Energy UK

The voice of the energy industry

Energy UK Response to Ofgem Consultation on DCC Price Control: Regulatory Year 2019/20

23 December 2020

About Energy UK

Energy UK is the trade association for the energy industry with over 100 members spanning every aspect of the energy sector – from established FTSE 100 companies right through to new, growing suppliers and generators, which now make up over half of our membership. We represent the diverse nature of the UK's energy industry with our members delivering over 80% of both the UK's power generation and energy supply for the 28 million UK homes as well as businesses. The energy industry invests £13bn annually, delivers £31bn in gross value added on top of the £95bn in economic activity through its supply chain and interaction with other sectors, and supports 738,000 jobs in every corner of the country.

Question 1: What are your views on our proposal to consider External Costs as economic and efficient?

Energy UK shares Ofgem's concerns on DCC's contract management and procurement processes more generally; this area has historically been one that Energy UK and members have raised concerns on to DCC, BEIS and Ofgem. This is especially relevant in relation to the cost of change quoted by DCC (and its service providers) for change impacting DCC systems (including Comms Hubs) and the amount of time taken by DCC to complete impact assessments of any industry driven change, as well as BEIS driven changes.

Although Energy UK broadly agrees with Ofgem's assessment, we have concerns that categorising costs relating to CSP North in particular as 'economic and efficient' is not indicative of the level of service provided by Arqiva as an external service provider during the regulatory year. As discussed in the answer to Questions 8, 9 and 10, there are several areas of specific and repeated poor performance within the Northern CSP region; throughout the Regulatory Year, DCC has not been able to sufficiently demonstrate that they have exercised the appropriate and necessary contractual leverage with Arqiva to make any meaningful steps to rectifying these ongoing issues. These issues continue to have a disproportionate impact on suppliers' ability to progress the roll-out in the north in an economic and efficient manner.

As such, Energy UK would urge Ofgem to continue to implement clear processes to seek evidence from the DCC that it is taking all appropriate and necessary steps available through its contractual relationship with Arqiva, and for the DCC to appropriately ensure that DCC's Customers are suitably protected and recompensed for the continued and repeated issues in the CSP North network that inhibit the roll-out. This should include, but not be limited to, appropriate reporting of Arqiva performance against the Service Level Agreements within the contract, details of any sanctions or action imposed by the DCC on Arqiva where a Service Level Agreement or any supporting documents (including, but not limited to the Joint Industry Plan) are breached, and how these can be used to provide financial recompense to DCC's customers unduly affected by delays resulting from CSP North. Energy UK welcomes further engagement from Ofgem on this point, including on how this information can be appropriately shared via industry forums, the SEC Panel and its subcommittees.

Additionally, Energy UK notes that 2019/20 is another year where the DCC have drastically exceeded their forecasted costs, which significantly disadvantages its customers. Although some of these are passed on through the Price Cap, DCC customers rely on being provided with accurate forecasts in order to manage cashflows and costs within their own Smart Programme, and as such significant increases in actual costs create additional pressures within the Smart roll-out, regardless of whether they are deemed economic and efficient. Energy UK urges Ofgem to require the DCC to improve its overall forecasting process, and to apply additional pressure on the DCC to encourage it to meet the forecasted costs as much as possible. Energy UK notes that this is something that has been requested in previous Price Control consultations, and as such requests that Ofgem begin affecting this change as soon as possible.

Question 2: What are your views on our proposals on DCC's approach to benchmarking of staff remuneration for both contractor and permanent staff?

Energy UK agrees with the Ofgem's proposal to disallow costs relating to benchmarking of staff remunerations. This is an area of significant concern for Energy UK and its members, particularly due to the fact this issue was raised by Ofgem in the previous Price Control consultation round. DCC's customers provided a clear set of recommendations within their responses last year for the DCC to ensure that remuneration was benchmarked against the whole staff costs, rather than on salaries alone.

It is therefore disappointing that these recommendations have not been followed ahead of this Price Control round, and that the DCC has not been able to demonstrate lessons learned from previous rounds of Price Control consultation and engagement with its customers through the appropriate governance and advisory forums. As such, it is wholly appropriate for Ofgem to disallow costs in this area, and Energy UK hopes to see that DCC have implemented the proposed actions as part of their next Price Control submission.

Question 3: What are your views on our proposals to disallow the cost of DCC's retention scheme?

Energy UK agrees with this proposal. Whilst Energy UK agrees that DCC needs to attract and incentivise talent, in order to ensure that the DCC is fit for purpose (which is the same for every organisation operating in the market), incentives should be targeted to award good individual employee performance and loyalty/long-service. It is therefore concerning to read Ofgem's assessment of how these retention benefits were being allocated, and Energy UK is disappointed that the DCC has not been able to demonstrate what other efficient options have been explored in order to boost staff retention.

Question 4: What are your views on our proposal to disallow the incurred and forecast costs associated with the product management team?

Energy UK agrees with this proposal and welcomes Ofgem's position that the DCC should not be expanding outside of core business operations without appropriate consultation with key stakeholders. This is a longstanding concern of Energy UK, our members and other DCC customers. DCC Users, especially Energy Suppliers, are facing year-after-year increases in costs, and it is a common opinion that the DCC must focus on getting the basics right before expending on new business and products. There is a concern that DCC sometimes needs to be reminded that it is a regulated monopoly, and so the focus of its core business should be at the forefront of its approach to delivery. Therefore, ensuring that DCC gets the basics right is a key aspect of this, in order for DCC to deliver a fit for purpose, stable and scalable infrastructure and especially across all CSP regions. It also is disappointing the DCC has not learnt the lessons from their proposed implementation of the Ecosystem Management Framework, especially around not following its own governance processes for obtaining customer support and buy-in for proposed new business initiatives and activities.

There is a perception amongst DCC Customers that it appears DCC's general approach when responding to technical impediments, whether actual or forecasted, is to increase staff numbers and therefore expenditure on staff, in order to rectify the issue. Energy UK notes that this is generally not a cost-effective or efficient approach, and leads to unnecessary costs being incurred without justification, which is of course to the detriment of DCC Users and the relationship between the DCC and its customers.

Additionally, it is disappointing that the DCC have not segmented core and future business functions within the product management team; this is a frustrating move given the need for accountability on costs that are being incurred as a direct part of administering the roll-out, versus those which the DCC is using to expand its own business structure. Energy UK urges Ofgem to enforce a stricter segmentation in how internal costs such as these are reported.

As with other questions within this consultation, Energy UK notes that it is important for the DCC to be able to demonstrate that DCC is fully costing and justifying additional spend in an economic and efficient manner, and are demonstrably engaging with their customers to seek views and gauge support. The DCC must prioritise actively seeking consensus through the appropriate advisory forums when attempting to justify expenditure on projects such as this, and must improve the level of transparency on all costs and associated justification provided which also needs to be supported by a consistent and fit for purpose communication approach.

Question 5: What are your views on our proposal to disallow the forecast variance of the Commercial Operations and Vendor Management teams?

Energy UK agrees with this Ofgem minded to decision in respect of the DCC's Network Evolution Programme. Energy UK and its members are supportive of the Network Evolution Programme, and remain committed to working with the DCC to ensure that it is able to be implemented swiftly with no compromise to quality given the issues DCC have encountered historically with Comms Hubs firmware (especially for CSP North). However, there remains significant ongoing concerns around the level of cost-detail and information provided to DCC's customers as part of the Network Evolution Programme, and as such, it is therefore disappointing that the DCC have not been able to appropriately evidence them in their submissions for Regulatory year 2019/20.

It could be argued that this is merely due to the Network Evolution Programme being in its relative infancy during this regulatory year, and that the DCC now has a more significant evidence base for costs of the Network Evolution Programme for use by the next Price Control round. However, there is still disappointment that the delay in this programme has resulted in this outcome with DCC unable to provide significant evidence to Ofgem – bearing in mind the initial 2G/3G sunsetting risks were discussed with DCC in the latter part of 2018.

Question 6: What are your views on our proposal to disallow the incurred cost variance associated with Preston Brook?

Energy UK agrees with this Ofgem minded to decision, and concurs with the DCC's assessment of how the transfer from Preston Brook to Brabazon House could have been managed. Additionally, allowing any additional costs to be granted for administering this move poses a risk of creating perception of conflicts of interest, given that Preston Brook is home to other Capita functions, and that the DCC already recover a shared service charge as part of the Price Control Process.

Question 7: What are your views on our proposal to disallow all variance in forecast internal costs?

Energy UK agrees with this proposal. There is a need for the DCC to provide more evidence and accurate costs for all of its work. The Smart Programme is at a critical juncture, and at a time when DCC customers are continuing to make efficiencies in their spending, it is important that the DCC demonstrate that they are also committed to delivering their part in the roll-out in a cost-effective manner and to ensure focus on DCC's core business.

Additionally, where the DCC propose variations to future internal costs, Energy UK expects that as part of the application, it should be able to demonstrate that they are simplifying and unifying their own organisational structure in order to deliver cost-efficiencies wherever possible. Currently there is significant concern about the disjointedness of the DCC's various functions (e.g. design, operations, regulation, etc…) which is particularly evident in the DCC's engagement with its customers, and it is often difficult to find consistent answers on the current progress and future planned DCC operations and projects. As such, in future Price Control rounds, the DCC must ensure that it is committed to streamlining their internal operations, delivering cost-efficiencies where possible, and ensuring internal alignment in its approach and external communications with DCC Users.

Question 8: What are your views on our proposed position on DCC's operational performance?

Whilst Energy UK broadly agrees with Ofgem's position based on the metrics provided, there remains significant concern that the current metrics within OPR do not accurately capture the specific operational requirements on the DCC, and as such, that the DCC is therefore being over-rewarded by design within the current OPR framework.

In particular, Energy UK is concerned that the SDM2 Core Service Requests methodology does not accurately capture the significant disruption seen in Install and Commission times and the distribution of over-the-air Firmware upgrades, particularly pronounced within CSP North during the Regulatory Year, including the accuracy of reporting performance for actual over-the-air Firmware upgrades. This reinforces the view that costs incurred for management of this contractor cannot be viewed as economic and efficient.

These issues have a disproportionate impact on the ability for suppliers to ramp-up smart meter installation activity in this region, and as such, the financial detriment faced by DCC customers go beyond the incentive figure captured within the OPR framework. It should be noted that this has naturally resulted in suppliers having to 'back-end' installations beyond 2020, and where they are facing constraints on being able to ramp-up installations due to the Price-Cap.

Energy UK therefore welcomes the implementation of the new OPR framework announced by Ofgem, which will allow failings in specific regions to fully be accounted for when assessing DCC Operational Performance. Energy UK assumes that this will allow Ofgem to fully account for the concerns raised by DCC's customers about poor DCC performance in specific CSP regions.

Question 9: What are your views regarding DCC's failure to ensure all CSPs met their contractual milestones and its wider performance in the North region?

It is disappointing that the DCC has been unable to ensure that Arqiva were able to provide full WAN coverage in line with their contractual milestone; this is somewhat reflective of the overall state of affairs in the CSP North region. As noted previously in this response, Energy UK and its members do not believe DCC has demonstrated that it is appropriately managing Arqiva as an external service provider, including failing to wield all necessary and appropriate contractual leverage where repeated poor performance has been encountered. During Regulatory Year 2019/20, these include:

1. The repeated delays encountered in the development and deployment of R2.0 Comms Hub firmware, especially where Comms Hub defects are being found by Energy Suppliers in their User Interface Testing – these defects should have already been identified by the CSP and DCC by the time the System Integration Testing phase completes.
2. Ongoing network stability issues, including the ability for Smart Prepayment to be deployed at-scale.
3. Installation and Commission Times, especially when compared to CSP Central and South.

As discussed in Question 1, 2019/20 marks the second Regulatory Year of poor performance in the CSP North region, with suppliers effectively prohibited from rolling-out Smart Prepayment to customers within this region, and the delayed availability of Dual-Band Comms Hubs nationally. Both of these are needed for the roll-out to progress at pace, protect the consumer experience, and for the roll-out to be completed in an efficient and cost-effective manner. In addition, the delays to the delivery of the Dual-Band Comms Hubs has resulted in significantly increased termination rates which has driven huge cost into the Programme and adversely impacted customer sentiment to the detriment of necessary rectification works to complete the gas meter installation.

Many believe that the primary cause of some of these issues appears to stem directly from instability within the CSP North network itself; industry is yet to see any evidence from DCC or Arqiva on whether that is as a result of sub-optimal network design or another reason. What is clear however, is that although some issues may be encountered in CSP Central and South (Telefonica), they are exceptionally more pronounced within the CSP North region. It is therefore particularly concerning that suppliers are having to continually fund rectification work, both through the DCC charges and through additional internal rectification processes by suppliers (including operating distinctly different processes and procedures) in order to operate in all CSP regions in the same manner.

It is worth highlighting that in December 2019 Energy UK developed a paper capturing a summary of Arqiva issues; this paper was provided to BEIS SMIP Stewardship and DCC's Senior Management to support discussion at the BEIS SMDG meeting that month. A copy of the Energy UK paper is included as an Annex at the end of this response. Following discussion at the BEIS SMDG, DCC then helpfully established the DCC CSP North Common Issues Forum in January 2020 to progress improvement plans. Whilst Energy UK welcomes the establishment of the DCC CSP North Common Issues Forum, many parties are concerned that little progress has actually been made to deliver overall operational improvements. The main focus at the DCC CSP North Common Issues Forum appears to have been on the Install and Commission process to ensure parity with CSP Central and South, and to address EDMI Comms Hub firmware issues. Given that it is now a year since the Energy UK paper was submitted to BEIS and DCC, Energy UK has asked BEIS to include an agenda item at the December 2020 BEIS SMDG to propose a SMDG focused deep-dive session in January 2021 for a stocktake on Arqiva progress against the issues highlighted in the Energy UK paper.

It is only late into the subsequent Regulatory Year 2020/21 that CSP North has entered the early stages of being able to support installation of SMETS2 Prepayment meters at scale, and that Release 2.0 Firmware has been available for EDMI Comms Hubs, significantly later than their equivalent counterparts in Central and South regions and for WNC and Toshiba Comms Hubs. Given that the root cause for many of these issues remains as yet undetermined, despite customers having raised them with the DCC for a significant period of time prior to this availability, it is also important that the contractual arrangements between Arqiva and the DCC are subject to greater scrutiny and transparency, particularly relating to enforcement of Service Level Agreements and sanctions. Energy UK notes that it raised this issue at the December 2020 SMDG meeting, and noted that it is important that Ofgem begins holding DCC to account for poor management of its external contract providers.

As such Energy UK and its members continue to be concerned about DCC's management of its external service providers, and note that in the specific instance of the WAN connectivity milestone, that the DCC has not appropriately evidenced why this issue could not have been sufficiently forecasted and accounted for. As such, and noting the other issues in the CSP North region, Energy UK expect Ofgem not to accept the DCC's request to raise the margin earnt for this milestone.

Question 10: What are your views on our proposed position on DCC's project performance?

Energy UK agrees with Ofgem's position. As discussed in the answer to Question 9, the delays to R2.0 availability in CSP North have significantly hindered the ability for suppliers to progress the roll-out.

Whilst Energy UK and its members appreciate the work gone into Release 2.0, it was still subject to significant delays that have inhibited the effective roll-out of Single Band Comms Hubs in the CSP North region and also overall delivery of Dual-Bad Comms Hubs for both CSPs. This has had and will continue to cause significant financial detriment to suppliers, due to them effectively needing to 'back-end' installations for previously technically ineligible customers into a time period that is both covered by the price cap and also subjects them to hard-targets under the new roll-out framework proposed by BEIS[1]. As such, Energy UK agrees that the DCC should not earn margin on this milestone, but also urges Ofgem to consider the holistic impact of the delays on the Smart roll-out.

Question 11: What are your views on our assessment of DCC's application to adjust its Baseline Margin?

Energy UK agree with Ofgem's proposal to reduce the DCC's Baseline Margin adjustment.

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

Whilst Energy UK cannot comment on the specific merits of each of the DCC's refinanced contracts with the CSPs and DSP, it notes its concern that the DCC is earning margin on the refinancing of these agreements. Whilst Energy UK welcomes top line savings these refinanced agreements provide for its

[1] BEIS' Consultation on the minimum tolerance and target levels under the Post-2020 Framework

members, enduring problems with the services provided still have a significant downstream financial impact on DCC's customers, in particular as discussed in the answer to Question 10.

As such, it is therefore disappointing that the DCC receives ECGS on these contracts when their overall impact on the DCC's customers and the overall costs associated with the roll-out programme is not taken into account. With that in mind, Energy UK notes its agreement with the measures proposed in Ofgem's consultation on increasing DCC's revenue at risk against OPR to ensure that poor performance against OPR is netted off against ECGS gains.

Question 13: What are your views on our assessment of Delivery Milestone 1?

Energy UK agrees with this proposal. The evidence is clear that the DCC missed the milestone and doing so had a significant financial impact on its customers.

Should you wish to discuss any of the above further, please do not hesitate to contact Daisy Cross at daisy.cross@energy-uk.org.uk

Annex – Embedded Energy UK (December 2019) paper for BEIS SMDG on Arqiva issues:

For BEIS SMDG _
Energy UK paper on