Scottish and Southern Energy Power Distribution Limited

Report of the Compliance Officer for the year to 31 March 2018
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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 ("Networks") business.

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 Networks 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 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 included in the appendix to this report 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 Networks business, 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), Scott Johnston (Networks Compliance and Internal Business Separation Compliance Officer (BSCO)), John Balfour (Head of Networks Business Assurance) and Beverley Grubb (Networks Regulation Manager). We hold quarterly update and review meetings with the Networks Business Assurance led by John Balfour and the Networks Compliance team led by Scott Johnston. Networks Business Assurance sits within the Networks business and is the principal function used by the business to ensure compliance with the business separation licence obligations. 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 Networks sites where we have undertaken interviews and reviews. During the year sites visited included Perth, Arbroath, Reading, West London and Slough, most of which were carried out in tandem with the Business Assurance and Compliance teams.

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, a significant amount of work has been undertaken by the Networks Business Assurance team to consolidate and enhance existing processes, controls and reference materials. This has not only strengthened the processes, procedures and monitoring activities within the business but has also allowed Networks Compliance to act in an independent monitoring and advisory role in respect of business separation matters.

During the year, the Networks Compliance team has also undertaken a detailed review of Networks Business Separation on which we have placed reliance. This year the work undertaken by Networks Compliance identified a few observations and one recommendation which have all been discussed and agreed with the business risk owners. 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.

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 Business Assurance and Networks Compliance 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.
2. Overall approach (Cont’d)

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.

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

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 again confirmed 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. Like all regulatory obligations, business separation requirements are housed within the group wide i-Comply system.

We monitor the effectiveness of strategic data confidentiality, autonomy of decision making of the Networks business and corporate governance issues. This involved reviewing relevant board and committee minutes and considering the operation of the decision making process with directors and officers. The composition 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 has a strong mix of executive and non-executive members, including 2 independent non-executive directors, and are supported further by experienced senior Networks, legal and regulation personnel. 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.

The SSEPD Board is supported by the Networks Management Committee. Membership of this Committee includes SSEPD directors and senior management from across the networks business.

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.
3. Managerial and operational independence of SSEPD (cont’d)

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. An updated e-learning package was introduced this year, completion of which is mandatory for those who have been specifically identified. This was rolled out in December 2017 with relevant Networks and Corporate personnel targeted to complete the training by 31 March 2018. This also forms part of the induction and training programme for new starters. Controls are in place to ensure that training is completed and action is taken, such as IT and physical access restrictions, where training has not been undertaken within the required timescales.

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 and potential business separation implications were identified, processes were followed 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.

A specific review of this area was carried out by the Compliance Team during the previous year. No material issues or control weaknesses which were likely to result in a failure to meet business separation obligations were identified.

In addition, Group Procurement are currently reviewing the SLAs in place to ensure these are all still required and that they reflect the nature of the services being provided to or received from other areas of the business as well as confirming that they are fully compliant with all current procurement regulations. This review was not yet complete at the time of our report however no significant issues have been identified to date.

In addition, the cross subsidy reports prepared by KPMG and audited regulatory accounts have not raised any material concerns from Ofgem.

This supports the fact that the SLAs and operating structure are not anti-competitive.
5. Customer system and confidential information

During the previous year, the Networks Business completed the development and full implementation of a new billing system which is independent from the rest of the SSE Group. This has removed SSEPD’s operational need to use the group-wide integrated Customer Services system, and the associated training and access control measures.

We again considered 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 regular meetings have been held with the Networks Business Assurance team to review progress against the previous year’s action points.

We plan to continue to meet quarterly with the Networks Business Assurance and Networks Compliance teams to ensure the improvements in monitoring controls that have been applied this year continue in 2018/19.

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 maintained and we are satisfied that none of the issues identified has resulted in any 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 transmission and distribution businesses within the market place.

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 board 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 non-executive directors. The creation of the Networks Management Committee during the previous year has not detracted from the role of the SSEPD board and has allowed it to focus on the most important areas of its 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 executives or staff who should not have access to it.

The SSE Group maintains 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.

In addition, a dedicated Sharepoint site within the SSE intranet has been built by Networks Business Assurance during the year. This provides access to a vast array of business separation policies, procedures and guidance material as well as information regarding assurance and monitoring activities undertaken. It also provides a means for the business to raise queries on any potential business separation related matters that may arise from time to time.

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 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 material complaints 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, Assurance and Compliance staff and SSEPD directors allow relevant issues to be aired and addressed on a timely basis.

10. The year ahead

The practices, procedures and systems in SSEPD’s Statement of Compliance have been fully implemented for many years. Accordingly, our role continues to be a monitoring function, in conjunction with Networks Business Assurance, Networks Compliance and the Regulation team, to independently assess continued compliance with the licence conditions, taking account of any developments in the business and to advise on any relevant issues which arise.

Henderson Loggie
9 May 2018
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.