Consumer Focus
Campaigning for a fair deal

Consumer Focus response to DECC consultation on smart metering implementation programme Stage 1 of the Smart Energy Code – on draft legal text

January 2013

About Consumer Focus

Consumer Focus is the statutory consumer champion for England, Wales, Scotland and (for postal consumers) Northern Ireland.

We operate across the whole of the economy, persuading businesses, public services and policy-makers to put consumers at the heart of what they do. We tackle the issues that matter to consumers, and give people a stronger voice. We don't just draw attention to problems – we work with consumers and with a range of organisations to champion creative solutions that make a difference to consumers' lives.

Following the recent consumer and competition reforms, the Government has asked Consumer Focus to establish a new Regulated Industries Unit by April 2013 to represent consumers' interests in complex, regulated markets sectors. The Citizens Advice service will take on our role in other markets from April 2013.

Our response

We are grateful for the opportunity to respond to this consultation. Our response is non-confidential and may be displayed on your website. We are more comfortable with many of the proposed arrangements than we were when they were developed initially following the consultation in April, but there are still some areas of concern.

Areas not covered by the consultation questions

We continue to be concerned that there are no plans to require parties to the Smart Energy Code (SEC) which wish to receive Data Communications Company (DCC) services to prove that they are 'fit and proper' to handle consumers' data. We fully accept DECC's opinion that the SEC accession process may not be the appropriate place to deal with this issue, particularly since SEC parties will not have access to consumer data simply by acceding to the SEC. We also understand, as made clear in the consultation document, that all parties will be subject to the Data Protection Act (DPA). However (as discussed below) we do not believe that this is a sufficient deterrent in itself, or that it will necessarily prevent careless mistakes. We would suggest therefore, as a minimum, that there be an element in the DCC user entry process which requires parties to prove that they have robust and DPA-compliant policies and processes regarding the handling of consumer data, and that any relevant employees within the organisation are fully trained in compliance with the Act. We would also suggest, as we have before, that parties be required to prove that they have not been found in breach of the DPA in the UK, or similar legislation abroad, for a certain number of years. This may not pick up potential risks for new companies or those which are entering into new types of operations but it would still provide greater protection than the current arrangement.

In addition, we are not satisfied that the current arrangements in the SEC provide sufficient deterrent to parties, once they have become users, from committing breaches of the DPA, particularly since these are rarely prosecuted. We note that a party will be considered to be in default of the SEC, and in danger of expulsion, only if it fails to comply with an enforcement notice issued by the Information Commissioner, and not simply if it is served with an enforcement notice as a result of being in breach of the Act. This could mean that parties could breach the DPA multiple times and still remain parties to the SEC and users of the DCC's services, as long as they then comply with any enforcement notices that are issued. It is not clear that enforcement notices will necessarily undo any damage which has already been done by a breach – in some cases this may be impossible – so with the currently proposed arrangement there is potential for considerable and ongoing consumer detriment. We would suggest that as a minimum SEC parties should be considered to be in default of the SEC if they are issued with an enforcement notice. We would also propose that there should be some sort of 'x strikes and you are out' process whereby a party which is found by the Information Commissioner to be in breach of the Act more than a certain number of times is in fact expelled from the SEC, unless there is the potential for serious consumer detriment arising from this expulsion, in which case another type of sufficiently serious sanction should be applied.

Responses to specific questions

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.

We have not been able to review all 277 pages of the draft legal text due to resourcing constraints. Our review has principally concentrated on the governance framework and how the modification and Panel/Change Board processes would impact on consumer well-being and good governance. In those sections it appears that the text delivers the Government's conclusions although in areas there is an absence of detail that makes it hard to tell how provisions would be applied in practice. For more detail on these issues please see our answers to later questions.

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

We would like to see the DCC's Charging Statement provide a stable, predictable, charging regime. This should reduce the risks of participation, which ultimately are priced through to consumers. We therefore welcome the conclusion in paragraph 83 that, following go-live, DCC set-up costs will be smeared equally across the duration of the contract. This should reduce year-on-year volatility.

In areas the timing of the calculation of charges carried out under Section K is unclear. For example, K6.1 sets out a requirement after each charging year for the DCC to estimate user charges for subsequent charging years, but it is not clear to what timescale that estimate would be made. Some flexibility in timings may be a good thing as it could enable the DCC to prioritise its work efficiently. However, it is also important that users know, or can reasonably forecast, their charges sufficiently early that they can manage the risk associated with those charges (for example, so they can know how to price them through to end consumer tariffs). Late notification of, and volatility in, existing network charges such as Balancing Services use of System (BSuoS) are often cited by suppliers as causing pricing risk that they end up passing on to consumers. It may therefore be useful to provide clearer deadlines for the advance notification of estimated charges in the SEC in order to avoid last minute notification of charging changes.

We agree that it makes sense to allow the fixed costs of providing elective services to be recouped from all those parties who come to use those services, and not simply the first to do so. However, we think there may be some grey areas where the provision of one elective service facilitates the development of others. For example, investments in software, hardware or human resources to deliver one elected service may defray the costs of future separate elective services that require similar technology platforms or skills. It is not clear to us where the limits on the 'second comer' principle lie where the second comer's demands overlap – but do not entirely coincide with – an existing elective service.

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.

We agree that it is sensible to have a threshold for the reason you give – because it may be unnecessarily bureaucratic to reapportion fixed costs where these are trivial. We have no strong views on whether £20,000 is an appropriate threshold. In practice, if the threshold proves to be too high or low it could be subject to modification through the usual code process.

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

We think that the members of the Panel nominated by industry should be elected by all Parties, however, there should be some safeguard to ensure that the panel is not dominated by a particular type of party, or that an important party category (eg Supplier or Network) is not left out entirely. This could be in the form of a *de minimis* requirement for certain party categories to be represented, such that if the vote alone does not deliver this, the nominee(s) in the relevant category with the largest number of votes replaces the nominee(s) with the smallest number(s) of qualifying votes. It could also be achieved by leaving a small number of spaces on the panel available as 'top up' at the chair's discretion.

We would not be in favour of Option A because it is not necessarily logical for each party category to have the same number of representatives, since some party categories, for instance electricity suppliers, may be more heavily involved in more aspects of smart metering than others, such as gas transporters. In addition, for many categories it may be unreasonable to expect that one member would be able to represent the views of the whole category (for instance within the 'supplier' category there may be very different views between large and small suppliers) so it could be necessary to have multiple members for each category, which could make the panel large and unwieldy. Another option would be to split some of the categories where this is likely to be an issue (particularly, we would suggest, the 'supplier' category) but we understand from the consultation document that the Government is unwilling to do this.

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

On balance, no, although we recognise that it represents an improvement on the voting arrangements in the April consultation.

We are pleased to note that each Change Board member, including the consumer representative, will have a vote on the board, and that each of the five categories of voting Party will have equal weight in contributing to the overall Change Board recommendation. This appears to us to give a much more balanced representation of interests than the previous model for two reasons. Firstly, because it would mean that less well resourced stakeholders such as consumer groups, small suppliers and ESCos would have equal ability to influence the Change Board's recommendation (and whether or not a subsequent Ofgem decision is eligible for appeal to the Competition Commission) as the dominant suppliers.

Secondly, because the need to win over a majority of eligible Party category votes in order to get an overall approval recommendation should increase the chances of proposals being developed in a consensual and collaborative way. This could improve inclusivity in the process and reduce the risk of 'block voting'.

There are three areas where the new proposals cause us some concern however:

- Undue discrimination between Big 6 and non- Big 6 DCC users
- Risks of conflict and/or inefficiencies in how the Panel and the Change Board work with each other
- Processes for voluntary or 'forced' abstention

Undue discrimination between Big 6 and non-Big 6 DCC Users

The proposals guarantee the Big 6 suppliers a seat each at the Change Board – they will fill the six 'Large Supplier' seats. However, small suppliers, network and DCC users will have fewer seats than participants in their voting categories. It is likely this would mean that Large Supplier representatives would feel free to represent purely their own company's views while representatives in other categories had to try and present those of a range of participants in their category. In many cases – particularly in the case of small suppliers – commercial positions may vary greatly within a category depending on each company's business model, so this brings a risk that the Change Board will less adequately represent the views of smaller participants than of large participants.

While the Big 6 will point to the bulk of DCC funding coming from them as a justification for their having guaranteed seats it should be noted that small suppliers are no less dependent than big suppliers on the DCC and SEC arrangements working properly. Guaranteeing votes for big suppliers but not for small suppliers could, in our view, be reasonably argued to constitute undue discrimination in favour of the former.

If the Government wishes to base an approval or rejection recommendation on the majority vote within each category of participant then it may be fairer to dispense with the Change Board completely and simply allow each Party to vote during the industry consultation process. These votes would then be tallied by category to give an overall recommendation per category group.

We would prefer to see the recommendation on whether to approve or reject a proposal being made by the code Panel rather than a separate Change Board, in line with the majority of existing codes.

Risks of conflict and/or inefficiencies in how the Panel and the Change Board work with each other

On most existing codes quality assurance on how a modification is assessed ('the process') and the final recommendation on whether to make a change or not ('the policy') are made by the same Committee.

For the SEC it is envisaged that the process will be governed by an independent Panel while the policy is governed by a representative Change Board with quite a different membership. This creates a range of practical issues.

For those organisations with members on both committees it may double the number of meetings they need to attend. For smaller stakeholders this is likely to be a particularly unwelcome burden. If Government is determined to go down the bicameral route we suggest efforts are made to ensure that monthly meetings of the two committees are held on the same day, one after the other, in order to reduce this burden.

Splitting the consideration of modifications across two separate bodies also undermines the natural synergies gained by having one body considering both the process and the policy. This is because process and policy are fundamentally linked – the way an issue is investigated should be driven by the policy questions being asked. Splitting these roles across two bodies increases the chance that modifications will be 'sent back' into the process for further assessment, or that the final recommendation will appear to bear no relation to the evidence gathered, because the views of the Change Board and the SEC Panel on what information is needed to reach a recommendation are at variance.

We would encourage Government to reconsider whether a bicameral approach is the best solution. We are concerned that a major reason for its adoption is to try and keep the large suppliers happy by guaranteeing them a vote on the final decision on whether to approve or reject a modification. If that is the desire, then, as previously highlighted, we would suggest it could be achieved more simply by allowing Parties to vote in favour of approval/recommendation during the industry consultation process without the need for a separate Change Board to do this for them.

We would prefer to see the recommendation on whether to approve or reject a proposal being made by the code Panel rather than a separate Change Board, in line with the majority of existing codes.

Processes for voluntary or 'forced' abstention

Paragraph 145 of the consultation document sets out that 'During the Report Phase of the modification process the Panel may determine which Party categories are likely to be affected by a modification proposal. Change Board members representing Party categories who are not likely to be affected will abstain from voting unless they can make a strong case otherwise.'

We would welcome clarity on how this should be interpreted as it is not clear from it, or from the legal text, whether the Panel's view of who should or should not vote in relation to any given modification proposal would be binding on the Change Board. This matters to us greatly as consumer interests will always be heavily outnumbered on the SEC Panel with the constituencies currently envisaged. If the Panel is effectively able to pick and choose who can or cannot vote on the Change Board in relation to any given proposal this would leave us worried that consumer groups, or other smaller stakeholders, could be precluded from voting on a case by case basis where their views differed from those of suppliers.

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?

No, we cannot see value in a pre-Ofgem appeal, and it is not clear who could hear such an appeal. We do not think that the Change Board could act as the appellate body because it made the decision that is being disputed. While the SEC Panel could be used, this would call into question the point in having a separate Change Board in the first place – as it would appear to indicate that the SEC Panel is at least as capable as it is of making a recommendation on modification proposals.

All modifications following Path 1 or 2 will go to Ofgem for decision. All Ofgem's decisions on those proposals will be eligible for judicial review. Many will also be eligible for appeal to the Competition Commission, subject to whether Ofgem's decision aligns with the Change Board's recommendation.

Modifications following Path 3 should, by their nature, not be contentious – if they were high materiality they should not be following the self-governance path – but could be appealed ex post to Ofgem.

Given the existence of ex post appeal rights to dispute Ofgem Path 1 or 2 decisions via either judicial review or Competition Commission, and Change Board Path 3 decisions to Ofgem, we do not see value in also including a further set of appeals procedures.

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 Stage 1 of the SEC?

We are concerned that the number of consumer representatives on the panel has reduced from two, in the previous consultation, to one. We understand DECC's position that if there is only one representative from each industry party on the panel (for instance through Option A in the consultation document), then two consumer representative gives disproportionate weight. However, we would argue that although each other industry party alone has only one representative, industry as a whole will have a number of representatives, and in cases where a number of industry parties' interests align, it would not be disproportionate to have multiple consumer representatives. Perhaps more importantly, the election process in the current drafting, Option B, could lead to a panel in which there happens to be more than one representative from a particular industry category, in which case two consumer representatives would not be disproportionate even according to DECC's logic. Option B seems to be relatively similar to the composition of the Balancing and Settlement Code (BSC) Panel, on which there are two consumer representatives without problems of disproportional weight. Therefore it would seem reasonable to allow two consumer representatives onto the SEC Panel as well.

In addition, we think it would be useful to explore the reasons for which the SECCo board must have the same composition as the SEC panel, given that there are other panels where the 'CodeCo' bears no particular relation to the panel. Given the resource constraints of the consumer representative we would find it reassuring to have in writing the information which we received anecdotally from DECC that presence on the board would not entail a high level of engagement. We would also appreciate written confirmation that there will be indemnity provisions to ensure there is no risk of liabilities arising to board members; we have not been able to find any evidence of this in the legal drafting although we have had this explained verbally.

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?

Yes, we do agree that they should be included in the SEC. We have no view as to whether they should be unlimited.

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?

Yes. However we would argue that the increase for each party should be proportional to the share of the fixed charges already paid by that party, rather than distributed equally across all parties paying the fixed charges.

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

Yes.

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?

We have not had time to review these provisions so we have no comments.

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.

As above, we have no comments.

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?

Yes, this seems sensible.

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.

We have no particular comments on the approach to transition

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.

We do agree with the intention to introduce a regulatory obligation on suppliers to enrol SMETS-compliant domestic meters with the DCC, but we may or may not agree with the structure of the obligation, depending on the final decision regarding it. We are somewhat confused as to what the Government's 'minded-to' position is on this matter. The above question suggests that the government is not contemplating a mandate for full enrolment of all SMETS-compliant meters, but rather an obligation for full enrolment of all SMETS-compliant meters which are installed after a certain date in the future. However, the Foundation Smart Market consultation suggests that a number of options for enrolment of all SMETS-compliant meters, including full enrolment of all meters regardless of when they were installed, is being considered. If DECC believes that the DCC is in the best interests of consumers, we would argue that Government should mandate full enrolment, and as quickly as possible.

This is because, as we understand from DECC, enrolment in the DCC brings particular benefits to consumers, such as ease of switching and access to certain energy services. Without an obligation to enrol *all* SMETS-compliant meters, regardless of installation date, there is a serious danger that some consumers will miss out on these benefits, at least until their meter is replaced or they move to a home with an enrolled meter. This is particularly a problem because all consumers will be paying for the DCC, so it is unfair that some may not receive the benefits of its existence. We understand that suppliers currently profess the intention to enrol all of their SMETS-compliant meters with the DCC once it is operational.

However, given the obligation to roll-out meters across the country within relatively tight timescales, installation of new meters may well become the key focus, rather than the enrolment of old ones. In addition, there may be commercial benefits to an incumbent supplier of not enrolling some consumers' meters because of the disincentive to switching due to the potential for loss of meter functionality, and the reduced ease with which consumers may be able to access their usage data.

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?

Yes.

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.

Yes.

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?

Yes.

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.

Yes.

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