

<b>Paper Reference:</b>	SECP_34_0807_06
<b>Action:</b>	For Decision

## Code Governance Review Phase 3 Outcomes: Materiality Guidance

### 1. Purpose

Following the key requirements arising from the Code Governance Review Phase 3 (CGR3), this paper provides the Panel with some initial materiality guidance for consideration. The guidance relates to whether a SEC Modification Proposal would require Authority approval or can be progressed as self-governance.

### 2. CGR Phase 3 outcomes and materiality guidance

In May 2016 the Panel considered the key requirements arising from the CGR3 outcomes<sup>1</sup>. One of the key requirements was for Industry to assess whether a modification is material, and therefore requires the consent of the Authority, in deciding whether to use the self-governance route. The output of this key requirement is the development of materiality guidance.

At the June Panel meeting, in the CGR3 Final Proposal updates paper<sup>2</sup>, the Panel was updated on the progress of the key requirements following a cross Code Administrator meeting that took place on 3<sup>rd</sup> June 2016. It was noted that at the meeting it was agreed that each Code should determine a view of materiality in respect of their specific Code and Modification requirements. Wider self-governance guidance could then be produced incorporating the materiality guidance.

It was also noted in the June Panel update that the materiality guidance for SEC Modification Proposals would be prepared for consideration at the July Panel meeting.

### 3. Materiality and the SEC

#### 3.1 Existing Provisions

##### Modification Paths

Modification Proposals are progressed through the SEC Modification Process via one of four paths:

- **Path 1: Authority-Led** (modifications that originate from the Authority as either a matter arising from a Significant Code Review or taking action on a European Commission Direction, and require Authority determination at the end of the Modification Process);
- **Path 2: Authority Determination** (modifications raised by those able to do so, but have a material impact meaning and Authority determination is required);

<sup>1</sup> SECP32\_1305\_05

<sup>2</sup> SECP33\_1706\_14

- **Path 3: Self-Governance** (modifications that are not Path 1 or Path 2); and
- **Fast-Track Modifications** – (modifications raised by the Panel to primarily correct typographical, cross-referencing and/or definition errors).

### Path requirements

For a modification to progress as a Path 3 Self-Governance the nature of the change must mean it does not meet the criteria that would mean it is Path 1, Path 2 or Fast Track Modification.

As Path 1 (Authority-Led) Modification Proposals require Authority Determination effectively by default as they relate to matters previously overseen or led on by the Authority, the focus of any materiality guidance to encourage use of Path 3 (Self-Governance), is on Path 2 (Authority Determined) Modification Proposals.

SEC Section D2.6 sets out which type of modifications must be progressed as a Path 2 modification and are set out below:

- the variations are likely to have a material effect on existing or future Energy Consumers;*
- the variations are likely to have a material effect on competition in the Supply of Energy or Commercial Activities connected with the Supply of Energy;*
- the variations are likely to have a material effect on the environment, on access to or privacy of Data, on security of the Supply of Energy, and/or on the security of Systems and/or Smart Metering Systems;*
- the variations are likely to have a material effect on the arrangements set out in Section C (Governance) or this Section D; and/or*
- the variations are likely to unduly discriminate in their effects between one Party (or class of Parties) and another Party (or class of Parties).*

Section D2.2 sets out that the Panel's determination on the Path, each modification proceeds as is conclusive unless the Authority makes a determination to the contrary. For example a modification that the Panel determines should be progressed as Path 3, could be overturned by the Authority and change to a Path 2 Modification Proposal if it determined that the changes were material in nature and therefore require Authority determination.

### 3.2 Proposed Additional Guidance and materiality information

With the exception of Section D2.6(e) all the criteria for Path 2 modifications include 'material effect'. It was noted at the 3<sup>rd</sup> June 2016 cross Code Administration meeting that each industry code materiality requirements, on how a modification should proceed, are subtly different based on the nature of the code and the changes proposed to that code.

When considering the SEC provisions on the meaning of 'material effect' the following additional guidance, set out in Table 1, could be used. The guidance has been taken from the perspective of what is material, and therefore would require an Authority Determination, i.e. the modification cannot be Path 3.

SEC reference	Potential materiality guidance
<b>General materiality considerations</b>	<p>Modifications that impact the</p> <ul style="list-style-type: none"> <li>• Technical Specifications (Smart metering Equipment Technical Specifications (SMETS), Communications Hub Technical Specifications (CHTS) and GB Companion Specification (GBCS)) that then require EC Notification are material and therefore cannot be Path 3, as the Authority undertakes the EC Notification process;</li> <li>• Technical Specifications (but do not require EC Notification) but may impact meter manufactures and therefore the Suppliers procurement of metering equipment could be considered material and therefore not Self-governance.</li> </ul>
<b>Section D2.6(a) - Consumer Impacts</b>	<p>Modifications that alter the Energy consumer experience:</p> <ul style="list-style-type: none"> <li>• positively or negatively; or</li> <li>• could increase the costs to them</li> </ul> <p>would likely be considered as having a material effect.</p>
<b>Section D2.6(b) - Competition</b>	<p>Any Modification Proposal that could foreseeably result in an outcome that gave an advantage or disadvantage to a:</p> <ul style="list-style-type: none"> <li>• Party Category or group of Party Categories; or</li> <li>• system solutions over others</li> </ul> <p>would likely be considered as having a material effect.</p>
<b>Section D2.6(c) - Environment, Data Privacy, security of the Supply, and/or on the security of Systems and/or Smart Metering Systems</b>	<p>A change:</p> <ul style="list-style-type: none"> <li>• that will have a negative (or positive) impact on the <b>Environment</b>, such as increase transportation costs and therefore greenhouse emissions will likely be considered material;</li> <li>• to <b>Data Privacy</b> provisions would be considered material;</li> <li>• that could impact <b>Security</b> requirements or has an impact on security provisions or licence conditions would likely considered to be material. For example modifications that add or expand security requirements may require an Authority determination; and/or</li> <li>• to the <b>security of Smart Metering Systems</b> could be considered material if it increased or reduced existing provisions. An increase could also be seen to have an impact on competition as a reduction in Smart Metering System security could give rise to Smart Metering Systems becoming weaker and liable to attack.</li> </ul>
<b>Section D2.6(d) – Governance</b>	<p>Modifications that:</p> <ul style="list-style-type: none"> <li>• alter the governance responsibilities within Section C, that do not have an associated driver from government policy or arising from a Significant Code Review or Authority led piece of work (such as CGR3) would be considered material; or</li> <li>• change Section D that alter the Modification Process and how it operates or the roles and responsibilities of those involved</li> </ul>

SEC reference	Potential materiality guidance
	would likely be considered material. The exception being where a modification relates to something arising from the Authority, e.g. the CGR3 outcomes that prompted SECMP0017 to be raised.
<b>Section D2.6(e) – undue discrimination between one Party(s) or class of Party(s)</b>	While this clause does not include the words ‘material effect’, a change that would increase discrimination between Parties or class of Parties would need to be progressed as a Path 2 modification.  However a modification that could reduce discrimination could be progressed as a Path 3 modification until such point where the Authority indicated that it should be progressed as a Path 2.

**Table 1: Proposed materiality guidance**

### 3.3 Areas for further consideration

Notwithstanding the additional proposed materiality guidance in Table 1, there are areas that still require further thought and consideration, which may result in the materiality guidance being updated and expanded.

In light of the variety of modifications currently going through the Section D ‘Modification Process’, it may be prudent to review the SEC materiality guidance and expand as necessary once a number of the active Modification Proposals have completed the process. Insights gained will help the guidance expansion, as worked examples can be incorporated as a guide to the type of changes that have required an Authority determination, and similar types of changes will therefore likely be treated the same.

## 4. Next Steps

Any comments from the Panel will be added to the guidance and incorporated into the information included on the SEC website and in the Modification Proposal form. In addition SECAS will share current thinking on materiality guidance with other Code Administrators as part of the cross code working on the CGR3 key requirements.

## 5. Recommendations

The SEC Panel is requested to:

- **NOTE** the contents of this paper;
- **CONSIDER** the proposed initial materiality guidance;
- **AGREE** that SECAS should further develop the guidance and publish on the SEC Website and add to the Modification Proposal form

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1<sup>st</sup> July 2016