

Rob Salter-Church  
Partner, Consumers and Competition  
Ofgem

[half-hourlysettlement@ofgem.gov.uk](mailto:half-hourlysettlement@ofgem.gov.uk)

Dear Rob,

Half-hourly settlement (HHS): the way forward

Pre-launch consultation on Significant Code Review in Draft Forward Work Programme

We welcome the opportunity to respond to both Ofgem's consultation on the way forward for half-hourly settlement and the proposal to open a Significant Code Review on mandatory HHS that is discussed in it and forms part of Ofgem's draft work programme, also currently out to consultation.

We strongly support Ofgem's initiative to drive forward the move towards HHS for domestic and smaller non-domestic customers. HHS is essential to enable the benefits of the smart meter roll-out to be realised for these customers and also to promote innovation and competition in the market, including enabling more demand side response and unlocking opportunities for local balancing.

We agree with the Competition and Markets Authority's provisional findings that, to date, the absence of a firm plan for moving to HHS for domestic and smaller non domestic customers and of a cost-effective option for elective HHS is giving rise to an Adverse Effect on Competition through the distortion of suppliers' incentives to encourage their customers to change their consumption profile which is reducing efficiency and competition in this market. DECC's latest figures show that by the end of September almost one million smart meters had been installed in domestic properties by larger suppliers. There is already great potential for the benefits of HHS to be realised.

We support the overall approach of enabling elective cost-effective HHS by early 2017 and then moving to mandatory HHS as the best means of realising these benefits. These benefits should be realised as soon as is practicably possible, taking account of the need for orderly change and of the other major industry change processes in place.

Below we explain our views on Ofgem's proposals for elective HHS, where you have asked in particular for views on the barriers to elective HHS, and the SCR process for mandatory HHS.

Elective HHS

We support Ofgem's intention to carry out work in this area in two stages, with the first batch developing changes based on the recommendations from the Settlement Reform Advisory Group (SRAG) Work Area 1 and the second looking to address other identified barriers to elective HHS. This seems a sensible and pragmatic approach at this juncture to expedite change; we do not consider that further special governance arrangements are required.

We have yet to see the report that is to be presented to the February BSC Panel meeting but understand that this is focusing on a simpler settlement process that could support elective HHS for Data and Communications Company enrolled meters. Although SRAG is carrying out valuable work there was in our view a missed opportunity we believe to give elective HHS more focus and to drive this work forward — the group's terms of reference were arguably too wide, its original time to report in June too long and the remit of being an advisory group not conducive to seeing rapid progress. Nevertheless determining settlement process changes to facilitate wider use of elective HHS is a necessary and important step.

In addition to the settlement process, a key issue that needs to be addressed as a matter of urgency is the differential costs of settling through elective HHS compared to profiles. Currently suppliers have a cost disincentive to move customers to HHS as the costs are higher. Supplier Volume Allocation (SVA) charges

should be reviewed, including the Specified Charges paid per half hourly metering system and how all the elements of SVA charges are allocated, for example, those in respect of the profile administrator. It will be futile to change the processes if the appropriate cost messages are not also in place for elective HHS.

One of the lessons learned from the implementation of P272 is the need to ensure that appropriate charging arrangements are in place across industry, particularly distribution and transmission use of system charges. As this was a major source of delay and additional complexity for P272 lessons need to be taken from this experience, particularly given the far greater numbers of meters. However, development for smaller customers has so far focused solely on the BSC, with no consideration given to the potential work that will be needed to align other codes, primarily the DCUSA and potentially CUSC.

The impact on distribution use of system (DUoS) charges of greater HHS for domestic and smaller non-domestic customers should be reviewed. We understand that DCPI79 has removed barriers for customers in Profile Classes 1-4 from moving to HHS. However, this is a critical area and we believe the DUoS arrangements should be thoroughly examined to identify any potential issues that could arise at the elective stage, particularly as they are also likely to be relevant when the move becomes mandatory.

One issue that needs to be considered is that although DUoS arrangements have been amended to ensure that for an *average* customer the price is the same for non-half hourly (NHH) and HHS, for individual customers there will be differences, meaning that some customers will have an incentive to move and others a disincentive. This is a potential barrier to switching for these customers. During the elective phase it may be appropriate to let the market dictate but at the mandatory stage the process needs careful consideration as to how and when customers are moved. The issue also has clear implications for distribution network operators' ability to recover their allowed revenues.

A further issue that should be considered in this respect is the potential problems caused by customers, having moved to HHS, subsequently moving back to NHH settlement in order to cherry pick the best prices. This has the potential to create significant industry disruption (and has, for example, been a particular problem in Scotland in respect of the tariffs for unmetered supplies) and would also run counter to the intended direction of travel to move all domestic and small non-domestic customers to HHS. We believe that any customers once moved to HHS should remain there.

The impact on NHH customers of possible changes to Grid Supply Point (GSP) group correction factors should also be considered. These currently apply to non half hourly consumption and losses and, as more customers become HHS, non-half hourly customers will pick up a greater proportion of all contributing factors that are not due to the difference between profiles and actual consumption. This may be less of an issue with elective HHS, as numbers will smaller, but should be examined, together with possible solutions, which may include ensuring that all FiT export is half hourly metered to eliminate one important contributing source.

Although not a direct barrier to elective settlement itself we believe there is one important barrier that exists to making effective use of HHS to develop innovative trading options and competition, also supporting the development of community energy and facilitate local supply. We believe that a current restriction on the use of Additional Balancing Mechanism Unit should be removed. Currently, if a supplier wants to establish a Balancing Mechanism Unit additional to the one it is allocated in every GSP Group, it must adhere to restrictions that mean it cannot consolidate different types of meters, for example half hourly and non-half hourly, import and export meters. This limits the flexibility to associate meters in the same geographic area and thereby the ability to develop innovative trading options, including local supply and community-led energy. Removing the restriction could be a straightforward way to facilitate this.

### Mandatory HHS

We support the use of a Significant Code Review (SCR) to progress the introduction of mandatory HHS for domestic and smaller non-domestic consumers as the best way to ensure overall coordination of the changes that are required over several industry codes and over licences. The lack of such coordination led to delay in the development of changes for the introduction of mandatory HHS for meters in profile classes 5-8 under P272, notably the development of suitable distribution use of system charging arrangements.

It is not wholly clear at this stage how the SCR will proceed: Ofgem has made initial proposals to change the SCR process though introducing additional Authority powers through the third phase of the code governance review, for which a decision and possibly licence drafting are due in the spring. We also note that the government has recently issued draft legislation that would give Ofgem temporary powers to direct industry code changes in respect of HHS and reduce the 56 day period between the notice of a licence modification being published and the licence modification coming into effect. It would also make Judicial Review the only route of appeal for an Authority decision which went against the recommendation of an industry code Panel, instead of the possibility to appeal to the CMA.

These proposals all seek to expedite the change process, and while this is welcome, it also puts more onus on the regulator to ensure that industry is fully engaged and that legitimate concerns are listened to while the rules, and the implementation timetable for them, are being developed. In this respect we welcome the comment in the recent letter to Elexon on its role in HHS that it is particularly important that Elexon makes every effort to consider the issues raised by small and entrant parties; this must apply to other aspects of the SCR.


We note the government's view that the CMA appeal route will not be needed in cases where Ofgem decides against code Panel recommendations because industry will be able to provide sufficient scrutiny of Ofgem's policy- and decision-making throughout the reform programme. The recent experience with the Electricity Balancing SCR suggests that, even where significant parts of industry is unhappy with aspects of the outcome, there is reluctance to use the CMA appeal route, partly because of the potentially large and uncertain costs that could be entailed. A change to use only of Judicial Review, which route would focus primarily on procedural issues, may not therefore have much practical effect but it again serves to stress the importance of full engagement.

Clearly strong programme management will be vital to ensuring successful and timely implementation. Lessons need to be learned from the whole P272 process, including understanding the pressures on industry to implement a series of major system changes. The switching SCR, smart meter roll-out and Project Nexus implementation will all absorb industry resources. All the potential implementation issues need to be flushed out at an early stage so that there is not a repeat of the successive delays with the implementation of mandatory HHS for Profile Classes 5-8.

Notwithstanding, we support Ofgem's ambition that by the first half of 2018 the central systems and industry rules will be in place to facilitate mandatory HHS and that it should then be in a position to make a decision on timescales.

It is taking fully six years from the initial BSC proposal to introduce HHS for Profile Classes 5-8 in May 2011 to implementation in April 2017; clearly this has been much too long. We share Ofgem's and the government's view of the importance of extending HHS to the domestic and smaller non-domestic market and we strongly support the need to progress and realise this through a structured and coordinated programme.

Yours sincerely

A handwritten signature in blue ink that reads "Nigel Cornwell". Below the signature is a long, horizontal arrow pointing to the right.