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16th July 2024

Email to: DCCRegulation@Ofgem.gov.uk

Dear Jakub,

DCC Review Phase 2: Governance and Central Registration Service arrangements

We welcome the opportunity to respond to Ofgem's consultation on DCC Review Phase 2: Governance and Central Registration Service (CRS) arrangements. Our response is non-confidential and may be published. We have set out our key observations below and our answers to the consultation questions are in the appendix.

General

Ofgem needs to ensure that the new DCC Licensee delivers higher smart metering system performance as it is a crucial element of energy infrastructure. Although governance is important, improvements in performance measures overseen by Ofgem are also crucial in protecting the interests of consumers. We support Ofgem in making these decisions, however, we need to see the whole package before we can reach any conclusions on Ofgem's proposals.

With any procurement under a competitive tender, the whole package of profit, governance and incentives are key to delivering good quality tenders and outcome for customers. We are concerned that the whole package is currently unclear, making it difficult to assess the governance aspects of Ofgem's consultation in isolation.

DCC costs are also a growing component of consumer bills so important to deliver value for money to consumers. With the roll out of 4G its budget will grow further. Effective regulation and governance as the licence comes up for renewal and potential reassignment is therefore essential.

Not for Profit status

We responded to the original consultation on the future of DCC in January 2023¹. At that time, it was our view that a not-for-profit (NFP) entity would be the best way to deliver DCC services. Following a recent initiative by SECCo, we have reconsidered this view and were recently signatories to an industry communication stating that Ofgem should also consider a "for profit" approach alongside the NFP option. We also recently commissioned research by

¹ <https://www.ofgem.gov.uk/consultation/dcc-review-phase-1-consultation>

Economic Insight on the application of incentives regimes on NFPs in the context of the NESO licence. This highlighted some of the difficulties in creating meaningful incentives especially for an organisation like DCC that will itself be negotiating contracts with a range of providers.

We are also concerned that a NFP will restrict the amount of potential bidders for the new licence, even if there are potentially non-core activities that can be profit making. Indeed, we are concerned that management time will be diverted away from the core purpose in that case.

Finally, the growing proliferation of not-for-profit and/or government owned entities in the sector risks creating complicated relationships, potentially creating a lack of transparency, and unclear ownership of industry deliverables, which is not in the interest of consumers. The accountability for deliverables and performance could become opaque to industry parties who are trying to deliver to end consumers and businesses.

As an example, we could see a situation emerging where there are numerous NFP and/or government owned parties interacting:

- Ofgem, as a non-ministerial government department as the strategic authority for codes.
- a not-for-profit code manager overseeing the change process and monitoring compliance.
- a publicly owned NESO with a wide-ranging role over the whole energy system
- DCC as a not-for-profit organisation with a central role of in the management of data flows to facilitate the market.

If a NFP structure is maintained, there also needs to be more analysis of what this means for governance and what lessons there are from other public sector or third sector entities e.g., Trusts and other bodies.

The consultation also seems to be written as if the Board will be serving a commercial driven entity so there appears to be some inconsistency with this and a potentially NFP entity.

Responsibilities of the Board

Before considering the makeup of the Board membership, Ofgem needs to consider what decisions will be taken by the Board as opposed to executives; this is not clear from the consultation. A draft Terms of Reference should be established and a scheme of delegation in terms of decision processes. As a minimum we would expect the Non-Executive Board to be responsible for:

- appointment and dismissal of the CEO and other senior staff,
- sign off accounts and strategy documents,
- sign off regulatory Business Plan and major expenditure or contractual decisions, and,
- challenge and hold the executive to account.

User representatives on the Board

Whilst we understand the rationale for Sufficiently Independent Directors (SIDs), we strongly believe that User representatives should be included on the Board, so the Board hears directly from Users the impact of DCC's performance and development. If User representatives cannot be on Board, then the recent Xoserve Board stakeholder led appointment process for Non-Executive Directors (NEDs) appears to have worked well.

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Always willing to discuss further, please contact myself or Rochelle Harrison.

Yours sincerely,

[Via email]

Will Webster

Head of Regulatory Economics

Centrica

APPENDIX

DCC Board composition questions

1. What are your views on the presented options for the future DCC board composition? Do you agree with our analysis that Option 4 (majority independent model) is the most appropriate to take forward? Please state your reasoning.

Given DCC's monopoly position and the impact its performance has on stakeholders' businesses, we strongly believe that stakeholders, i.e. users, should be represented more explicitly than in a majority independent model. The Board needs to hear directly from stakeholders any impacts poor performance is having or how potential investment decisions will impact, which we feel does not adequately happen via DCC's executive team currently. Therefore, our preference would be for User representatives to be able to sit on the Board.

We agree that the Board should have at least one consumer representative, we would prefer that more than one director had consumer advocacy experience (please see answer to question 5) and majority independent would be beneficial. However as mentioned above, we strongly feel that DCC's Board should include representatives from the industry it serves. In our consultation to the Code Managers consultation, we referenced the example of RECCo, and we think similar considerations apply here.

The RECCo example demonstrates that having directors who are currently engaged in the relevant segments of the energy industry is vital in the formation and development of a code manager. This ensures the code manager's operations and strategy remain focused on the most important issues to our industry. They can contribute a wealth of experience at a guiding level. Diversity in the board membership negates any concerns on impartiality and we believe your concerns in this area are unfounded given the role of a board. We prefer 50% to 80% of code manager board directors to be directly engaged in the industry, with a minimum of 50%, and do not support more prescriptive measures. Independent directors are welcomed with the relevant experience and skills to add to an effectively functioning board, but we don't believe they are a requirement for code manager impartiality and efficient operation.

We also ask that Ofgem considers whether a Trustee Board approach could give the right balance between User / Stakeholders' input and challenging executive team to improve performance. A Trustee style Board that has stakeholder representatives and sufficiently independent directors making the majority should be examined in the event of a NFP model being used. The Board should then have the objective of focusing on performance improvement that impact energy consumers in the first instance which energy industry stakeholders understand well.

2. What are your views on the current and proposed Licence requirements on Sufficiently Independent Directors? Do you agree that one or more of the current Licence-imposed Independence Requirements may be relaxed in favour of more discretion afforded to the Board?

Yes, we agree that having independent directors with recent experience in either a DCC customer or service provider's organisation would bring helpful insight and so the Licence Condition (LC9.8) should be relaxed. However, stronger representation from SIDs with energy industry experience, particularly consumer facing organisations, would be more beneficial in improving the performance of DCC for consumers.

A consumer objective in the Licence could also bolster the Board's direction of the executive team. Such as, *due regard must be taken to ensure that value for money and expected performance are delivered to end consumers from strategic and operational*

decisions made by the Board and Executive team. Expected performance would be the target OPR measures (once the regime is fit for purpose).

3. Do you agree with our proposal that the Chair of the future DCC board should meet the requirements on 'Sufficiently Independent Directors' without exception?

Yes, we agree, especially if the Chair has the casting vote in a split Board decision.

4. What are your views on our analysis and proposal not to introduce additional requirements or restrictions on the size of the future Board and on the number of executive members and shareholder representatives?

With a majority independent and stakeholder board, we agree that restricting the number of shareholder and executive members is not required.

Board appointment process and requirements questions

5. Do you agree with a possible requirement on the Board to possess expertise in certain core areas? Do you agree with the areas we have identified? What are your views on the implementation options?

We agree that amongst the Board the core expertise should be covered by the diversity of experience within its membership. However, we believe that there being a consumer champion should not be covered by one member alone and should have a minimum proportion [say 25%] of the Board, also including industry representatives. As mentioned above, DCC should also have a consumer objective in the Licence.

6. Do you agree with our proposal to represent consumer voice via a requirement on the appointment of a Sufficiently Independent Director with consumer advocacy experience?

Yes, but as mentioned above, our preference would be for more than one SID to have consumer advocacy experience, along with a consumer impact licence objective.

7. What are your views on Ofgem's role in the Board appointment process? Do you agree with our proposal that the Authority could have a role in the appointment process of non-executive directors? Which option would provide the most appropriate and effective accountability framework, and why?

We are unclear whether Ofgem's role would be a help or a hinderance in the process, nor what risk is mitigated by this step, particularly if gaining Authority approval significantly slowed down the appointment process. We suggest that Ofgem applies a 'fit and proper' test to Board members appointments, during the appointment process, instead.

8. What are your views on the role of DCC customers and other stakeholders in the Board appointment process? Do you agree with our proposal to provide representation for DCC customers on the Nomination Committee? What should be the role of an industry representative in such an arrangement?

As mentioned above, we would prefer direct stakeholder representation rather a nominee SID, however if stakeholder involvement on the Board is not agreeable to Ofgem then the current Xoserve Shipper nominated Non-Executive Director (NED) process seems to have worked well.

Xoserve's governance arrangements require 4 Shipper nominated NEDs and 4 by networks [Funding, governance and ownership \(xoserve.com\)](#) Shippers are required to have a nominations committee who appoint their NEDs (made up of 2 I&C Shipper reps and 2 Energy UK member reps). The committee scoped with Xoserve what skills and experience were needed for the 3-year term for the NEDs, adding plenty about engagement with Shippers. We shortlisted and interviewed the candidates (longlisted by a recruitment consultant) and made the appointments. Xoserve did not have to approve, but they were keen on the ones chosen. Direct engagement in appointing is needed to make sure the industry knowledge and challenges are understood, but the industry needs to input to and agree on a scope for each role that will serve a business purpose.

9. What are your views on our proposals for an additional requirement on the Chair's experience and Ofgem's role in the initial appointment of the Chair? In what other way should the appointment process for the Chair be different to that of other DCC Board members?

We agree that the Chair should have Board level experience of an organisation a similar size and status as DCC. Whilst we feel that Ofgem should be able to veto a Chair's appointment due to their level of experience or not being fit and proper, we are unsure what risk mitigation or help having Ofgem's approval would give.

More widely Ofgem should consider the order in which Directors are selected and who is responsible for this, as it is not clear from the consultation. Ideally both Ofgem and DCC Users should have an influence on the nomination of both the Chair and the SIDs.

Incentivisation questions (Chapter 4)

Unfortunately, DCC does not have incentives from competition, which would lead to stronger performance management, as customers cannot choose to shop elsewhere – this is what shareholders / for profit organisations have as signals to apply pressure to management. Reputational incentives have little value for monopoly businesses as customers are unable to go elsewhere regardless of reputation or media scrutiny. This is one of the reasons we would suggest Ofgem reconsiders whether the licensee should be a for profit organisation.

The vote of no confidence in entire Board should be voted for by stakeholders that are impacted by DCC's performance and cost – i.e., fund payers and network users. The level of impact also needs to be considered, i.e., proportionality, possibly with small users having a single vote under a certain threshold. Proportionality needs to be carefully considered so the larger users are not penalised when there are a significant number of small users. One possibility would be for small users to have a pooled voting block into a max of 10 out 100 votes.

10. What are your views on changes to the term of appointment of non-executive directors? Do you agree with our proposals to limit the initial term of appointment for non-executive directors to 3 years, and to allow for up to two reappointments with the total term limited to a maximum of 9 years?

This proposal seems reasonable; however, appointments should be lagged so all SIDs are not renewed or appointed at the same time. Corporate memory is key for an organisation like DCC where programmes, contracts and even step change can take several years to deliver. At the same time, 3-year terms allow for changes to be made in the makeup of the board's skills and experience in line with developments in the industry and requirements on DCC.

11. What are your views on the identified reputational incentives and associated enhanced regulatory requirements? How effective do you believe these incentives can be?

Reputational incentives for monopoly businesses have virtually no impact on driving performance improvements. However, if used for executive remuneration packages reputational incentives may have more impact. Alongside the changes to governance, the Operational Performance Regime must be properly aligned and measured to energy consumers' key interests, i.e. made fit for purpose.

A customer satisfaction survey run by an independent organisation would be an improvement on the current customer satisfaction report written by both SEC Panel and DCC. Whilst we agree that DCC should have a right to reply, being able to influence the score is inappropriate as DCC has a conflict of interest.

As the Smart DCC licence is a monopoly, customers and end consumers have no route other than performance metrics to signal issues and obligate DCC to improve. Therefore, it is essential that the performance regime is targeted and measured correctly to alleviate end consumers' pain points within DCC's ecosystem. These must include (but not limited to):

- the length of time and number of system outages per year (maintenance, incidents, Business Continuity and Disaster Recovery (BCDR) testing etc.), regardless of whether 'allowed' by SEC.
- prepayment vend success;
- download and activation of Over the Air (OTA) Firmware (FW), to ensure devices are maintained.

We agree that cost management should be aligned to the performance process and DCC should continue to publish an annual business plan covering the next five years. Ofgem should encourage DCC to include in its business plan, forecasts for all 5 years' costs and prices, alongside expected improvements in service and metrics.

12. What are your views on direct financial incentivisation of executive leadership and key staff? What would make those incentives effective? Please consider their interlink with the reputational incentives.

As part of our response to the consultation on the NESO licence we commissioned a report to look at appropriate incentive structures for, what will be, a government owned entity. Similar considerations are relevant for DCC, if the NFP model is used.

We shared our NESO licence / Economic Insights report with yourselves, and we are happy to discuss in detail if needed.

13. What are your views on the proposal to grant stakeholders the power to issue a (non-binding) motion of "no confidence", its objective and requirements? If implemented, what should be the methodology for determining a qualified majority and distribution of votes among stakeholders?

It has some merit, but we are concerned that it will remain unused due complexity of issuing the vote and majority or held back in case a bigger issue arises later in the year (such as when a major programme or release goes live).

The voting should be aligned to the proportion of funds each DCC User pays towards DCC's fixed charges per year. The proportion could be based on the last invoice received from DCC as these are sent monthly. The vote could be administered by SEC Panel or the future Code Manager.

Interim changes to governance (Chapter 5)

14. Do you agree with the identified priority areas of interim changes? Are there other governance changes that should be implemented in the Licence extension period?

Yes.

15. What are your views on the possible retention of current Sufficiently Independent Directors on the Board of DCC2? What provisions may need to apply to facilitate this?

This seems sensible if the SIDs are performing their duties well and the new licensee is agreeable, perhaps Ofgem should review on Licence handover in case of disagreement.

CRS questions (Chapter 6)

16. Do you agree with our proposal that it would be appropriate to remove provision of the Centralised Registration Service (CRS) from the DCC Licence and transfer the obligation to the Retail Energy Code (REC) to be delivered by RECCo?

Yes, we agree with the transfer of Central Registration Service (switching service) to RECCo. DCC should therefore not be a signatory to REC, nor a provider of services.

We hope the transfer improves DCC's services for smart metering and enables a significant cost saving from RECCo taking over. Whilst we understand that cost savings are not guaranteed, intuitively having less duplicated effort reviewing the same Service Providers' contracts and performance should mean end consumers see improved value for money from the Central Switching Service. We also hope that the reduced duplication will speed up resolution of outages and issues, whilst improving communication to Service Users.

Currently we have no view on how long the separation of services and the transfer of obligations will take, a project plan and key success criteria would be useful to understand, we will support RECCo with its transition plan.

17. What are your views on the considerations we have identified under option 1?

Please see answer to question 16.