Scottish and Southern Energy Power Distribution Limited

Report of Compliance Officer
for the year to 31 March 2017
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Duties of Compliance Officer
1. Introduction

Condition 42 of the electricity distribution licences of Southern Electric Power Distribution plc ("SEPD") and Scottish Hydro Electric Power Distribution plc ("SHEPD") and Special Conditions 2B and 2I of the electricity transmission licence of Scottish Hydro Electric Transmission plc ("SHE Transmission") require that distribution and transmission are managed in such a way that they do not restrict, prevent or distort competition elsewhere in the energy industry and the absolute confidentiality of related, commercially sensitive information is maintained. Other conditions of the licences prohibit cross subsidisation between separate businesses and discrimination between suppliers by the distribution business, in addition to a financial ring fence. SEPD, SHEPD and SHE Transmission are managerially and operationally run under the governance of their parent, Scottish and Southern Energy Power Distribution Limited "SSEPD".

SSEPD have agreed with The Gas and Electricity Markets Authority ("the Authority") and published their Statement of Compliance which sets out how SSEPD comply with the licence requirements specifically on the restriction on use of certain information and independence of the distribution and transmission businesses.

Condition 43 of SEPD's and SHEPD's licences and Transmission Special Licence Condition 2H require SSEPD to appoint a Compliance Officer to facilitate compliance with the licence restrictions on use of certain information and the independence of the distribution business within SSE plc.

Henderson Loggie, Chartered Accountants, is the Compliance Officer appointed by SSEPD. On behalf of Henderson Loggie, the Compliance Officer role is led by George Hay (partner) and Gavin Black (partner). The licences require we report annually to the Directors on our activities over each year to 31 March, and that the Licensee reports thereafter to the Authority on the Compliance Officer's activities and other relevant issues.

The specific duties of the Compliance Officer are attached but principally we are responsible for supporting SSEPD in its compliance with the separation licence conditions. This includes providing advice to SSEPD on complying with the confidentiality and separation obligations placed on the distribution and transmission businesses, monitoring the effectiveness of the practices, procedures and systems adopted by SSEPD, investigating complaints and reporting annually to the SSEPD Board. We are also required to liaise with the Authority on all of these matters as appropriate.
2. Overall approach

During our period of appointment as Compliance Officer, we have developed a Compliance Audit Programme ("CAP") which details the monitoring and testing we consider necessary to ensure systems, procedures and controls are dealing efficiently and effectively with separation as required by Conditions 42 & 43 (Distribution) and Special Licence Conditions 2B, 2H and 2I (Transmission) together with SSEPD's Statement of Compliance as agreed by the Authority.

Our main contacts throughout the year at SSE have been the SSEPD Board and senior managers including Colin Nicol (MD, Networks), Bev Keogh (Director of Networks Business Assurance), John Squire (Director of Group Compliance) and Beverley Grubb (Regulation). In particular, we again had quarterly update and review meetings with the Networks Compliance team led by Scott Johnston who continued to act as Internal Business Separation Compliance Officer (BSCO) for the Networks business. Networks Compliance is part of SSE's Group Compliance, a Corporate function, which is independent of the Networks business. We again visited a selection of sites of the distribution and transmission businesses where we have undertaken interviews and reviews. During the year sites visited included Perth, Aberdeen, Salisbury, New Forest, Basingstoke and Portsmouth (Walton Park), some of which were carried out in tandem with Compliance Team reviews.

Wherever appropriate we have utilised SSEPD and SSE resource, including the Networks Business Assurance and Compliance teams, as part of our review, with our role in such circumstances being to review the work undertaken, the results and conclusions reached and any remedial action taken. During this year the Networks Compliance team continued to develop its activities which created an increased level of control within the business compared to prior years which together with an increased level of activity within the Networks Business Assurance team this has allowed a more detailed level of monitoring of processes and controls. In addition, steps have been taken to reallocate more responsibility for Compliance to the Business Assurance team so that Networks Compliance can carry out more of a monitoring and advisory role in respect of business separation matters.

During the year two specific compliance reviews relative to Business Separation were carried out by the Networks Compliance Team on which we placed reliance.

These were “Review of Business Separation Controls Relating to IT Systems and Premises Access in Distribution and Transmission Networks” and “Review of Business Separation Arrangements between Networks and other companies within the SSE Group”.

Other monitoring and review was undertaken directly by us including communication with operational and administration managers and staff to discuss issues arising from separation, focusing on areas such as staff training, branding, physical separation and access, IT, data confidentiality and managerial separation.

Our approach focuses on the Statement of Compliance issued by SSEPD and the objectives set out in the relevant licence conditions. We visit a selection of SSEPD operational sites and look at the scope and results of the work undertaken by the Networks Compliance and Business Assurance teams. We also hold discussions with SSE Regulation department and review the Ofgem website to identify particular areas of risk or other areas we should specifically consider in the current year.

This year, we again considered the risks associated with the increased transmission activity, as well as new connections (in distribution and transmission), HR, physical access, cross subsidies and staff transfers.
2. Overall approach (Cont’d)

In addition, we discussed the outcome of the investigation into SSEPD’s Connections business in certain parts of England with Regulation and Management to determine whether there were any business separation issues arising but none were specifically identified to us.

We have not been required to meet with Ofgem this year and have not been contacted by them.

Our report is structured in line with SSEPD’s Statement of Compliance. It sets out the results of our review and our assessment of SSEPD’s compliance with the terms of that Statement and accordingly the relevant licence conditions.

3. Managerial and operational independence of SSEPD

We consider there are several distinct facets which are important in achieving managerial and operational separation as required by the licences and Ofgem. These include legal and physical separation, autonomous boards with autonomous decision making processes, appropriate contractual and service level agreements, data confidentiality and branding of the separated businesses.

The practical aspects such as the creation of separate legal entities, physical access restrictions and branding have been specifically verified. We also spoke with staff and managers across the business to confirm processes and procedures were being followed. Our work has continued to again confirm that the culture throughout the organisation relating to separation remains robust and has increased as a result of the continuing emphasis on all compliance issues throughout the Networks business and the group generally. A new group wide project called “i-Comply” was introduced during the year and we reviewed how Business Separation obligations were dealt with within this new framework.

We monitor the effectiveness of strategic data confidentiality, autonomy of decision making of the distribution and transmission businesses and corporate governance issues. This involved reviewing relevant board minutes and considering the operation of the decision making process with directors and officers. The make up of the board of SSEPD and the regular board meetings help ensure appropriate governance is maintained and reinforce SSE’s recognition of separation. The board composition has been reviewed and strengthened over recent years with the appointment of senior distribution and regulation personnel to complement the SSE plc director and SSE Executive Committee members, as well as the required involvement of independent non-executive directors.

In addition, the board’s terms of reference and the capital authorisation corporate policy are regularly reviewed to maintain the independence of SSEPD and reinforce the corporate governance procedures.

During the year the corporate governance framework was amended by the creation of a Networks Management Committee and we have concluded that this does not detract from the operation of the SSEPD Board and all appropriate matters are still considered and dealt with by the board.
3. Managerial and operational independence of SSEPD (cont'd)

Whilst absolute separation would not be consistent with SSE's shareholder and stewardship responsibilities, systems, procedures and structures have been implemented and continue to operate to ensure the key objectives of separation have been met. In particular, the group structure has allowed effective managerial and operational independence within the group's strategic plan. Underpinning this is a philosophy whereby access to information and data is prevented where separation requires it and we consider its implementation has been robust and thorough. Where systems enhancement or development is undertaken, separation issues will be considered. There are occasions where small numbers of non-Networks staff will have access to certain parts of Networks systems as necessary for the performance of their duties, mainly in relation to the provision of services for the Networks business. In such circumstances, we found effective procedures and systems to be in place to consider the business separation risks and ensure these are mitigated.

The ongoing training of staff on confidentiality and the seriousness with which SSEPD and SSE would regard any breaches continues to ensure the underlying philosophy and approach adopted by SSE in this area is maintained. A new e-learning package was introduced last year, completion of which is mandatory for all relevant personnel who have been specifically identified. This training was completely revamped during the course of the year using a more user friendly and more focused approach depending on specific roles performed by different individuals. This was rolled out from October 2016 with all relevant personnel having completed the training by 31 March 2017. Monitoring and control systems to ensure completeness of personnel trained were also improved during the year. Incorporating the revamped training into the current induction training pack is currently being carried out. SSE places particular emphasis on confidentiality clauses in staff appointment letters and regularly reinforces the importance of confidentiality and clearly sets out the disciplinary process which would follow any breach. There have been no disciplinary proceedings during the year under separation, confidentiality or competition conditions of employment.

Where staff transfers took place in the year, where it was necessary to consider any separation implications, processes were formalised during the year and actioned to ensure that steps were taken to ensure that any risks were mitigated with individuals being briefed and signing specifically drafted documentation to confirm their awareness of their obligations under the licence. The procedures in place whereby any significant transfers would be discussed with us are still effective.

4. Common services

We have considered the service level agreements ("SLAs") in place and discussed their operation in practice with no issues being identified.

A specific review of this area was carried out by the Compliance Team during the year as mentioned in Section 2 and this review did not identify any material issues or control weaknesses which were likely to result in a failure to meet a business separation obligations.

In addition, the cross subsidy report and Regulatory accounts audited by KPMG LLP have not raised any material concerns from Ofgem.

This would imply the SLAs and operating structure are not anti-competitive.
5. Customer system and confidential information

Previously particular focus has been given to the integrated Customer Services ("CS") system and the related staff induction and training programmes and we have concluded that SSEPD’s approach was in line with their stated and accepted philosophy. During the year the Networks Business completed the development and full implementation of new billing systems which are now independent from the rest of the SSE Group. This has now removed the SSEPD’s operational need to use the CS system. This year our audit work included:

- confirming systems, processes and procedures are still appropriate;
- reviewing the Networks Compliance team’s internal review work on the IT security profiles and access controls and resultant follow up action plans.

We confirmed the Networks Compliance function continues to allocate significant resource to this area, each year undertaking a specific review of business separation access controls and with a standing remit to consider separation issues as part of all compliance review assignments.

During the year, the Networks Compliance team have followed up the previous year’s report and quarterly meetings have been held with the Networks Compliance and Business Assurance teams to review progress against the previous year’s Action Points, all of which were completed. In addition the Networks Compliance team have carried out additional reviews with a view to reducing the risk of any issues arising in these areas.

This year their work identified a reduced incidence of various minor administrative issues relating to inappropriate access authority for staff. Whilst such minor issues increase the risk of non-compliance, we do not consider they gave rise to any actual problems and the points raised are being acted upon timeously.

We plan to continue to meet quarterly with the Networks Compliance and Business Assurance teams to ensure the improvements in monitoring controls that have been applied this year are continued in 2017/18.

SSEPD has procedures in place to ensure access to information specifically designated as confidential is restricted at all times. From our work we are satisfied that SSEPD continues to comply with its stated Business Separation policy and to implement and enforce rigorously procedures and controls commensurate with that policy.

An issues log is now maintained and we are satisfied that none of the issues identified has resulted in any actual specific business separation problems.
6. Branding

SSEPD's stated policy is to maintain a separate identity from other parts of SSE plc. Branding continues to be effective and is reinforced in the market place through the correct branding of vehicles, sites, literature and adverts, and stationery.

We are satisfied that branding is in keeping with the group policy and consistent with the need to separately brand the power transmission and distribution businesses within the market place.

During the year to 31 March 2016 the branding of the Networks business was reviewed and significant changes were introduced during 2016/17. We were consulted at various times during the previous year about these changes and are comfortable that the changes to branding are perfectly acceptable from a Business Separation perspective and have, in fact, strengthened the distinction between the Networks business and the rest of the SSE group.

7. Responsibility

Separate legal entities for the operating subsidiaries create an appropriate structure for separation to be effective. The formal procedure of regular SSEPD board meetings underpins this and we consider these to be fundamental to achieving effective separation. The composition of the board was previously strengthened to reflect in particular, the growth in transmission and comprises 5 executive directors together with three Group non-executive directors (one of which is Chairman) recognising the importance of SSEPD board responsibilities, together with two independent directors following the introduction of this requirement in April 2014. The creation of the Networks Management Committee during the year has not detracted from the role of the SSEPD board and has allowed it to focus on the most important areas of it's responsibility.

This board has clearly defined terms of reference and a remit which allows SSE Group to continue to meet its corporate objectives whilst satisfying the Licence requirements. In addition, the corporate governance policy has been approved by the PLC board which recognises the role of the SSEPD board and empowers it with prime responsibility for protecting the independence and confidentiality of commercially sensitive information. In this regard, we note that the Capital Authorisation Corporate Policy continues to partially exempt SSEPD from the group's capital expenditure approval procedure to ensure confidential information is not made available to inappropriate executives or staff.

During the year, SSE Group has implemented an i-Comply portal, which houses key regulatory and legislative obligations for all its businesses, with detailed rules being assigned to business owners. This provides a holistic view of the regulatory regime and ensures that it is centrally maintained, regularly updated and that ownership for compliance is clearly assigned. A designated group has been assigned to maintain the accuracy of the regulatory content.

As an independent, external compliance officer, our approach brings an objective review of the practices, procedures and systems in place or planned to help ensure the conditions of the licences and the Statement of Compliance are being achieved.
8. Complaints

We have established a procedure with SSE's Regulation and Compliance Teams whereby any complaints received relating to separation will be advised to us with a covering letter setting out the investigation work to be undertaken by SSEPD. We will review details of SSEPD's response to the complainant and any remedial action taken or proposed and we will consider if we should undertake our own investigation. Whilst there can be no guarantee that every relevant complaint would be dealt with by the Regulation or Compliance teams, we are satisfied all those with substance would be notified to them.

We have received confirmation that there have not been any complaints of a Business Separation nature notified to the Regulation or Compliance teams this year.

9. Advisory role

Our remit as Compliance Officer includes providing input on separation issues to help ensure policies and procedures are consistent with the Statement of Compliance and meet the expectations of Ofgem where practicable.

Meetings with Regulation and Compliance staff and SSEPD directors allow relevant issues to be aired and addressed on a timely basis.

10. The year ahead

The appropriate practices, procedures and systems in SSEPD's Statement of Compliance have been fully implemented for many years. Accordingly, our ongoing role continues to be to monitor compliance, in association with the Group Audit, Networks Compliance, Business Assurance and Regulation teams, with the relevant systems and procedures in light of the licence conditions, independently assess SSEPD's compliance taking account of any developments in the group's business and to advise on any relevant issues which arise.

Henderson Loggie
26 May 2017
Attachment 1 - Duties of Compliance Officer

1.1 The duties and tasks assigned to the Compliance Officer shall include:

   a) providing relevant advice and information to the Licensee for the purpose of ensuring its compliance with the Relevant Duties/Requirements;

   b) monitoring the effectiveness of the practices, procedures and systems adopted by the Licensee in accordance with the statement referred to in Condition 42 of the Distribution licences and Special Condition 2H of the Transmission Licence;

   c) advising whether, to the extent that the implementation of such practices, procedures and systems requires the co-operation of any other person, they are designed so as reasonably to admit the required co-operation;

   d) investigating any complaint or representation made available to him;

   e) recommending and advising upon the remedial action which any such investigation has demonstrated to be necessary or desirable;

   f) providing relevant advice and information to the Licensee for the purpose of ensuring its effective implementation of:

      i) the practices, procedures and systems adopted in accordance with the statement referred to above; and

      ii) any remedial action recommended in accordance with sub-paragraph (d); and

   g) reporting annually to the directors of the Licensee – in respect of the year ending 31 March 2003 and of each subsequent year – as to his activities during the period covered by the report, including the fulfilment of the other duties and tasks assigned to him by the Licensee.

1.2 As soon as is reasonably practicable following each annual report of the Compliance Officer, the Licensee shall produce a report:

   a) as to its compliance during the relevant year with the Relevant Duties/Requirements; and

   b) as to its implementation of the practices, procedures and systems adopted in accordance with the statement referred to above.
1.3 The report produced in accordance with paragraph 1.2 shall in particular:

a) detail the activities of the Compliance Officer during the relevant year;

b) refer to such other matters as are or may be appropriate in relation to the implementation of the practices, procedures and systems adopted in accordance with the statement referred to above; and

c) set out the details of any investigations conducted by the Compliance Officer, including:

i) the number, type and source of the complaints or representations on which such investigations were based;

ii) the outcome of such investigations; and

iii) any remedial action taken by the Licensee following such investigations.