Rachel Clark
Switching Programme
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23 December 2016

Dear Rachel

Draft DCC Business Case for DCC activities during the Transitional Phase of the Switching Programme

SSE welcomes Ofgem's consultation on the Draft DCC Business Case and the opportunity to provide in depth feedback from our experienced subject matter experts.

We have set out some key observations below. These are in addition to our specific responses to the questions, contained within annexes to this letter:

- **Annex 1** contains our response to the specific consultation questions.
- **Annex 2** contains our further observations on the appendices included within the consultation.
- **Annex 3** contains a series of additional questions which we consider essential to drive further clarity and necessitating supplementary consultation, as highlighted below.

Key Observations

SSE strongly support the objectives of the programme in delivery of a reliable, fast and cost effective switching process which delivers appreciably better outcomes for consumers.

However, we do have an overarching concern that the level of detail offered in the business case is often inadequate, therefore preventing an effective response. This is clearly not ideal and within our response we have sought a constructive approach by including a set of essential questions which should provide clarity to stakeholders and generate appropriate and meaningful responses. We are therefore concerned that you "do not anticipate further consultations on the business case before it is baselined" and we strongly encourage a re-consideration of this approach which appears at odds with your intentions thus far in seeking effective, transparent and extensive engagement with industry.

We have previously indicated our concerns with the sums minded for the DCC in their delivery of procurement, for the new switching service – currently circa £30m. We have sought to draw attention at industry fora to relevant and comparative studies conducted on behalf of Ofcom on a related consumer service offering, to perform cross platform switching for fixed line voice, broadband and Pay TV within Great Britain. Their estimates to build and implement this brand new, and in our view comparable, supplier switching mechanism are circa £ 10-12m.[1] We believe on the face of the scale of differences between

[1] Further to detailed analysis, please note our summary findings:

The extensive report and appendices were prepared by independent consultants, Cartesian on behalf of another UK regulator, Ofcom for a recent and significant consumer switching consultation.

both sets of estimates, achieving a similar purpose , would appear to warrant a full review with the appropriate rigour and transparency.

Our concerns over the lack of clarity on the DCC Business Case are further heightened when we note in your covering letter that, "DCC should continue to be funded to participate in the switching programme in a broader set of activities than just procurement". We feel this aspect requires clearer definition and could materially impact on industry's view of a business case that represents value for money. A full and detailed definition of this "broader set" of activities intended for assignment to the DCC would therefore appear clearly beneficial for all to see.

In preparing this response, we are fortunate in drawing informed contributions from highly experienced staff with extensive and very relevant expertise. In particular our Commercial Group representative is ideally placed to provide a clear insight to help you in dealings with your service providers. We therefore welcome considerations on next steps at the earliest opportunity. If you have any questions on any aspect of this response, could you please direct this to both Martyn Edwards on martyn.edwards@sse.com and Mark Anderson on mark.anderson@sse.com

Yours sincerely

Adam Carden
Head of Industry Codes, Regulation

We accept the costings are based upon different models, but which are intended to deliver a similar overall purpose. A constructive and informative cost comparison is therefore achievable by taking the components of each whilst retaining a contextual view. The Cartesian proposals are for a modern mesh communications platform between communications providers and a Customer Information Management system, which 'synchronize customer information across all of service provider systems and reconciles customer data inconsistencies'. The modelling appears to include costs on behalf of all communication providers (similar total cost comparisons for all energy market participants are likely to arise from the RFI), so the proposal structures are different, but by 'considering in the round' are comparable.
In addition, unlike the market comparators offered in the parallel DCC margins and incentives consultation, this study appears to have greater credibility by being a more representative UK consumer based example, rather than drawing upon US or other worldwide principalities with macroeconomic characteristics and circumstances which differ to a greater or lesser degree.
Most importantly in terms of the significant absolute cost comparison, Cartesian's estimates are **£10-12m** (for build and implement of a new cross platform consumer switching function and service for the GB telecoms market). The Data and Communication Company estimates are **£30m** (for procurement only of a replacement switching service for the existing GB energy market). We believe on the face of the scale of differences between both sets of estimates, achieving a similar purpose , would appear to warrant a full review with the appropriate rigour and transparency, even if at a first glance you perceive the similarities as being superficial?
All of the Ofcom consultation material is available via the below link: https://www.ofcom.org.uk/consultations-and-statements/category-1/making-switching-easier

Annex 1: SSE response to specific consultation questions

Question 1: Is DCC's approach, as outlined in the business case, clear enough about how DCC will account for activities it is asked to undertake and how delivery can be assessed? If not how could this be improved?

We find that DCC's approach is not clear enough about how it will account for the activities that it is asked by Ofgem to undertake. There is very little detail in the draft business case about how DCC will account for it's activities and how delivery assessment will be carried out, other than very generalised mention of 'reporting', the Requirements Traceability Matrix (section 6.2.1), and a Switching Advisory Group with industry and Design Forums (section 8.3.2).

DCC identifies the following milestones as key indicators of their achievement:

- CRS technical specification complete
- CRS tender packs complete (for the latest of multiple major procurement projects)
- Contract award recommendation reports approved (for the latest of multiple major procurement projects).[2]

We are concerned that the low number and rather simplistic nature of the above milestones offered in the business case will not provide enough suitable indication for DCC to be monitored regularly and through earlier stages of activity, resulting in a lack of overall accountability, in addition to an overall lack of clarity regarding how DCC's activity towards all milestones would be assessed or regulated.

We would request that more information be provided by DCC on the governance and reporting structure that they would propose to use to manage the procurement process, in order to ensure effective measurement of DCC's activities. In addition, more definitive terminology, milestones and timescales should be provided by DCC in order to provide clarity on their planned activity, as well as avoid ambiguities in understanding of their remit in the role of procurement contractor.

Question 2: Are the business case's structure and base assumptions clear enough to use in setting a realistic programme budget and forecast charges as part of the ex post plus regime? What can be done to address any concerns?

The DCC draft business case's structure and base assumptions are not clear enough to use to set a realistic programme budget and forecast charges as part of an ex post plus regime.

DCC states within the business case that it will comply with Ofgem's overarching programme principles to exhibit certain behaviours, including being economic and efficient.[3] However it is arguable that DCC's proposal to operate under an ex post plus regime is in conflict with the desired economic and efficient behaviour. An ex post plus regime by nature lacks the necessary cost management structure to restrain costs from becoming excessive. There is also a risk that an ex post plus regime will put DCC, already a monopoly presence within Ofgem delegated activity, in a position of excessive power. We

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[2] DCC, Draft DCC Business Case for DCC activities during the Transitional Phase of the Switching Programme, v2.1, 23/11/16, Section 1.6.2, Item 37, p 13.

[3] Ibid., Section 6.3, item 99, p 29.

would recommend that an ex ante regime be considered, or at least an interim threshold regime in order to safeguard the integrity of the programme budget in the long term.

Regarding DCC's ability to set realistic costs, throughout the business case there is repeated reference to the 'high level of uncertainty' making it difficult to predict budget and forecast charges. We have concerns that the contingency costs described by DCC have been enhanced to unnecessarily high levels without proper justification beyond the aforementioned 'uncertainty'.[4]

Examples of the unnecessarily excessive charges mentioned in the business case include the Capita overhead charge at 9.5%[5], which would normally be assumed to already be included in the margin costs. A 15% margin is stipulated[6], which in an industry where 3-5% profit is standard, is extremely high. We would request detailed further justification as to why this high level of margin is required.

Overall, we would also request justification as to the high level and variance in the costs outlined between the previous version of the draft business case and this current version, where the costs appear to have been increased without specified reasoning in the document. The materiality threshold mentioned in the business case is levelled at 35%. We would argue that this level is not acceptable, and would have expected the threshold at between 1-10%. We also note that the materiality threshold was stated at 33% in version 1 of DCC draft business case, an extra 2% has been added in the current business case.[7] We also note that in the previous version of the draft business case, a majority of the staff resource cost was attributed to contractors and consultancies, whereas in the resource costing tables in this version of the DCC business case it is shown that permanent DCC staff will cover the majority of the resource requirement.[8] Therefore, it has not been clearly identified by DCC in this business case how their anticipated costs will reach such a high level.

Question 3: For those activities that Ofgem is proposing should be carried out by DCC but could be carried out by other parties (i.e. non-core activities not relating to procurement and development of the technical specification) have the correct activities been assigned to DCC or would other industry partners be better placed to take these on? If so, which activities, which industry partners and why would they be better placed?

We have identified from the draft business case several activities which are proposed to be carried out by DCC, but could be carried out by other parties or industry partners. We believe that to separate these roles from DCC and assign them to other parties would be beneficial to the programme. It would engender transparency through independence of

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[4] For example: Ibid., Section 6, item 78, p 25: "... there is typically a greater level of uncertainty associated with activities planned to take place further in the future. There are also a number of key design and delivery decisions still to be taken by the Ofgem Switching Programme that will determine DCC's activities during the remainder of the transitional Phase." Similar statements are repeated in Section 7, 7.1, 7.2,7.3, 8.3.4, 8.5.2, 9.3, 10, the key risks in table 25 (R008), 11.3, 11.4.1, 11.4.2, 11.5, 13.5.

[5] Ibid., section1.5.3, item 25., pp 11 of 117.

[6] Ibid., Section 1.6.1, item 32, p 12 and Section 9.1, item 210, table 13, p 63.

[7]Ibid., Section 1.5.1, item 23, table 1, p 10.

[8] Ibid., Section 9.4, Item 27, tables 16, 17 and 18, p 67 and Section 9.4.2, item 250, table 22, p 73.

activity ownership, and therefore improve the quality of output through focussed tasking and responsibility for each activity.

The following activities are examples of those which could be carried out by parties other than the DCC:

- Programme management[9] (i.e. Managing DCC's and other's input into the overall programme) – This is an activity which will cause a conflict of interest for DCC between its role as procurement contractor and a role of management and process alignment. We would suggest that Ofgem itself should provide overall programme management in order to monitor and align all processes, or if not possible, an independent body should be responsible for this very significant task.
- Data cleansing [10]– This is a very broad and wide ranging activity. Issues regarding data cleansing/ updating are currently an industry wide concern, so again a separate body external to the DCC, given this specific role as their task would be better placed to take an in depth review of the situation in order to generate an effective solution for all.
- System Integration[11] - Leadership of SI activity requires complex and intricate involvement with multifaceted industry systems, and should be assigned to a specialist role qualified in this area. A company which wins the tender process to build the CRS may be well placed to naturally progress into functioning in this role.
- Assurance[12] – It is stated in the business case that an independent assurance body would be sourced by Ofgem and paid for by DCC. We believe that this would negate the level if independence that the assurance body would have from DCC. Therefore we would suggest instead that an assurance body be appointed and paid for separately by Ofgem.

A related issue of concern to us is DCC's statement that it's current premises is at capacity at only 8 FTE[13]. We question their resource ability to effectively manage the procurement exercise, before the addition of any other responsibilities, as the amount of usable staff they have is so low. We would expect a much larger contingent of staff would be required for a programme of this size, including a number of experienced staff. We also question why they consider they have appropriate office space for a programme of this size and whether Ofgem considers that DCC do in fact have adequate software required to run a programme of this size (included in non staff costs).

Question 4: Should the management reserve and contingency (Section 11.4) be included within the upfront charges on industry and what is the justification for this? Does the level of management reserve feel appropriate for the Switching Programme, taking into account the type, scale and actuality of potential unknowns?

We propose that the management reserve and contingency is not appropriate and should not be included within the upfront charges on industry. This is because there is no formal

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[9] Ibid., Section 1.4, item 15, p9 and Section 8.3.1, items 131 and 132, p 43.

[10] Ibid., Section 7.3.2, item 111, table 6, p 35.

[11] Ibid., Section 7.3.2, item 111, table 6, p 36.

[12] Ibid., Section 1.6.2, item 39, p 13.

[13] Ibid., Section 9.5, item 253, p 73.

process within the Ofgem programme governance to approve the DCCs use of contingency and management reserve. Under the current proposal the DCC can use both these monetary resources and are only expected to report once this has happened. The DCC have also stated that the industry should fully expect all of this reserve to be utilised and there is no process to recoup any underspend.[14] We would request that there be a governance process in place that monitors the draw down of any management reserve or contingency. This should include appropriate justification and approval before distribution of funds.

[14] Ibid., Section 9.2, item 220, p 65: "For the avoidance of doubt, contingency and management reserve will be included within the charging statement, as the programme should expect that these costs will be incurred by DCC."

Annex 2: Observations on Ofgem appendices included alongside the consultation

Appendix A - Requirements Traceability Matrix

We note that though the Requirements Traceability Matrix contains a lot of detail, there are many gaps in significant information, and we would request that further information about these areas is required in order to ratify the business case. For example, there is no mention of the following areas or who will be responsible for them:

- Risk and issue management
- Governance
- Assurance
- Performance management
- Third party activity

We would also like to request further explanation of the following statement:

> "DCC's role should enable the Switching Programme to use DCC expertise across workgroups"

We suggest that this statement implies expanding the scope of DCC and their role in the Switching Programme. Please can we have confirmation of what is meant by this statement?

Additionally, we propose that the Requirements Traceability Matrix requires further scrutiny by Ofgem, especially with regard to DCC's costings of what is appropriate and reasonable and aligning those with Ofgem expectations. As DCC has raised these costings as a risk in the RAIDO log, it is therefore likely that this may be used to later justify a request from DCC for more budget and/or time to deliver the Ofgem/Industry interpretation if it differs from the DCC interpretation. This risk could be mitigated if clear measurements are put in place now.

Appendix B – Process Breakdown Structure

We note that the PBS diagrams may be subject to significant change in future. It may be possible to create and sign off plans for these activities now, however because a solution will not be chosen until October 2018 and deliverables will not be signed off until the end of DLS (with a milestone end date of February 2018). It would be useful to note here the expectation of change/ flexibility from the blueprint plan. We also note that the dates written into the PBS do not match with dates provided in the Ofgem plan. Which plan is correct/ which are the correct dates?

Appendix C - DCC Switching Programme Plan

We note that the deadline date for the RFI is set in this plan at 23/02/16. We would question whether Ofgem is set on the 23/02/16 as the deadline for the RFI? Would it not be appropriate and beneficial to the level of output to extend the date due to the scale of the RFI?

We would also query whether Ofgem accept to baseline this plan and hold DCC to account? Are Ofgem accepting of the October 2019 date?

There are a lot of additional activities which DCC have put on their plan which we would suggest may overstep their remit, in that they are assuming additional responsibility. Is Ofgem accepting of DCC's proposed remit as per this plan?

The plan also suggests DB2 (consultation publication) as August 2016 and DB3 (final decision) as December 2017. This is pushed to the right compared to what we had originally assumed to be delivered in May and September 2017. Is Ofgem aware of and accepting of the movement in these dates?

Appendix E - DCC Switching RAIDO

The DCC Switching RAIDO appears to indicate that DCC may need to take on a whole host of additional work. For example, additional work on a CRS industry interface, transition governance work and prescriptive technical specification requirements are mentioned in the RAIDO with no indication of potential timelines, costs or resources required to support this additional work. No mitigations are mentioned.

Throughout the business case, the RAIDO Log is referenced as the location for further information on all risks, assumptions, issues, dependencies and opportunities. However, within the RAIDO log there are only risks included. Have the assumptions, issues, dependencies and opportunities been documented elsewhere and will these be published for review?

We would like to highlight Risk008 in particular as worthy of further scrutiny and analysis. This risk reiterates the ‘uncertainty’ that is mentioned throughout the business case, however it is confirmed here in the RAIDO that there is no planned mitigation or proposed reduction in the level of uncertainty around DCCs procurement exercise until the end of DLS which is February 2018. We would argue that a risk should be noted here of a potential change in date to the right as a direct result of activity alignment with the end of the DLS.

Appendix G - DCC Assessment of Potential Incentives

The DCC Assessment of Potential Incentives is of great concern to us, because within the document DCC negatively reviews every potential incentive that could be applied to their involvement during the Transitional Phase of the Switching Programme and deems each incentive as ineffective or unnecessary, without adequate justification as to why the incentives are not appropriate. We would highlight the following incentives as of particular relevance to DCC involvement and would suggest they be reconsidered as appropriate incentives:

- Number of bidders
- DCC participation in workstreams
- DCC Switching Business Case quality
- General product quality
- Stakeholder engagement
- Product timeliness
- Time taken to transpose solution into technical specifications
- Variance to DCC Switching Business Case forecasts / materiality thresholds.

Also in relation to DCC incentives, on reading Ofgem’s consultation paper on ‘Draft direction on margin and incentives for DCC's role within the Transitional Phase of the Switching Programme’, we note that within this document Ofgem mention they are proposing to monitor stakeholder satisfaction with DCC activity via a six monthly survey, however Ofgem ‘do not intend to place margin at risk based on stakeholder feedback at this stage in the programme’ as they believe ‘reputational risk to be a sufficient driver'[15]. We would suggest that this is not enough of a measure on DCC's stakeholder activity. We would also suggest that the reputational risk mentioned is not enough of a significant driver. We would argue that instead, financial incentives would better motivate DCC toward effective and timely delivery.

[15] Ofgem, Consultation paper Draft direction on margin and incentives for DCC's role within the Transitional Phase of the Switching Programme, 24/11/2016, p 6.

Annex 3: Supplementary questions necessary to complete the consultation response

Please find our further and more detailed queries on the Business case, arranged by Question area and supporting document title below.

As previously indicated we consider these additional questions essential to provide clarity on DCC's Business Case and may necessitate a supplementary consultation.

Question 1: Is DCC's approach, as outlined in the business case, clear enough about how DCC will account for activities it is asked to undertake and how delivery can be assessed? If not how could this be improved?

Please can DCC define the meaning of the terms:

> 'regular' – as used in context: "Under the ex post plus arrangements, DCC is required to set out its planned activities and costs upfront in a published business case and report its actual and forecast costs to Ofgem on a regular basis throughout each regulatory year."[16] Similar contextual usage arises in Section 1.7 and Section 42.
>
> 'endeavour' – as used in the context: "In the first baselined version of the DCC Switching Business Case to be published in March 2017, DCC will endeavour to align the scope scenarios more closely to the reform packages included in Ofgem's Blueprint Request for Information." [17]

Will Ofgem consult with industry on whether to give to give responsibility to DCC for the delivery strategy and security and service management during the DLS phase and Transitional Phase? [18]

Can Ofgem define the boundaries that would fall under DCC's remit in the role of Programme management? We are concerned about a conflict of interest here. [19]

Can Ofgem confirm whether DCC is correct in defining its First General Objective as to develop, operate and maintain the CRS? From previous published documentation and discussion we had understood their only agreed objective was to procure the CRS. [20]

Can Ofgem confirm whether DCC is correct in defining its Second General Objective as to include 'reduction of charges payable for mandatory business services'? Industry had previously been told at EDAG 11 (as per Meeting minutes, point 7), that any savings will be non recoverable. [21]

Can Ofgem confirm whether DCC will have involvement in commercial arrangements in DBT and live operation phases? This is implied in the business case. [22]

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[16] DCC, Draft DCC Business Case for DCC activities during the Transitional Phase of the Switching Programme, v2.1, 23/11/2016, Section 1.2, item 3, p 5.

[17] Ibid., Section 1.3, Item 10, p 6.

[18] Ibid., Section 1.3, Item 11, p 6.

[19] Ibid., Section 1.4, Item 15, p 9.

[20] Ibid., Section 5.2, Item 73, p 22.

[21] Ibid.

[22] Ibid., Section 8.4.1, Item 161, p 52.

Question 2: Are the business case's structure and base assumptions clear enough to use in setting a realistic programme budget and forecast charges as part of the ex post plus regime? What can be done to address any concerns?

SSE's recommendation is an ex ante regime be considered instead of the ex post regime proposed in the draft business case. The points below outline our concerns regarding an ex post regime:

DCC proposed incentive milestones do not start until autumn 2018, therefore between now and then are we to assume that the DCC are guaranteed all payments even if they do not fulfil their remit adequately? [23]

DCC's proposed margin is 15% with a fixed rate of return, so we perceive that there is no incentive for DCC to pertain the most cost effective rates from suppliers because DCC is guaranteed this money regardless of costs paid, is this correct? Also, we question whether the 15% margin is on top of external costs? We query this because DCC was awarded the procurement contract based on internal costs only, so are there additional non staff costs, additional 9.5% overhead as well as the 15% margin? We also note that the 15% margin is ex ante so fixed throughout whole programme. [24]

> "This is a downside-only financial incentive. DCC proposes that the level of margin at risk is proportionate to the percentage of the cost base for DCC activities relating to delivery of the incentivised milestones. Based on the current forecast costs this equates to 25% of DCC margin at risk."

DCC are stating here that only 25% of their margin is at risk, this would mean that they are guaranteed 75% margin. What is the rationale behind this? [25]

Could OFGEM clarify why they believe it is appropriate to classify external contractors and consultants as internal costs? (external costs are defined as being, "those relating to Fundamental Service Providers") [26]

Appendix E - DCC Switching RAIDO

Ofgem may require DCC to lead on the majority of activity including transition, governance, assurance, etc. [27]

Throughout it suggests that DCC have planned/costed on their role being very basic outside of the procurement process and as such we think it is likely that the £34m costs will increase. This is because DCC have baselined their role as taking minimal responsibility whereas Industry and Ofgem believe DCC's role to be more onerous and accountable.

We believe the tender packs should be built with contractual milestones and incentives. Meeting these milestones will significantly deter and mitigate industry and the programme from delay. [28]

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[23] Ibid., Section 1.6.2, Item 37 p 13.

[24] Ibid., Section 1.6.1, Item 32 p 12 and Section 9.1, Item 210, table 13, p 63.

[25] Ibid., Section 1.6.2, Item 38 p 13.

[26] Ibid., Section 13.4, Item 340 p 101.

[27] DCC, Appendix E DCC Switching RADIO, 8/12/2016, Risks 011, 020, 022, 023, 024 & 028.

[28] Ibid., Risk 030.