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### **Consultation on Stage 1 of the Smart Energy Code**

On behalf of Scotia Gas Networks (SGN) and SSE plc, we are pleased to provide comments on the above consultation. We welcome the ongoing engagement with the Smart Metering Implementation Team and have provided answers to the specific questions posed by DECC in the attached annex.

We are still concerned about the approach being taken on DCC charging. In particular, distribution network operators have no specific mechanism for funding DCC costs at this time. Even under RIIO-GD1, there is no automatic mechanism for recovering such costs. Due to the uncertain nature of future smart metering costs this has been left to be dealt with through the uncertainty mechanisms. It is critical that appropriate network funding arrangements exist before costs are allocated to ensure networks are not exposed to inappropriate risk as a result of DCC smart metering costs. We believe there are a number of possible approaches and would be happy to discuss them further with DECC and Ofgem.

We also strongly disagree with "Pay Now Dispute Later" for DCC invoices and the exclusion of DCC from sharing any part of the costs for bad debt. We feel the current approach in these areas does not sufficiently incentivise the DCC licensee to provide efficient and effective billing and credit management functions.

We broadly welcome the proposals for the Change Board but we would urge DECC to consider improvements to allow greater participation in the modifications process by materially affected parties. We believe the Change Board should, in the first instance, deal with all decisions relating to the progress of individual modifications with the independent Panel providing oversight of the process and dealing with appeals and disputes as suggested. During the transitional period, we believe the Panel membership should be expanded to take into account its additional powers in the modifications process.

We urge DECC to reconsider its proposals for Elective Services. In particular, we believe retaining the data details as part of a bilateral contract could impact the security and efficient delivery of the Core Services by restricting visibility of elective data items from the oversight of other SEC parties.

Finally, we note comments on page 15 of the consultation document which indicate the Government is not persuaded that the National Electricity Transmission System Operator should constitute a new Party category under the SEC. Instead, it is suggested aggregated consumption data could be more efficiently obtained through DNOs. We believe further



consideration should be given to how this would be achieved. We are concerned that the regulatory and commercial framework as currently drafted would not permit this. There are also important data protection issues to be considered. Furthermore, it is not clear how such data would be provided. It is likely to result in additional costs to distribution network operators. It is also important that all Parties contribute to cost to the extent they benefit from data and that should be appropriately incentivised to ensure only efficient costs are incurred.

We look forward to early visibility of the next stages of the Code and the planned timescales for review, consultation and implementation.

Please call me if you have any questions

Yours sincerely

## Annex – Consultation Questions

### General question on SEC legal drafting

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 agree that in the main, the Government conclusions have been reflected in the legal text. Instances where interpretation seemed to be varied were highlighted to DECC/Wragge and Co. at the recent SEC Stage 1 Draft legal review. We look forward to these amendments being passed to Parties in early January 2013, therefore our comments without this amended copy, are on the original draft.

In Section A, we are concerned with the drafting of a number of the defined terms. In particular:

- “Bank Guarantee” – we do not believe that acceptability to the DCC should form part of the definition. It is up to each SEC party to manage the acceptability of its own financial arrangements.
- “Cash Deposit” – we are concerned that the title to funds transfers to the DCC. Deposits should be held on trust until such time as there is breach.
- “Default Interest Rate” – we believe that a default rate of 8% above base is particularly high.

Also, of particular interest is a legal definition of “transition”, how long it will endure, which SEC stages it will span and when the baseline will be passed to formal Governance. Transition is referred in the legal drafting, but is missing from the legal definitions.

In Section C6, we question the need for the power to convene sub-committees at this stage, given the limited scope of the Stage 1 SEC Modification process. As the DECC Programme will still be running it will be the place for the content of the SEC to be discussed, shaped, determined and drafted. Also, we are keen to ensure that standing sub committees, set up under C6.2, do not continue indefinitely without periodic review by the Panel. We would ask DECC to consider including review dates for all sub-committees.

In Section C8, we question why all SEC Sub-Committee or Working Group members should have costs and expenses under £10,000 recovered without being part of the Approved budget. We can understand why the independent panel members may have reasonable costs reimbursed.

In Section D6.5, we do not believe it is necessary that the representatives from SEC Users at Working Groups should act independently. It is their expertise which is needed at this type of meeting, and there is an element of party role which will inform their experience in this area. As the Panel and the Authority will be acting independently, we believe they will provide the appropriate checks and balances throughout the process.

In Section E, we believe that stating specific data items to be provided by Network Operators to support access control in the main body of the Code is not the best approach. Experience from other codes shows that this can become problematic to manage. In Sections E2.1 and E2.2 the data items are very specific without acknowledging the life of that data. Some items may be optional or empty for valid reasons under specific reasons set out under the relevant Code. To avoid issues of non-compliance or in getting the list amended on change to the relevant Codes, it would seem more appropriate for data items to reside in a separate subsidiary document that could be more easily amended.

In Section E2.2, only the UNC is specifically mentioned. We would like to seek clarification that the omission of iGT UNC is an oversight and that the provision of access control data for iGT supply points will not be delayed.

In Section I1.5 sub-paragraphs (d) and (e), if a party is obligated to provide information legally, the DCC must be compelled to comply. Providing "reasonable assistance" is not sufficient to allow parties to discharge their obligations.

In Sections I1.7 to I1.14, the right of audit and investigations should be left to the ICO who are the experts in Data Protection. There is a double jeopardy issue allowing the DCC to audit/investigate parties and also being subject to the ICO's powers.

We believe care needs to be taken with the legal drafting of Section M8 and the consequential changes around the key exchange processes which are still being discussed. In particular, consideration should be given to ensuring that party default does not adversely impact critical process, such as key exchange, which is essential to the operation of Smart Meters.

## DCC Charges

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

We broadly agree with the format of draft Charging Statement set out in Annex D of the consultation. However, we continue to have a number of concerns about the approach to DCC charging more generally.

We welcome changes to DCC invoicing to deal with manifest errors but continue to disagree with the "Pay Now Dispute Later" approach. We urge DECC to consider the alternative of allowing Service Users to withhold amounts in relation to disputed items. We feel that this approach, alongside the expedited disputes process proposed, would still ensure DCC cashflow is protected. It would provide a more robust incentive for DCC to quickly resolve disputes and also offer equivalent protection to Service Users from disputed invoices.

We are concerned that arrangements to socialise the cost of bad debt with Service Users excludes the DCC licensee from these costs. We believe that due to the credit cover arrangements it will be unlikely that bad debt will occur. But where it does occur, DCC may have played a part in this situation by allowing debts to accrue beyond the credit cover. In such a scenario, DCC should incur a proportion of these costs otherwise we are concerned there will not be sufficient incentive for the DCC to effectively manage debt. We note that incentives for robust credit management will form part of the licensee's price control but we believe an explicit incentive should also exist in the SEC, as it will for other licensed entities.

Finally, further consideration should be given to the timing of publication of indicative and final DCC charging statements and commencement of charging periods to tie in with gas and electricity network operator charging obligations and Regulatory Years. Network Operator charges currently apply for the Regulatory Year commencing 1<sup>st</sup> April and have to be notified to the Authority and Suppliers / Shippers in advance. We are concerned that the timescales proposed for DCC charges do not tie in with network obligations. As networks are generally restricted to changing charges once per annum (except in exceptional circumstances) and have very strict provisions for dealing with under or over recovery of revenue we are concerned arrangements could leave networks exposed.

### 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.

Yes we agree that there should be the opportunity for users to share the costs of elective services, in the same way that the model already accounts for the core service costs across all users.

It seems appropriate, that a threshold should be applied to "first come, subsequent comer", once the period of exclusivity of elective services has been passed, it appears better to share the costs with all subsequent users of that service. However we question the threshold for the costs, believing it more appropriate to start around £100,000. The administrative burden of overseeing all elective services (of which there could end up being thousands, in individual bilateral contracts), which fall over the threshold during the full 5 years, would seem to outweigh the benefits of trying to apportion these costs. Bearing in mind the administrative burden would be time of Code Administrator, DCC, DCC Service Providers, Panel, Users of that particular elective Service. Knowing that the initial user requesting the elective service can determine whether to accept the development costs/terms/conditions set out in the quote. All initial users know that they may be the only user of this service and therefore will make the relevant business decisions at the time of accepting the elective service quotation.

#### SEC Panel

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 believe that Panel membership should be representative of the liabilities placed on parties to the Code. We prefer election by equal numbers from each Party category. However, we believe the current proposals are too restrictive on licensed parties (Suppliers and Network Operators) and influence should be increased particularly given the liabilities and funding obligations the Code will place on them.

We are concerned that the limited membership of the Panel is not appropriate during the transitional arrangements; particularly as it is proposed that the Panel will have the modification powers of the Change Board. We would urge DECC to consider extending the membership of the Panel in the transitional period.

#### Modifications

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

We are concerned that the proposed composition of the Change Board only allows 3 seats for all Network Operators, both Gas and Electricity; and large and small. We do not believe that the level of representation is sufficient given the differences between the different types of networks and the funding and liability obligations placed on these parties under the SEC.

We also believe greater flexibility should be provided to allow any party to attend the Change Board if they deem it necessary. With this approach there is a small risk that all parties will wish to attend. In the unlikely event that all parties wanted to attend, it is likely that the modification, under discussion is probably one which would benefit from a full discussion from varied SEC Parties. Generally attendance at meetings will self regulate to a group of core members, especially if participants attending are not reimbursed expenses/costs. We firmly believe in the principle that all SEC Parties should have a right to attend and to discuss changes rather than limiting attendance to the Change Board only.

We agree with the decision making arrangements for the Change Board, but we feel that asking the Panel to consider every self-governance and urgent change would place an excessive burden on Panel members. The assessment of self-governance, urgent and fast tracked changes should be considered by the Change Board in the first instance.

We would prefer a governance model where the Panel is responsible for independently overseeing and monitoring the modifications process and providing it is representative of all party categories, it may be appropriate to allow the Panel to deal with appeals against decisions of the Change Board. However if the Panel is actively involved in making decisions on how individual modifications are to be progressed e.g. whether they should be urgent or fast tracked, there is a risk of conflict of interest. We believe such decisions should be made by the more representative Change Board.

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?

Yes, we believe the Panel would be the appropriate body to consider appeals from the Change Board. However, as set out above, in order for the Panel to act independently, it is important that the Panel is not actively involved in the modification process. Decisions on the progress of individual modifications should be made by the Change Board in the first instance. Utilising the independent Panel should provide the industry with a more proportionately cost effective management of appeals and allow issues to be resolved before involving the Authority.

We would look for this process to be defined ready for, or during, SEC Stage 1, to clearly set out the steps and timescales.

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?

Licensed parties are faced with significant risks under the code, therefore, it is important that the modifications and appeals process is robust and reflects the ultimate liabilities of parties. A governance model which protects the interests of parties that has some additional costs is much preferable than a cheaper approach that does not protect parties' interests.

#### Liabilities

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.

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?

No, the proposal does not incentivise parties to follow best practice. Parties could breach the SEC, safe in the knowledge that others will pick up their liabilities. This does not follow general regulatory practice set out in other codes, which aim to place obligations or incentives on those best placed to manage them. Also, whilst the offending party would be excluded from the SEC and the DCC, we are concerned that such behaviour could go undetected for a long period of time, which will increase the liabilities of parties who conform. We are particularly concerned that large suppliers and networks will be called upon to cover the majority of the shortfall which will lead to greater costs for insurance and risk planning. Such costs are likely to ultimately be passed on to the consumer.

More suitable alternatives include:

- The DCC licensee should be obligated to obtain adequate indemnity insurance as part of the bid process. SEC Signatories could be obligated to pay a proportion of this cost.
- SEC Signatories could pay a bond to join the DCC that could be called upon by the DCC to cover shortfalls.
- SEC signatories could pay into a contingency fund.

Appropriate rules can be included within SEC to ensure that a mechanism is in place to govern the process to release funds from the bond/contingency fund.

#### Dispute resolution

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

Yes, it should promote efficiency and costs savings. We agree with the principles relating to whether the SEC Panel, Ofgem or an independent arbitrator is used.

Lengthy litigation could leave SEC parties in a hiatus and could have consequential affects on the administration of the SEC.

However difficulties may arise in respect of any IPR claims where the technical knowledge of the technology courts would be very useful. We urge DECC to give this issue more thought in relation to IPR.

#### Code co-ordination

**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 believe that the proposed drafting for change co-ordination with other codes is appropriate.

#### Passing registration information to the DCC

**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.**

Yes, we agree with the requirement to provide the identified data and the legal drafting of the obligations. We note that once the SEC is in force, the requirements in the Code will need to be reviewed against the requirements in other Industry Codes to provide data to the DCC. This is to ensure that the requirements are only stated in a single place and that the Codes do not introduce contradictory obligations. We also note that some of the specified data items are optional or may be blank for valid reasons under other Industry Codes.

We note that the UPRN field is currently optional under existing Industry Codes and that whilst there are benefits to Network Operators to confirm the extent of the roll out into a single view for use by suppliers and other stakeholders. There will be an additional resource requirement on Network Operators to match metering points to a UPRN and this should be recognised within the relevant price control settlement (RIIO-ED1).

#### Transitional arrangements

**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?**

We are concerned that the Secretary of State's right of veto are potentially an expansion of the powers granted under the Energy Act without the requirement to lay orders in Parliament.

As stated above in response to Question 4, we are concerned that the limited membership of the Panel is not appropriate during the transitional arrangements; particularly as the Panel will have the modification powers of the Change Board. We urge DECC to consider extending the membership of the Panel in the transitional period.

We believe it is important that as much clarity and certainty is provided in this critical transitional period as possible regarding governance arrangements and definition of transitional period.

**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.**

As stated above in response to Question 4, as paragraph L1.3 (d) gives the Panel the functions of the Change Board in respect of Urgent Proposals in the transitional period, we urge DECC to consider extending the membership of the Panel, during transition, using Section L2.

**Licence conditions**

**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 support the early migration of all compliant meters into the DCC to enable the delivery of IA benefits. However this must be subject to technical and commercial viability to ensure we deliver the most economic solution to our customers.

The Government has made it clear that pre-mandate deployment of smart meters would be at the installing supplier's commercial risk. We cannot accept any socialisation of costs that may arise through adoption. Given that pre-mandate smart meters would have been deployed for the commercial advantage of the installing supplier, it is wholly unreasonable for subsequent suppliers to underwrite another's commercial risk – this would seem to be entirely at odds with our competitive market model. We firmly believe that any such costs arising must be borne by the installing supplier as it is through their direct action that these costs have arisen.

We believe that the DCC services should be allowed to stabilise before any mandatory enrolment is permitted, thus enabling a sufficiently informed and reality based decision making process. The criteria for this stabilisation should be agreed with the SEC panel and signed-off when achieved. Following this sign off we would expect all meters, to which the mandate applies, to be adopted as soon as is reasonable practicable/within 6 to 9 months.

For Network Operators, the potential benefit of data from smart meters is reduced when "gaps" in the information available exist. We are concerned that if large numbers of pre-SMETS and SMETS1 meters are installed the information available to Network Operators to deliver wider network benefits will be greatly reduced and other solutions may be required to deliver smart network solutions.

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.

We agree that the licence conditions as draft generally meet the identified policy requirements, however we are concerned that the current drafting of condition GG.3 in the draft electricity licence condition (and equivalent drafting in subsequent licences). This would appear to provide licensees with the freedom to determine whether they are obliged to comply with certain areas of the SEC. We note that other industry codes, such as the Connection and Use of System Code (CUSC), clearly state which sections of the code apply to which licensees or users. This level of clarity is essential within the SEC; otherwise Suppliers and Network Operators may not be applying the SEC evenly and there would not be clarity regarding what is required to be compliance with licence obligations.

Secondly, we would welcome drafting within the licence condition that allows the Authority to provide guidance as to under what circumstance a SEC party may be able to apply for derogation. Under Supply Licence Condition 11 ('Compliance with Codes'), the Authority, after consulting with licensees and other relevant parties, may produce guidance in which it bases any decisions for derogation. We would welcome similar clarity for the SEC.

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?

Whilst we agree with the principle that Network Operators should accede to and comply with the SEC, we are concerned that the networks benefits of Smart Metering do not arise until a significant volume of meters are installed within each geographical area. Network Operators will be charged by the number of potential installations regardless of whether the necessary volumes of actual installs are achieved in the early years of roll-out. We believe an alternative charging approach based on the actual installations and level of penetration within a Network Operator's area would better align charging with benefits to Network Operators.

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.

As set out under question 17 above, we are concerned that as currently drafted there is insufficient clarity regarding which sections of the SEC a network operator is required to comply with in order to comply. As set out above, we believe the approach adopted in other codes such as the UNC should be adopted under the SEC, with each section clearly stating which users or parties are required to comply.