggest that only one member needs to be present in each of the Party categories of Small Supplier and Other DCC User. Or a minimum number of attendees across all Party categories could be set – six, for example. This would cater for those instances where the Board's agenda has nothing of interest on it other than to one Party category.

Question 6: Do you think that the SEC should provide for Parties and the consumer representative to appeal Change Board recommendations before they are submitted to Ofgem? If so, what is the appropriate mechanism for determining such appeals?

An appeals process is essential

- 6.1 We agreed that the ability to appeal Change Board recommendations is an essential provision of the SEC drafting. In our view it would be appropriate for the Panel to delegate appeal decisions to an independent sub-committee. The initial appeal route must not limit the ability of a Party to subsequently bring an appeal to the Authority.

Appeals must be tightly time-constrained

- 6.2 It is vital that the within-code appeals mechanism cannot be employed to frustrate the change process. For this reason, a clear set of rules with specified timescales is necessary. We consider it appropriate that an appeal cannot delay the progression of a change by more than a month.

Question 7: Do you have any further comments, or views on the cost implications to SEC Parties, regarding the proposals for governance, the modification process and the approach to appeal rights set out here and reflected in the legal drafting of Stage 1 of the SEC?

- 7.1 We have no comments other than those made in response to question 6.

Question 8: Do you agree that liability provisions for intellectual property rights and confidentiality should be included in the SEC. If so, do you agree that they should be unlimited?

- 8.1 We agree that liability provisions for intellectual property rights and confidentiality should be included in the SEC, and that they should be unlimited.

Question 9: Do you agree with the Government's proposal that in instances where the DCC is exposed to liabilities that exceed what it can claim from the person causing the original breach, the net liabilities for the DCC will be recoverable from SEC Parties by way of an increase in the DCC's fixed charges?

- 9.1 It should be an absolute priority of the Government to design the contractual regime in such a way as to incentivise DCC behaviour to minimise exposure to misaligned liabilities. In such circumstances, additional charges to suppliers may ultimately be passed to consumers.
- 9.2 We do have some reservations about the general narrowness of the liabilities provisions as currently drafted. One area of commercial risk with a huge impact for suppliers is where a loss of WAN, caused by the CSP, results in periods of downtime for large numbers of installers. Whilst there is a need to balance protection for suppliers with the cost implications of over-insurance by the DCC, we think this matter requires further consideration alongside other provisions, guarantees and service standards which are yet to be drafted.

Question 10: Do you agree that the Government's proposal to allow DCC to link service provider and SEC disputes in the arbitration process?

- 10.1 We agree that this is a sensible approach to dispute management.

Question 11: Do you agree that the proposed legal drafting covering change co-ordination with other codes meets the requirements as set out in chapter 5?

- 11.1 Yes, this is a key requirement and it is sensible to have this obligation reflected in code drafting for the purposes of efficient industry governance. Equivalent drafting could be introduced to other relevant industry codes.

Question 12: Do you agree that the proposed legal drafting for the SEC covering obligations on SEC Parties to pass registration information to the DCC is appropriate? Please provide a rationale for your views.

- 12.1 The legal drafting to support obligations for the provision of registration information is appropriate and we are supporting all development work currently underway to achieve this necessary outcome.
- 12.2 We do not see an alternative at this time to allow the DCC to perform the core function of access control during rollout, and so it is vital that this work is completed on time.

Question 13: Do you agree with the proposed variation to the SEC modification regime in the transitional period, including a right of veto for the Secretary of State?

- 13.1 There are good reasons why the ability to raise standard modifications should be limited during the transitional period, not least to limit the potential to create uncertainty for Parties operating under a new governance regime for new services.
- 13.2 The Panel and Code Administrator will perform a vital role in giving guidance to any Party wishing to raise modifications during the transition stage, and should be used by all Parties for this purpose.

- 13.3 The Secretary of State should be uniquely positioned to understand the wider impacts of any proposed change on the SMIP, and for this reason we have no objection to its proposed right of veto (although we believe it is unlikely that it will be used).

Question 14: Comments are invited on the approach to transition as set out in this chapter and section L of the SEC. Please provide rationale to support your views.

- 14.1 We welcome the visibility of enrolment procedures provided in Section H and agree that this section, along with those others proposed in the consultation, should be brought into force at some time following the designation of the SEC, rather than at day one.
- 14.2 We also note the significant dependencies on discussions elsewhere in the programme around enrolment and adoption, and would like to emphasise the critical importance of the work in market proving, and agreeing on products approved for adoption, as referenced in section H.
- 14.3 As we noted in our previous response, the diverse views amongst Suppliers about the governance arrangements during early rollout period mean that this phase in the life of the SEC is as important, if not more important, than the enduring model. It is now vital that the programme (and industry) commits sufficient resource to allow all interested stakeholders to understand as soon as possible exactly how and when they can expect to interact with a part- or fully-functioning DCC, as well as what restrictions may exist.

Question 15: It is the Government's intention to introduce a regulatory obligation on suppliers to enrol SMETS-compliant domestic meters with the DCC and that this obligation would apply in relation to smart meters installed (from a specified point in the future). Do you agree with this intention? Please provide a rationale for your views.

- 15.1 British Gas fully supports the DCC as the entity that operates smart meters. For SMETSv2 equipment, coupled with a comms hub provided by the CSP, this is also the most practical solution.
- 15.2 For SMETSv1 meters, we would expect DCC to take on these meters in due course, and furthermore that this becomes the most attractive option to suppliers with such meters. In other words, the commercial arrangements for adoption and enrolment should dictate that SMETS-compliant meters are managed by DCC, without the need for an obligation.
- 15.3 In our view, reliance on a regulatory obligation alone will not secure the most commercially appropriate approach for suppliers and their customers. For this reason we are very keen to fully understand how adoption and enrolment provisions for all SMETS-compliant meters will be reflected in the SEC drafting and welcome further opportunity to shape these requirements.

Question 16: Do you agree in principle with the placing of a licence condition on gas and electricity suppliers to accede to and comply with the SEC?

- 16.1 We agree with the placing of a licence condition on gas and electricity suppliers to accede to and comply with the SEC. In our response to the government's last consultation on SEC, we made clear our support for the non-distinction between so-called 'domestic' and 'non-domestic' suppliers, on

the basis that large domestic suppliers also tend to have large non-domestic portfolios. We continue to support the differentiation of supplier category by number of customers only (although we have continued concerns that customers of small suppliers deserve identical protections to those of the large suppliers).

Question 17: Do you agree that the licence conditions as drafted meet the policy requirements as set out in the chapter? Please provide a rationale for your views.

17.1 We agree that the licence conditions as drafted meet the set policy requirements.

Question 18: Do you agree in principle with the placing of a licence condition on gas and electricity network operators to accede to and comply with the SEC?

18.1 We agree with the placing of a licence condition on gas and electricity network operators to accede to and comply with the SEC. The potential of the SEC to become the unifying governance structure across the energy industry is significant, and the inclusion of network operators is central to this development.

Question 19: Do you agree that the licence conditions as drafted meet the policy requirements as set out in the chapter? Please provide a rationale for your views.

19.1 We agree that the licence conditions as drafted meet the set policy requirements.

END