Consultation on DCC Price Control RY2021 / 2022

E.ON Response (December 2021)

General Comments

E.ON welcomes the opportunity to respond to Ofgem's consultation on the DCC Price Control for the Regulatory Year 2020-2021 (RY20/21). As with previous Regulatory Years, E.ON employees have continued to work collaboratively with the DCC on a range of topics and programmes, with this approach helping to resolve specific operational issues and challenges that have impacted installations or service delivery to energy consumers.

In addition to responding to the individual consultation questions, we thought it would be helpful to provide commentary on specific headline topic areas in this initial section of our response. Additionally, we would be happy to engage further and assist with any clarification points where required.

<u>Fundamental Service Provider Costs</u>

Reviewing the Ofgem consultation document, we are concerned by both the continued rise and the scale of the increase in costs associated with the DCC's Fundamental Service Providers. E.ON believes that the DCC and its Contract Management function in particular, has a critical role in ensuring that all reasonable steps are taken to keep cost increases to an absolute minimum. DCC Users should not be expected to fund the rectification of DCC compliance failures which could have been prevented with better forward planning and control. Where cost increases do materialise, it is reasonable to expect the DCC to justify and explain the rationale for these increases as a detailed input into Ofgem's annual DCC Price Control process. In the event that the DCC cannot, or fails to, provide suitably detailed justifications and supporting evidence, E.ON believes that the costs should be disallowed outright.

<u>Ex-Ante Versus Ex-Post</u>

It is our view that the complexity and effort associated with reviewing the DCC's costs could be alleviated through the introduction of a complementary ex-ante approach. Requiring the DCC to agree its programmes and their associated costs upfront and before they are incurred, would provide DCC Users with greater clarity. As an organisation that funds DCC activities, E.ON believes it is appropriate for DCC Users to be given the opportunity on an ex-ante basis to scrutinise the scale of the costs that the DCC is proposing to incur, alongside supporting justification and any associated benefits detail. Adopting such an ex-ante approach would, we believe, allow the ex-post stage to focus on the actual outcomes and results achieved by the DCC.

Although the DCC may propose that their Quarterly Finance Forum allows a level of ex-ante scrutiny, E.ON firmly believes that this activity should be undertaken independently. This could be delivered through the enduring SEC governance structure.

Factors Spanning Multiple Regulatory Years

Many of the DCC's programmes and initiatives are designed and implemented across multiple years, meaning that decisions the DCC takes in one Regulatory Year can materially impact DCC Users in subsequent years. Firstly, work to finalise the DCC's Next Generation Comms Hub strategy did not progress at the appropriate pace in RY20/21, which will directly result in DCC Users having to replace much larger volumes of 2G/3G Comms Hubs in the 2025-2030 window. Secondly, while the DCC concluded work on the DSP contract extension in RY20/21, subsequent activities associated with the resulting DSP Technology Refresh have been poorly managed and planned by the DCC in RY21/22. This, and the more general lack of proactive tracking of hardware and DCC solutions that are approaching an end-of-life status, means that DCC Users are facing a considerable number of DCC-imposed maintenance outages during RY21/22 and RY22/23. A number of these DCC-imposed maintenance outages will impact services to energy consumers and based on current information shared by the DCC, it appears very likely that the overall level of downtime will significantly exceed what is permitted in the Smart Energy Code. The associated impacts are due to factors solely in the control of the DCC, yet DCC Users are being required to accommodate the DSP Technology Refresh at short notice irrespective of the disruption the DCC's plans generate.

DCC Headcount Growth

Given the level of headcount growth year-on-year, we believe that the DCC should be required to provide additional explanation and full transparency on its headcount plans going forward. E.ON is concerned that the DCC could be undertaking recruitment activities that expand business partnering and industry stakeholder management functions which fundamentally protect the commercial interests of the DCC, rather than DCC Users. On this basis, we firmly believe that the DCC should be required to provide additional evidence on the responsibilities of newly recruited staff in each Regulatory Year, so that this evidence can be scrutinised by both Ofgem and DCC Users on the basis of value for money and tangible delivery benefits.

DCC User Portal Costs

We are concerned that the Ofgem consultation document makes no apparent reference to internal or external costs incurred by DCC in its delivery of the DCC User Portal solution. The DCC repeatedly claimed that the new Portal would provide DCC Users with easy access to services and information, but also replace aspects of the DCC's Sharepoint solution. Following its launch, it was apparent that the DCC User Portal did not meet the requirements raised repeatedly by DCC Users during industry forums and DCC-led workshops. In RY21/22, the DCC User Portal has been quietly and gradually side-lined by the DCC, with information continuing to be shared either via the Sharepoint solution or the DCC's corporate website over the year.

Based on a recent update, we understand that the DCC is looking at yet further work to either enhance or even replace the DCC User Portal. E.ON does not believe that DCC Users should be expected to fund any Portal-related costs incurred in RY20/21, or any additional costs associated with the redevelopment of the DCC User Portal in subsequent regulatory years. It is our opinion that work in this area should be specifically included within DCC's disallowed costs.

Q1. What are your views on our proposal to accept DCC's External Costs incurred in RY20/21 as economic and efficient?

We disagree with Ofgem's proposal to accept DCC's RY20/21 External Costs.

Fundamentally, we do not believe that DCC Users should fund cost overruns where these are incurred as a result of inefficiencies that are within DCC's control and remit. DCC Price Control consultations in previous regulatory years have highlighted cases where inefficiencies have occurred owing to DCC-managed programme overruns or contract management failures. Fundamentally, it is disappointing to see evidence of similar cases reoccurring in RY20/21 (and RY21/22). The current model whereby DCC's cost overruns are, in the main, passed through to DCC Users warrants further examination. We firmly believe that the DCC and its parent shareholder should be responsible for costs caused by DCC inefficiencies that repeatedly reoccur over multiple Regulatory Years, or those that could be reasonably avoided.

Service Quality – SMETS1

Reviewing the commentary in the Price Control consultation, we believe that the SMETS1 costs detailed in paragraph 2.13 should be reviewed and disallowed. The additional SMETS1 related costs were not incurred as a result of DCC User actions or decision-making, but instead were due to the DCC's lack of contingency planning, their poor contract management approach and potentially poor requirements specification. DCC's failure to manage these factors then led to Urgent Work Orders, unexpected change requests, additional support intervention and subsequent additional activities, with the result that additional costs were then incurred by the DCC.

In 2020, repeated incidents affecting the SMETS1 Dual Control Organisation (DCO) occurred, impacting both the enrolment of SMETS1 meters at pace and their in-life operation post enrolment. It is E.ON's belief that the DCO incidents most likely stemmed from a combination of poor requirements specification by the DCC, or issues in the design/build/test phases being missed by the DCC and its contracted service providers. Similar issues have blighted the SMETS1 FOC release, resulting in the go-live being delayed multiple times in RY20/21, with stability issues also emerging in RY21/22 which have affected the enrolment of FOC L+G meters at pace.

Given that these, and other SMETS1 related issues should have realistically been avoided or controlled by the DCC, we are very surprised that the associated SMETS1 cost increase of £4.26m is being considered for approval on the grounds it is "economic and efficient".

Service Quality - Performance and Reporting

As part of the RY20/21 DCC Price Control process, we believe that Ofgem should also consider the quality of services delivered by the DCC and its Service Providers. Based on the DCC's own reporting that it presented to various industry forums, such as the SEC Operations Group, there is evidence that the DCC has failed to meet specific SEC Service Level Agreements during RY20/21.

Reliability or performance failings affecting the DCC end-to-end service, such as the ongoing issues in CSP-N, typically also impose inefficiencies and costs onto DCC Users as a result of process workarounds, triage or retry activities. This means that DCC Users are incurring costs owing to DCC's non-compliance with relevant obligations.

In July 2020, DCC had to explain an issue that impacted its Code Performance Measure reporting over the 2019/2020 period for CSP-N. Once the underlying reporting issue had been worked through and resolved, the revised reports revealed an even lower level of performance than had previously been outlined. It is important to note that Code Performance Measure 1 was reported as being below the minimum requirement throughout the year, due in the main to ongoing issues with the deployment of firmware to meter assets installed in the CSP-N region. Over this time period, E.ON and other DCC Users will have experienced a degraded level of service, but also incurred associated overheads due to process inefficiencies, workarounds and collaboratively supporting DCC's investigations.

During RY20/21, the DCC reported the occurrence of fifty-one major incidents affecting its service. In total, these incidents resulted in circa 198 hours of lost service time, with the incidents operationally impacting DCC Users. Given this level of service downtime, we believe it is reasonable to question whether DCC's management of its Fundamental Service Providers was sufficiently effective and whether its costs were economic and efficient.

*Service Quality – DCC Change Management*

Over RY20/21, work to progress and deliver various Technology Refresh activities was undertaken by the DCC and its Service Providers. While the CSP-N Technology Refresh was delivered early in 2021, there was disruption to certain CSP-N services in the preceding weeks. DCC Users were specifically requested to halt certain activities, including firmware deployments to on-supply meters, for a number of weeks ahead of the refresh activity taking place. The impact was compounded by a requirement to reschedule the Technology Refresh to a contingency date owing to an unrelated high severity incident, meaning that the request to DCC Users to halt certain activities was extended.

Separately, the DCC also appeared to make progress in extending the contract for the current DSP services in the latter part of RY20/21. However, it is now apparent that planning for the resulting DSP Technology Refresh associated with this contract extension has not been undertaken in a structured way. Following updates to the SEC Operations Group in Q4 2021, it is apparent there will be significant disruption to operational services during RY21/22 and RY22/23 as this DSP Technology Refresh is delivered. Proactive negotiation of the DSP contract extension, coupled with better planning on the resulting DSP Technology Refresh, could have meant that the DCC avoided certain inefficiencies or minimised the likely disruption to DCC Users in RY21/22 and RY22/23.

*Service Quality – Communication Hub Defects*

DCC Users have faced a number of material defects or issues with DCC managed solutions or devices. Specific defects have blighted the Release 1 and Release 2 Comms Hubs procured and supplied by the DCC, with defect investigation and resolution often spanning multiple regulatory years. E.ON have been involved in protracted discussions with the DCC over SMETS2 Comms Hubs that we have deemed "not fit for purpose", owing to the defects that have been identified either during testing, at the point of installation or that have emerged during in-life operation. Where a DCC Comms Hub variant is identified as having material defects, E.ON does not believe that it is appropriate for the DCC to continue shipping defective devices, or to continue recovering rental charges from DCC Users who cannot install the devices without adopting workarounds or without experiencing significant operational issues. While E.ON and the DCC have debated these principles on various occasions, the DCC has not agreed to adopt a revised strategy to rental charge recovery.

Given our protracted discussions on certain faulty Comms Hub variants with the DCC, including during RY20/21, E.ON has significant concerns that the current CSP contracts do not appropriately protect DCC Users from costs associated with rectification and stock holding of non-compliant Comms Hubs. As the DCC is nearing the point of concluding contract negotiations on its Single Band Next Generation Comms Hub variant in Q4 2021, we would expect that the DCC's Contract Management team will have addressed this and other relevant topics during its discussions with prospective suppliers.

In conclusion, we believe that DCC's External Costs should be re-examined, and further costs disallowed by Ofgem.

Q2. What are your views on our proposal to disallow the variance in enduring forecast costs for S1SP_3b and a proportion of the UIT forecast costs for DSP?

We agree with Ofgem's proposal.

It is our opinion that various factors or activities that were within DCC's control, contributed to delays and defects which could have been reasonably avoided. On the basis that factors were within the DCC's control, the forecast costs should be disallowed in E.ON's opinion.

Q3. What are your views on our proposals on DCC's approach to benchmarking of staff remuneration for both contractor and permanent staff?

We agree with Ofgem's proposals on renumeration benchmarking, and we welcome the level of scrutiny being applied to the DCC's Internal Costs overall.

The gradual re-balancing of the permanent to contractor staffing ratio by the DCC is also welcome, but we are concerned at the apparent continued growth in DCC staffing numbers. It is reasonable for DCC Users to expect the DCC's headcount to plateau and decline as the large SMETS1 Enrolment and Adoption programme tails off, and the volume of SMETS2 related developments and changes reduce.

We are surprised that the DCC's headcount forecasts continue to be on a growth trajectory over subsequent Regulatory Years. The DCC Price Control consultation does not explain the driver for the very significant growth in permanent roles forecast for RY21/22, and this has not been explained to a sufficient level of detail in the DCC's Quarterly Finance Forum sessions. Given the level of growth in headcount year-on-year, we believe there should be additional transparency on the DCC's headcount growth.

Question 4: What are your views on our proposal to disallow the Shared Service Charge associated with external services procured for Additional Baseline activities such as NEP and ECOS?

We continue to believe that there should be very close scrutiny and considerable challenge of Shared Service Charges and fees paid to the DCC's parent company. On this basis, we agree with Ofgem's position in this area.

While we have limited insight and visibility on the Shared Service activities and their associated costs, we believe that the DCC should be required to robustly evidence that these Capita-provided services offer good value for money. On this basis, we believe that the DCC should be required to undertake independent benchmarking of the services delivered, but also the associated costs.

Question 5: What are your views on our proposal to disallow non-resource recruitment costs in the Commercial and Operations cost centres?

Based on the evidence presented, we agree with Ofgem's proposal to disallow non-resource recruitment costs in the Commercial and Operations cost centres.

We believe that the DCC should be required to provide additional detailed justification to support the recruitment costs being incurred. Given the continued annual growth in DCC headcount, including in RY21/22, it is impossible for DCC Users to determine what individual staff in the DCC are tangibly delivering on behalf of DCC Users and energy consumers. We are concerned that the DCC could be undertaking recruitment activities that expand business partnering and industry stakeholder management functions which fundamentally protect the interests of the DCC, rather than DCC Users. On this basis, we firmly believe that the DCC should be required to provide additional evidence on the responsibilities of newly recruited staff in each Regulatory Year, so that this can be scrutinised by both Ofgem and DCC Users from the perspectives of value for money and tangible delivery.

Question 6: Do you have any views on potential proxy measures to calculate cost disallowances in areas where DCC may not have acted economically and efficiently, but the dependencies and scale of the impact are not clear?

E.ON firmly believes that in cases where the DCC cannot provide suitable and sufficient evidence to justify their costs, then the costs under scrutiny should be disallowed outright. Reviewing the Ofgem consultation document, it is concerning to note that the DCC have had to receive multiple requests before additional evidence on certain cost elements is provided.

We are surprised at the level of costs apparently incurred by the DCC in support of the security aspects of SMETS1 device testing. Although commissioned following specific changes introduced into the Smart Energy Code by BEIS, the scope of testing undertaken, and its duration would typically result in costs far below the headline increase outlined in the consultation document. Given this, we recommend that the DCC is asked to present a detailed breakdown of its costs in this area so that these can be appropriately scrutinised by Ofgem, the SEC Panel and the SEC Security Committee.

Owing to commercial confidentiality, the DCC Price Control consultation provides DCC Users with limited information and evidence on the DCC's activities and performance. It is therefore very difficult for DCC Users to suggest additional ex-post proxy measures that would not inadvertently result in unintended consequences occurring. Additional ex-post proxy measures could well result in the DCC skewing its behaviour to maximise the costs that are permitted. In reality, we believe that there is a risk that the introduction of additional ex-post proxy measures could actually lead to a worse outcome, rather than an improvement.

The introduction of ex-ante reviews of DCC programmes and other costs could offer an alternative approach. Assuming such reviews were conducted according to a clearly defined set of principles and by a body with suitable DCC User representation (e.g. the SEC Panel), this approach would mean that the DCC would be required to explain and justify planned expenditure ahead of it being incurred. While the DCC may suggest that its Quarterly Finance Forum currently provides this level of scrutiny, E.ON would disagree with this position if it were presented.

In conclusion, E.ON continues to believe that the DCC should be measured on its ability to deliver core services and industry programmes according to time, cost and quality metrics. Where the DCC continues to over commit, under deliver and overspend, it is appropriate for DCC costs to be either disallowed through the annual Price Control process or rejected during an upfront ex-ante review.

Question 7: When it is determined that DCC may not have acted in an economic or efficient manner, but an appropriate methodology cannot be applied to calculate the proportion of costs impacted, we propose to take these instances into account when deciding DCC's score under the Contract Management and Customer Engagement aspects of the OPR. What are your views on this proposed approach to be adopted from RY2021/22 Price Control, if an alternative measure is not determined?

Currently, we would support Ofgem's proposed approach for the RY21/22 Price Control.

Question 8: What are your views on our proposal to disallow forecast variances in Network Evolution, SMETS1, and ECoS programmes?

We agree with Ofgem's proposal to disallow forecast variances on these DCC-led programmes, given that each of these major programmes has encountered delays and issues due to factors within the DCC's control.

While the DCC progressed work on its Network Evolution programme during RY20/21, this did not deliver results to the extent that could have reasonably been expected. Much of the DCC's focus in RY20/21 was on the definition of its strategy for the Next Generation Comms Hub (NGCH) solutions. While plenty of effort was expended in developing strategy options, the approach adopted by the DCC generally lacked focus and direction, with many of the strategy options subsequently being discounted months later. E.ON believes that the DCC could have concluded work on its NGCH strategy much quicker and more efficiently, allowing it to progress procurement activities earlier. Time wasted by the DCC in the early stages of the NGCH programme in RY20/21 cannot be recovered, with the result that deliveries of NGCH devices will be considerably later than could have realistically been achieved.

Delays to the delivery of NGCH devices will impact energy suppliers in subsequent regulatory years, given that we will be forced to continue fitting legacy 2G/3G Comms Hub devices into 2024. The recent announcement by the Department of Digital, Culture, Media and Sport on 2G/3G coverage sunsetting, means that SMETS2 installations completed before the end of 2023 and the arrival of 4G NGCH devices, will require a further site visit to physically replace the DCC-supplied legacy Comms Hub. Had the DCC accelerated tangible delivery in its NGCH programme during RY20/21, the first deliveries of 4G NGCH devices could have been achieved by late 2022 or early 2023 at the latest, reducing the volume of these repeat site visits that installing suppliers will now need to undertake.

Question 9: What are your views on our proposal to disallow the costs associated with DCC's activity relating to EVs? Please provide any evidence if you have engaged with DCC in this area.

We agree with Ofgem's proposal. E.ON believes that the DCC should remain focused on the delivery of its core services and programmes for DCC Users, until the point that the DCC has fully justified its Electric Vehicle activities and the associated costs to the relevant industry governance forums.

While the DCC's licence allows it to examine potential innovation opportunities, its work on innovation-related activities has generally appeared to lack structure and direction, with this continuing to be the case into the current RY21/22 window. In previous Regulatory Years, the DCC's Business Development plan has focussed on innovation activities that the DCC believed would "revolutionise healthcare" and "enable precision agriculture", rather than its mandatory activities that support DCC Users.

Innovation work associated with electric vehicles clearly has the potential to support Net Zero targets and ambitions, meaning that the DCC may well have a role to play in this area. However, the DCC must formally engage with DCC Users through the recognised independent industry governance forums to raise awareness, ensure alignment of scope, and that projected DCC costs are reasonable and proportionate. Formal review and sign-off is essential, especially where costs end up being funded by DCC Users. While the DCC may claim that its Quarterly Finance Forum offers the opportunity to scrutinise its innovation activities and their associated costs, E.ON remains to be convinced of its effectiveness in this area.

Additionally, we do not believe that the DCC fully engaged DCC Users during RY20/21 on its activities relating to the "Elective Communications Services Overhaul" or the "DCC Boxed". The DCC's business case for the DCC Boxed solution came under significant scrutiny in RY21/22, only after it was formally presented to specific SEC Sub-Committees. By this stage, we believe that the DCC had broadly determined the solution design and had potentially incurred costs, all without validating whether the product would be purchased in sufficient volume by DCC Users to cover its costs.

Overall, we believe it is reasonable to require the DCC to provide a detailed breakdown of the costs incurred by staff involved in innovation-related investigations or work. Rather than simply providing costs at a summary headcount level, we believe it should be possible for DCC to precisely detail the time spent on individual innovation topics by DCC staff, plus any associated costs. Doing so would allow the DCC to demonstrate the costs incurred during advisory/collaboration activities (e.g.

engaging industry workgroups), and those costs which have been incurred for DCC 'business development' activities.

Question 10: What are your views on our proposals to disallow forecast cost variances in the Corporate Management, Commercial, Finance, Operations, and Programme (Service Delivery) Cost Centres in RY21/22 and RY22/23, and all baseline forecast costs for RY23/24 onwards?

We fully agree with Ofgem's proposal to disallow the forecast cost variances specified.

While the DCC has stated a belief that its Service Disaggregation strategy will lead to procurement cost savings, it appears that this strategy could well introduce considerable inefficiencies elsewhere. We believe that the proposed increase in headcount and costs in the specified DCC Cost Centres is the first of the inefficiencies resulting from the DCC's Service Disaggregation strategy. We are concerned that DCC are trying to resolve the issues associated with managing a larger and complex range of service providers, by increasing the number of internal staff across DCC at a cost to DCC Users.

Going forward, we suspect that the DCC's plans for service disaggregation will also introduce additional complexity in completing service maintenance and testing activities in subsequent years. This complexity is likely to result in the DCC demanding an increased number of maintenance outage windows or extensions to the duration of individual outage windows. If our fears are realised, this will result in the DCC imposing additional costs and disruption onto DCC Users. Such outcomes would appear to conflict with the DCC's ambition to reduce costs through its disaggregation strategy.

We are also concerned that the DCC is recruiting additional staff into Corporate Management functions, primarily to facilitate business partnering and industry stakeholder management activities which fundamentally protect the interests of the DCC, rather than DCC Users. On this basis, we fully support Ofgem's proposal to disallow forecast cost variances in this area.

Question 11: What are your views on our proposed position on DCC's performance under OPR and trial run for customer engagement, and implementation of the contract management incentive?

Reviewing the various assessments on the Customer Engagement element, the divergence in scores is both significant and worrying. Having reviewed the assessment scores from E.ON's perspective, our position is more closely aligned to that of the SEC Panel. Comparing the assessments outlined in the consultation document, we are unclear whether the apparent divergence is due to a difference in understanding, alternative assessment approaches, or whether there is a fundamental disagreement in performance. Ultimately, we believe this element needs to be investigated, analysed and ultimately addressed.

Based on evidence presented to the SEC Operations Group by the DCC themselves, SEC Service Levels were not met at times during the RY20/21. On this basis, it is difficult for E.ON to reconcile the proposed outcome with the actual experience of service quality and performance at points during the regulatory year. We have outlined comments on service quality issues in our response to earlier questions.

Given the issues that E.ON have faced with various SMETS2 Comms Hub variants, and our experience of the DCC's SMETS1 E&A programme, we strongly suspect that a number of the service failures originate from the management of DCC's service providers. Where requirements are poorly defined, or DCC's service providers have scope to misinterpret requirements, this ultimately results in solutions that DCC Users deem as "not fit for purpose". Ultimately, DCC Users should not be expected to incur rental costs for DCC Comms Hubs they cannot install, or costs for repeat site visits to remediate installations where the WAN coverage does not meet the contracted level.

It is our opinion that service failures involving the DCC's service providers are due in part to shortfalls in the DCC's contract management approach. On this basis, we fully agree that an independent audit model in this area is required.

Question 12: What are your views on our assessment of DCC's application to adjust its Baseline Margin?

We broadly agree with the Ofgem assessment of DCC's application to adjust its Baseline Margin.

Question 13: What are your views on our assessment of DCC's application to adjust its ECGS?

We agree with Ofgem's assessment of DCC's application on adjustments to ECGS.

While cost savings from refinancing are clearly welcome, we believe that the DCC should now be in a position to actively explore and secure additional cost savings in other areas of its operations. As DCC contracts come up for review or renewal, we believe it is reasonable to expect DCC to proactively identify significant savings or efficiencies on behalf of DCC Users. We would hope to see the DCC being challenged to deliver savings in other areas through Ofgem's Price Control processes.

Question 14: What are your views on our proposed position on DCC's costs associated with the Switching Programme?

While we agree with Ofgem's position on the DCC's Switching Programme costs, we do note that the costs overall appear to be continuing to increase. A further review of the DCC's costs in this area is likely to be warranted in due course.

Question 15: What are your views on our assessment of Delivery Milestone 2 and Delivery Milestone 3 of the Switching Programme?

We have no significant comments on Ofgem's assessment.