



Department
of Energy &
Climate Change

Smart Metering Implementation Programme

Government response: consultation on consequential changes to the DCC Licence to support provisions in the Smart Energy Code concerning financing of communications hubs

30 January 2014

General information

Purpose of this document:

This document concludes on a consultation to update the DCC licence so that it supports provisions in the Smart Energy Code around the financing of communications hubs.

Issued: 30 January 2014

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Territorial extent:

This consultation applies to the gas and electricity markets in Great Britain. Responsibility for energy markets in Northern Ireland lies with the Northern Ireland Executive's Department of Enterprise, Trade and Investment.

Additional copies:

You may make copies of this document without seeking permission. An electronic version can be found at <https://www.gov.uk/government/consultations/new-smart-energy-code-content-stage-2-consequential-consultation-on-changes-to-the-dcc-licence>.

Other versions of the document in Braille, large print or audio-cassette are available on request. This includes a Welsh version. Please contact us under the above details to request alternative versions.

Confidentiality and data protection:

DECC intends to summarise all responses and place this summary on our website at www.decc.gov.uk/en/content/cms/consultations/. This summary will include a list of names or organisations that responded but not people's names, addresses or other contact details. In addition DECC intends to publish the individual responses on its website and you should therefore let us know if you are not content for the response or any part of it to be published. We will not publish people's personal names, addresses or other contact details. If you indicate that you do not want your response published we will not publish it automatically but it could still be subject to information requests as detailed below.

Further, information provided in response to this consultation, including personal information, may be subject to publication or disclosure in accordance with the access to information legislation (primarily the Freedom of Information Act 2000, the Data Protection Act 1998 and the Environmental Information Regulations 2004).

If you do not want your individual response to be published on the website, or to otherwise be treated as confidential please say so clearly in writing when you send

your response to the consultation. For the purposes of considering access to information requests it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded by us as a confidentiality request.

Quality assurance:

This consultation has been carried out in accordance with the Government's guidance on consultation principles, which can be found here:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/60937/Consultation-Principles.pdf

If you have any complaints about the consultation process (as opposed to comments about the issues which are the subject of the consultation) please address them to:

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1 Summary

1. Smart Meters are the next generation of gas and electricity meters. They will offer a range of intelligent functions and provide consumers with more accurate information, bringing an end to estimated billing. Consumers will have near-real time information on their energy consumption to help them control and manage their energy use, save money and reduce emissions.
2. On 23 September 2013, a new licensed entity, the Data and Communications Company (DCC), was established. Together with its sub-contractors, the Data Service Provider (DSP) and Communications Service Providers (CSPs), the DCC will provide a Smart Meter communications service. The DCC will offer a means by which Suppliers, Network Operators and others can communicate remotely with Smart Meters in Great Britain.
3. The Smart Energy Code (SEC) is a new industry code which has been created through, and came into force under, the DCC Licence. The SEC is a multiparty contract which sets out the terms for the provision of the DCC's Smart Meter communications service, and specifies other provisions to govern the end-to-end management of Smart Metering.
4. In October 2013 we consulted¹ on the SEC drafting with respect to a range of issues ('the October consultation'). In December 2013² we published our conclusions on one specific aspect of that consultation, namely the proposed provisions in the SEC to support the charging arrangements for third party financing planned for the first tranche of communications hubs in the northern CSP region (5% of the total or approximately 1.4m communications hubs).
5. The December response document also included a further consultation ('the December consultation') concerning a number of proposed minor amendments to the DCC Licence, identified as a result of the October consultation as being necessary to complement the provisions within the SEC.
6. This document forms the Government response to the December consultation on the proposed amendments to the DCC Licence.
7. The sections below summarise responses received to the December consultation, and our response to those comments. Annex 1 contains the revised DCC Licence text. The final SEC text (with respect to the communications hubs financing provisions) is published separately in the Government Response to the Consultation on New Smart Energy Code Content (Stage 2)³. Both sets of text will now be laid before Parliament before taking effect (subject to Parliamentary approval) on or shortly before 31 March 2014 (other regulatory measures will be laid at the same time, to take effect in early April).

¹ Available at <https://www.gov.uk/government/consultations/new-smart-energy-code-content-stage-2>

² Also available at <https://www.gov.uk/government/consultations/new-smart-energy-code-content-stage-2>

³ Also available at <https://www.gov.uk/government/consultations/new-smart-energy-code-content-stage-2>

2 Response to December 2013 proposals

2.1 Proposals

8. The October consultation set out four proposed provisions in the SEC to support economical and efficient procurement of communications hubs. These were:
 - First Provision: to allow the DCC to invoice separately for communications hubs financing charges, and require service users to pay these charges into a separate ring-fenced bank account;
 - Second Provision: to permit the DCC to recover from service users all outstanding monies due on deployed communications hubs in the event of a default in payments;
 - Third Provision: to allow the DCC to budget prudently in setting its charges to ensure that there is sufficient working capital to avoid an inadvertent default, in practice achieved through a float covering the cost of three months' payments for the communications hubs concerned; and
 - Fourth Provision: to give financiers limited third party rights under the SEC to pursue outstanding sums direct from service users, but only in the circumstance that Ofgem determines that the DCC is unable or unwilling to do this.

9. In December we concluded that it was appropriate to introduce these provisions into the regulatory framework. However, following comments received in response to the October consultation regarding the first provision above we considered it necessary to make some minor consequential changes to the DCC Licence.
10. We explained that the changes were necessary to align the policy position, as set out in the October consultation and concluded upon in December, with the drafting of the DCC Licence. We said that we did not consider that the Licence changes would have any additional direct impact upon users.
11. The first proposed change was to Condition 11.12 (Part D: Management of External Service Provider Contracts) to allow for the flow of payments now envisaged.
12. The second proposed change made clear that payments for communications hubs financing from users are to be treated as regulated revenue under the Licence. As a consequence it was also necessary to allow the DCC to direct such payments into ring-fenced accounts that are held by the financiers (although the DCC will be responsible for determining the amount and frequency of charges).

13. To achieve this we proposed moving the DCC's existing obligation to ring-fence its income from its previous position in Schedule 5, Annex 1 and place it in Condition 27. We proposed further modifying Condition 27 to permit the payment of certain income (i.e. communications hubs financing charges) into accounts held by other parties.
14. We also added a change purely 'for the avoidance of any doubt' to the definition of Regulated Revenue in Condition 35 to make it clear that these payments fall within the definition of 'Regulated Revenue'. This ensures that any interest earned in these accounts is returned to the DCC at completion (i.e. when all communications hubs in a particular tranche have been delivered and paid for); if appropriate these sums would then be returned to users through the usual price control mechanism.

2.2 Summary of responses

Make up of respondents

15. We received seven responses to the consultation, from five energy suppliers, the DCC and Ofgem.

Comments

16. One supplier said that, although it still had reservations over the approach taken in the SEC drafting, it thought the opportunity to achieve lower cost financing arrangements should not be missed and so had no objections to the Licence drafting.
17. A second supplier reiterated the comment it had made in respect of the third provision in the SEC consultation, namely that it thought a one month float would be adequate (rather than a three month float) and that the three month proposal was therefore excessive. Otherwise it had no comments on the licence drafting other than recognising the need to align the Licence with the SEC provisions.
18. A third supplier said that it supported the proposed approach to align the Licence with the SEC provisions. It had a number of comments and requests for clarification on the drafting.
19. On the Licence drafting it asked, with respect to Condition 27.14 (c), how the 'reasonable rate of interest' is to be determined and whether it will be published. It also believed that the requirement that any payments in error (including any interest earned) should be returned promptly to the relevant SEC Party would only be workable if there is transparency regarding the rate of interest.
20. The third supplier also asked if the arrangements for future tranches of communications hub procurement, led by the DCC and subject to ex post review by Ofgem, would be set out in the SEC.

21. The fourth supplier said that it believed that the Licence drafting would allow the provisions in the SEC to be extended beyond the first tranche of 5% of communications hubs in the northern CSP region (these being the only ones for which third party finance is currently planned). It said it wanted assurance that DCC users would have the opportunity to fully engage with and comment on future communications hubs financing arrangements. It said that the drafting should be amended either to apply specifically to the first tranche of hubs or to introduce an appropriate 'sunset clause' that would force the industry to 'openly review these conditions at an appropriate future date'. It was concerned that the change to the definition of regulated revenue in Condition 35 could leave suppliers open to the third SEC Provision (in effect a three month float) for all communications hubs financing and not just those anticipated in the October consultation.
22. The same supplier also said that the consultation text drafting with respect to Condition 11.12(b) appeared to remove the obligation on CSPs to pass on revenues to relevant external parties and suggested that this drafting should be reinstated.
23. Its final comment was a concern that the Licence drafting combined with the SEC provisions potentially allowed the DCC to breach its Licence obligations if Ofgem had determined (under the fourth SEC provision discussed above) that the DCC had been unwilling or unable to pursue bad debt.
24. The fifth supplier had no comments on the Licence drafting, it reiterated a comment it made in response to the October consultation, about the potential implications of the transfer of liabilities between current CSPs and their successors, and the efficient alignment of replacement activity across communications hubs and its own smart meters. It noted that there was time to address these concerns, and looked forward to doing so with the rest of industry.
25. Ofgem suggested that the reference in Condition 11.12(b) to 'financing, procuring, providing or operating Communications Hubs' should be reduced to just 'financing' as the only intent of the provisions in the October consultation was to support the financing of communications hubs. It also suggested that consequential changes would then be necessary in Conditions 27 and 35.
26. Ofgem also noted that it was important that the original intent of Condition 11 was maintained and not altered by these amendments.
27. The DCC made a similar point with respect to Condition 11, noting that in the future there may be a financing arrangement that does not require direct payments from either the DCC or SEC Parties to financiers.
28. The DCC also made a number of minor drafting comments including a request, in the interests of economical administration, for less inflexible timing for payment of any interest that has accrued in the specified account, back to the DCC.

2.3 Government response

29. The Government agrees that the intent of the original drafting of Condition 11.12(b) should not be lost (as noted by an energy supplier, the DCC and Ofgem). We have achieved this by combining the original (pre-December consultation) drafting in Condition 11.12(b) with the Condition 11.12(a).
30. We have also addressed Ofgem's comment that the provisions that provide for payments from SEC Parties direct to third parties (and not the DCC) are with respect to the financing of communications hubs and not intended to be used more broadly. Condition 11.12(b) now makes this clear. For consistency similar changes are required in Condition 27.14C and to the definition of regulated revenue in Condition 35.
31. We note the response from one energy supplier that it continued to prefer a one month rather than three month float under the third SEC Provision. However, as we explained in our response to the consultation on the SEC provisions for this policy (see paragraphs 57-59 of the December consultation) we continue to consider that the additional cost to users in funding an extra two months float is significantly outweighed by the savings secured, that it would not be possible to secure these savings on the basis of a one month float, and that the proposal is proportionate.
32. In response to the supplier who asked how the 'reasonable' rate of interest will be determined in Condition 27, we note that the term 'reasonable' is used throughout the DCC Licence and is intended to direct the DCC to undertake a reasonable course of action in response to the set of circumstances that are relevant at the time. We do not consider that specifying a required level of interest into the Licence at this point is necessary or appropriate. We also note that ultimately it would be for Ofgem to assess whether the DCC had secured a reasonable rate of interest as it would with any other licence obligation.
33. In response to the same supplier's concern that, without transparency over the level of interest earned, it would be difficult to determine if the correct sums had been repaid to SEC Parties in the event of an mistaken overpayment by SEC Parties, we note that the Licence places obligations on the DCC to keep records of every financial transaction or financial event relating to the operation of the account referred to in Condition 27.14C. It must also make these records available to Ofgem upon request.
34. Following comments from the DCC on the timing of any interest payments back to SEC Parties, we have made a minor change to the Licence drafting to allow these to be made 'as soon as reasonably practical' rather than 'promptly'. This is because for very small amounts it may not be efficient or practical to immediately return such sums.
35. Two suppliers asked for clarity with respect to future procurement of communications hubs tranches. As we explained in the December response to the October consultation, we have concluded that the Licence changes and SEC provisions should be future-proofed to allow their use in further tranches *if appropriate*. It is important to note that it will be for the DCC to undertake the

most economical and efficient procurement to deliver its obligations under its Licence and the SEC, and that whatever approach it takes will be subject to ex-post review by Ofgem (with respect to whether it was economical and efficient). Furthermore the DCC is required under Condition 16 Part D of its Licence to consult its users on its approach to procurement. Ultimately Ofgem has the powers to make changes to the Licence, for example to support the efficient and economical procurement of future tranches, should it consider it necessary in light of the experience from this arrangement.

36. If, following this exercise, the DCC were to identify alternative arrangements that provide better value for money than further SEC modifications (and potentially Licence changes) could be required. If the same arrangements were used then we would not expect any significant changes to the regulatory framework.
37. In response to the fourth supplier's concern that the SEC provisions combined with the Licence changes allowed the DCC to 'breach its obligations', we do not consider that this is the case. This is because the fourth SEC provision (giving financiers limited third party rights to pursue debt directly with SEC Parties) does not 'excuse' the DCC from its obligations. Indeed, its use could only be triggered when Ofgem had determined that the DCC had not met its obligations to pursue sums owed. The DCC could still be in breach of its Licence or SEC obligations even if the fourth provision had been triggered.
38. With respect to the fourth supplier's concern that the definition of Regulated Revenue in Condition 35 could mean that suppliers were obliged to support all communications hubs financing with a three month float, we do not believe that this is the case. As set out in the December consultation the change to the definition was 'for the avoidance of doubt' to make it clear that any payments under the SEC from SEC Parties to defined third parties would be treated as regulated revenue. It does not extend the circumstances in which such payments can or must be made.
39. With respect to the fifth supplier's comments with regards to the need to efficiently align replacement activity for future communications hubs, we continue to consider – as set out in the December consultation - that this will be an important part of the DCC's role when it undertakes future procurement.

2.4 Next Steps

40. The DCC Licence modifications that we now intend to introduce are attached at Annex 1; those for the SEC can be found in the Government Response to the Consultation on New Smart Energy Code Content (Stage 2). They will now be laid before Parliament and, subject to Parliamentary approval, will come into force on or shortly before 31 March 2014.

Annex 1: Confirmed changes to DCC Licence conditions

Condition 11.12:

Replace Condition 11.12 with the following –

“The arrangements to which paragraph 11.11 refers must include such procedures or other matters as may be necessary to ensure that revenues flow either:

- (a) from the Licensee to the Relevant Provider for and in connection with the provision of Fundamental Service Capability to the Licensee; and then from the Relevant Provider to persons engaged (indirectly pursuant to the Relevant Contract) in the business of financing, procuring, providing, or operating Communications Hubs; or
- (b) from the Licensee (or, where the SEC so provides, from SEC Parties) to persons (other than the Relevant Provider) engaged (indirectly pursuant to the Relevant Contract) in the business of financing Communications Hubs,

in such manner, at such times, and to such extent as will ensure that:

- (i) the Relevant Provider is able to fulfil its obligations under the Relevant Contract; and
- (ii) the Licensee is able to be provided with the goods, services, and resources necessary to enable it to fulfil its obligations under this Licence.”

Condition 27

In Condition 27, add new paragraphs 27.14A, 27.14B, 27.14C and 27.14D (in a new part F1) as follows –

“Part F1: Ring-fencing of the Licensee’s revenues

27.14A Subject to paragraph 27.14C, the Licensee must ensure that all revenues that:

- (a) accrue to the Licensee from Service Charges levied in accordance with the provisions of Condition 18 (Charging Methodology for Services) and of Condition 19 (Charging Statement for Services); or
- (b) are otherwise received by the Licensee in relation to the carrying on of the Authorised Business of the Licensee,

are paid into and held and maintained in a Secure Account (but without prejudice to the full and timely disbursement from that account of all monies that are properly payable by the Licensee).

27.14B For the purposes of paragraph 27.14A, a “**Secure Account**” is a bank account held within the European Economic Area in the name of the Licensee that:

- (a) is separate from any bank account or bank accounting arrangement, however described, that is held in the name of or is otherwise operated by or on behalf of any Affiliate or Related Undertaking of the Licensee; and
- (b) is so structured and controlled that the revenues accruing to it and any interest that is earned on them can only be used for the purposes of the Authorised Business of the Licensee as carried on under this Licence.

27.14C To the extent provided for in the SEC, the Licensee may direct SEC Parties to pay amounts due by way of certain Service Charges relating to the provision of Communications Hubs into a bank account held in the name of a person (other than the External Service Provider) engaged (indirectly pursuant to an External Service Provider Contract) in the business of financing those Communications Hubs. The Licensee must ensure that:

- (a) such bank account is one which bears a reasonable rate of interest, which is held within the European Economic Area, and which is exclusively used to receive payments of such amounts;
- (b) the payment of such amounts into such bank account is in settlement of the Licensee’s obligation under the External Service Provider Contract (or any direct agreement entered into by the Licensee in relation to the External

- Service Provider Contract) to pay an equivalent amount in respect of those Communications Hubs (unless returned under paragraph 27.14C(c));
- (c) any amounts paid by a SEC Party into such bank account in error are returned to that SEC Party as soon as reasonably practicable after the error is identified (together with any interest earned);
 - (d) an amount equal to the interest that accrues to such bank account (excluding that referred to in paragraph 27.14C(c)) is paid to the Licensee as soon as reasonably practicable after it so accrues;
 - (e) the only withdrawals made from such bank account are in the amounts the Licensee is due to pay under its obligations referred to in paragraph 27.14C(b) and are made when the Licensee is due to pay the same (or are otherwise made in compliance with the Licensee's obligations under paragraphs 27.14C(c), (d) or (f)); and
 - (f) once the Licensee has paid all of the amounts that it is (or will become) liable to pay under the External Service Provider Contract (or any direct agreement entered into by the Licensee in relation to the External Service Provider Contract) in respect of those Communications Hubs, an amount equal to the balance then held in the bank account is promptly paid to the Licensee.

27.14D The Licensee will:

- (a) keep records, in a form that may be readily inspected and analysed, of every financial transaction or financial event relating to the operation of the Secure Account or any bank account of the nature referred to in paragraph 27.14C; and
- (b) if the Authority so requests, provide the Authority with access to such records for inspection by it at any time.”

Condition 35

In Condition 35, replace the definition of “Regulated Revenue” with the following –

Regulated Revenue means in relation to each Regulatory Year the actual revenue, measured on an accruals basis:

(a) received by the Licensee through Service Charges that are levied in accordance with the provisions of Condition 18 (Charging Methodology for Services) and Condition 19 (Charging Statement for Services); or

(b) otherwise received by the Licensee in relation to the carrying on of the Mandatory Business,

after the deduction of value added tax (if any) and any other taxes based directly on the amount concerned. Paragraph (a) above shall be deemed to include any and all amounts paid by SEC Parties under the SEC to persons (other than the External Service Provider) engaged (indirectly pursuant to an External Service Provider Contract) in the business of financing Communications Hubs.

Schedule 5

In schedule 5, replace annex 1 with “not used”.

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URN 13D/327