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for energy consumers

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Dear Michael,

Ofgem response to the request for an extension to the Implementation Date of Balancing and Settlement Code Modification P272: Mandatory Half-Hourly Settlement for Profile Classes 5-8

On 20 March 2015, Elexon wrote to us on behalf of the BSC Panel to request, in accordance with Section F, Paragraph 2.11.8, that we approve a delay to the implementation of BSC Modification P272 by 12 months. This letter sets out our response to this request.

P272 mandates that consumers in Profile Classes (PCs) 5-8 with advanced meters are settled half-hourly (HH) from 1 April 2016. Ofgem, the Government[1] and the Competition and Markets Authority[2] have all recognised the importance of HH settlement in improving the functioning of the retail market. As we have previously set out, we are disappointed with the pace of the industry's preparations to date for the move to HH settlement.[3]

While we share some of the concerns raised by the BSC Panel regarding the risks to consumers associated with the current Implementation Date as described below, **we have decided not to approve its extension request**. We are concerned that, on its own, an extension to the deadline will not address these risks. It could also reduce the incentives on suppliers to start moving their PCs 5-8 customers to HH settlement as soon as possible.

We would be open to consideration of alternative solutions to address the risks to consumers. One example is introducing a mandatory start date for migration alongside a later Implementation Date for P272. Any solution could also consider a reporting requirement to monitor transition.

We encourage the industry to take steps to consider whether a more robust solution is available that fully addresses the risks to consumers by changing how all sites in PCs 5-8 with advanced meters are moved to HH settlement under P272, and bring forward any modification proposals necessary.

[1] Department of Energy and Climate Change, 2015. *DECC's Response to the Competition and Markets Authority's Updated Issues Statement.*
[2] Competition and Markets Authority, 2015. *Energy market Investigation: Updated Issues Statement.*
[3] Please see our open letter on the industry's role in creating the market conditions necessary to support the realisation of the benefits of smart metering, which is available on our website: https://www.ofgem.gov.uk/ofgem-publications/85909/letteronindustryroleinsupportingdelivertofsmartmeteringbenefits.pdf

BSC Modification P272

Ofgem approved P272 on 29 October 2014.[4] We consider it is in consumers' interests to be settled using their HH consumption data. In particular, it will strengthen competitive pressure on suppliers by putting in place stronger incentives on them to encourage demand-side response among their customers. Where consumers respond to price signals, this can lower bills, promote a more sustainable energy system and help maintain security of supply.

Significant time has passed since P272 was raised and it is not due to be implemented for nearly another year. We have previously written to stakeholders to highlight the important role that the industry has in creating the conditions necessary to realise the benefits of smart and advanced metering. In particular, by implementing necessary modifications to the BSC and other industry codes in a timely way.

BSC Panel's request for delay

The BSC Panel requested that the Implementation Date for P272 be moved from 1 April 2016 to 1 April 2017. This was because of two concerns that the BSC Panel considered material:

- The risk to customers and settlement accuracy from moving a large number of sites to HH settlement after the implementation of BSC Modification P300 on 5 November 2015.[5] The BSC Panel considered that the process for moving sites to HH settlement was not designed to accommodate the volumes that suppliers are expected to migrate after this date.
- The likely interruption of supply contracts where a consumer is moved to HH settlement and has a contract that extends beyond 1 April 2016. The BSC Panel noted suppliers' view that a better customer experience would be achieved if migration to HH settlement happens at contract expiry.

The BSC Panel also said that there are a large number of consequential industry changes being progressed to support implementation of P272. Some members of the BSC Panel had concerns that the outcome of some of these changes was uncertain.

The BSC Panel commented that the concerns it identified were widespread. It highlighted that a large number of suppliers, including all larger suppliers, supported an extension. The BSC Panel also noted that an extension to the implementation date should not stop suppliers from moving their customers to HH settlement sooner.

Ofgem's response

We have considered carefully the points raised in the BSC Panel's letter and in responses to its consultation on the extension. We have also met bilaterally with a number of stakeholders at their request. Below we set out our views on the concerns raised by the BSC Panel. We assessed these concerns against all relevant factors in reaching our decision. This includes the criteria that we said were particularly relevant in order to justify any delay. As advised at the BSC Panel meeting on 12 February 2015, this is that the concerns raised are: material; unable to be resolved within existing timescales; and industry wide.

[4] More information about our decision can be found on our website: https://www.ofgem.gov.uk/publications-and-updates/balancing-and-settlement-code-bsc-p272-mandatory-half-hourly-settlement-profile-classes-5-8

[5] A modification to the Distribution Connection and Use of System Agreement (DCUSA), called DCUSA Change Proposal 179, has recently introduced new distribution charging tariffs for HH sites. P300 enables some of these new tariffs to be used.

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Risks to consumers and settlement from moving the large majority of sites to HH settlement from November 2015

When we approved P272 for implementation on 1 April 2016, we assessed concerns raised by some stakeholders that this did not give sufficient time to transfer all sites to HH settlement. We said that we would not expect sites with whole current meters, which account for around 55 percent of those in PCs 5-8, to be transitioned to HH settlement until P300 is implemented on 5 November 2015. However, we noted that suppliers would be able to move sites with current-transformer (CT) meters from 1 April 2015. Taking this and other factors into account, including improvements to the Change of Measurement Class (CoMC) process that is used to transfer sites from non-half-hourly to HH settlement, we concluded that implementing P272 on 1 April 2016 gave sufficient time to migrate all PCs 5-8 sites to HH settlement in an orderly way.

However, from the evidence we have subsequently seen, it seems likely that the large majority of consumers in PCs 5-8 will be migrated to HH settlement from 5 November 2015. The evidence we have at this time includes migration plans submitted by some suppliers to the Performance Assurance Board (PAB).

Suppliers have put forward a variety of reasons for this. One important factor is that their systems and processes, and in some cases those of their Supplier Agents, are not ready at this time to start moving CT-metered sites to HH settlement. While we recognise that P272 has a significant impact on suppliers, they have had significant forewarning in order to make the necessary preparations. We are disappointed given we approved P272 nearly six months ago and it has been more than a year since we set out our view that the modification facilitated the BSC Objectives and was consistent with our statutory duties, so therefore likely to be implemented.

We are concerned that moving the majority of sites to HH settlement in less than five months increases the risk of errors occurring during the CoMC process. That process has never been tested at that scale. We consider that this risk is material because errors during the CoMC process may have an impact on consumers by causing delays to, or inaccurate, billing. We have seen significant detriment to consumers from late or inaccurate bills in the past as a result of major changes that suppliers have made to their IT systems. Errors during the CoMC process may also lead to inaccuracy in settlement, to the detriment of effective market functioning. We note that the PAB, as the body responsible for BSC performance assurance, has said to Ofgem that existing migration plans present a significant risk to settlement.

The risk of errors arising during the CoMC process can be considered industry-wide. This is because all suppliers will be affected by inaccurate settlement. Moreover, it is unlikely that the risk of errors can be mitigated effectively within current timescales given most suppliers' current readiness. We note that, of 13 suppliers that responded to the BSC Panel's consultation on an extension to the Implementation Date, more than half said they were unable to implement P272 by 1 April 2016 and a further two expressed serious concerns. These suppliers supply nearly all sites in PCs 5-8.

Risk to consumers from contract interruption

By improving the accuracy of settlement, P272 will change the costs that a supplier incurs to supply its customers in PCs 5-8. Therefore, on moving a customer to HH settlement, the supplier may wish to change the contract it holds with that customer. Making the prices paid by consumers more cost-reflective is central to realising the system-wide benefits of HH settlement.

However, contract interruption could lead to negative outcomes for some consumers. If the supplier raises the price of energy mid-contract, in some circumstances we understand that the consumer cannot exit the contract or must pay a charge to do so. As a result, the consumer may be unable to shop around for a deal that best suits their needs. In addition to increasing bills unexpectedly for some consumers, this could undermine consumer

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confidence and engagement in the longer term, and affect attitudes towards smart and advanced metering among consumers more widely. Such engagement will be critical to ensuring there is competitive pressure on suppliers to develop new tariff offerings and other services to help consumers better manage their energy consumption, thereby delivering demand-side response benefits.

We considered the risk of contract interruption in approving P272. Based on our understanding of the typical length of contracts with business consumers, we thought that a minority of supply contracts were at risk of interruption. Where suppliers did choose to interrupt contracts, we considered that there was sufficient time to engage affected customers, enabling them to manage their energy budget effectively.

However, based on new evidence provided by some suppliers, we are concerned that more contracts than we estimated are at risk of interruption. This is partly because some suppliers have continued to sign NHH contracts of more than one year since we approved P272. Given the risk of negative outcomes that could come from contract interruption, we consider that this would constitute a material concern if large numbers of consumers were affected. We note also that suppliers could avoid interruptions by absorbing any changes in cost, although this may be less feasible for smaller suppliers.

Other concerns

We note the view of some BSC Panel members that there is uncertainty about some changes to industry codes that are linked to P272. We are not convinced that this justifies a delay to implementation. Many changes necessary to support implementation of P272 have been approved and are due to be implemented shortly. Moreover, we consider that suppliers are able to manage any remaining uncertainty. This is business-as-usual given that frequent industry-led changes to the industry codes are a feature of the gas and electricity sectors.

More than half of suppliers expressed concerns regarding transmission and/or distribution charging arrangements. The concern regarding transmission charging has been resolved with the approval of Connection and Use of System Code Modification Proposal (CMP) 241.[6] On distribution charging, suppliers said they were waiting on Distribution Network Operators (DNOs) to confirm Maximum Import Capacity (MIC) for each CT-metered site. The industry had the opportunity to prioritise this work sooner and should have done so. We understand that DNOs and suppliers are now working together to put in place a robust process for identifying MICs. In the meantime, some suppliers have told us that it is possible to access maximum demand information from advanced meters, which we consider may give a reasonable initial view of MICs for the purposes of talking to consumers about how moving to HH settlement could affect their bills.

Next steps

Our primary concern is to mitigate the risks to consumers from implementing P272. While we are concerned about the risks to consumers from a large-scale migration taking place over a few months and from widespread contract interruptions, we do not think that granting an extension will address them. In particular, we note that suppliers could continue to place consumers on NHH contracts until the last possible moment. We are therefore not approving the BSC Panel's request for a 12 month extension to the Implementation Date.

We consider that other measures, potentially including, but not limited to, an extension to the Implementation Date, are needed to fully mitigate the risks identified. The industry has tools at its disposal to deliver a comprehensive solution that addresses these risks by

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[6] Suppliers were concerned that moving customers during the charging year would result in overcharging for use of the transmission network to supply consumers in PCs 5-8. CMP241 prevents this from happening. Further information can be found on our website: https://www.ofgem.gov.uk/publications-and-updates/connection-and-use-system-code-cusc-cmp241-tnuos-demand-charges-during-implementation-p272

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changing how the migration of all sites in PCs 5-8 to HH settlement under P272 is implemented. This includes raising a modification to the BSC that, by changing how P272 is implemented, would enable it to better realise the BSC Objectives. Any such modification should be raised and progressed quickly to minimise uncertainty.

To ensure that consumers' interests are protected, at this time we consider that the industry should consider:

- The importance of maintaining momentum, i.e. starting the migration as soon as possible to mitigate the risks of large-scale migration in short timescales.

- The best approach for delivering a positive outcome for consumers by minimising contract interruption.

- The way in which any new approach would interact with other changes to industry codes, particularly those that facilitate implementation of P272 including CMP241.

For the avoidance of doubt, in the absence of any new modifications being raised, the requirement on suppliers to implement P272 by 1 April 2016 remains. This underlines the importance of the industry acting quickly to bring forward modifications that fully address the risks to consumers from implementing P272 by this date.

In addition, we encourage suppliers to take steps now to communicate to their customers in PCs 5-8 how they will affected by P272. This includes providing information on how their bills may change and the actions they can take to mitigate this including through energy efficiency measures or demand-side response. It is important that suppliers do this in a timely way to give consumers the opportunity to plan ahead. We will also be publishing a factsheet for consumers to complement these efforts.

If you have any comments or questions about this letter, please contact Jonathan Amos at smartermarkets@ofgem.gov.uk.

Yours sincerely

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cc: Adam Lattimore, Elexon

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